Conference Report

October 2014

London Conference on Globalization and World Order

The London Conference 2014
Globalization and World Order

CHATHAM HOUSE
The Royal Institute of International Affairs

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The Royal Institute of International Affairs

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Charity Registration No. 208223

ISBN 978 1 78413 023 7

A catalogue record for this title is available from the British Library.

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Typeset by Soapbox, www.soapbox.co.uk

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Foreword

This report serves as a record of the inaugural London Conference on Globalization and World Order, convened by Chatham House on 2–3 June 2014 at Lancaster House in London.

The London Conference has three aims: to be comprehensive in debating how best to manage the profound economic and political rebalancing taking place across the world; to go behind the headlines and debate the trends underlying and connecting current events; and to build an international community of experts with a shared understanding of the major challenges accompanying globalization.

This inaugural conference was fortunate to draw together high-quality speakers for each session, who offered perspectives reflecting their geographic and sectoral diversity. It benefited enormously from the ideas for themes, speakers and participants suggested by its steering committee. The conference would not have been possible without the generous support of its two founding partners – Accenture and Chevron – and its supporting sponsors – Bloomberg and Rio Tinto – as well as the generous cooperation that we received from the Foreign & Commonwealth Office in hosting the event at the historic Lancaster House in St James's. And the quality of the debate, insights and ideas generated over the course of the conference was driven largely by the input from its 200 participants. Steering committee members, sponsors and participants are all listed in the next section, along with speakers' details and the conference programme.

The report itself opens with a short essay which explores one of the main conclusions of the conference: the loss of trust that appears to be permeating relationships between governments, and between governments and their citizens, as a result of the pressures they are all under from the process of globalization. This is followed by the key insights from each of the five main sessions of the conference on 3 June.

The final section brings together the five papers written by members of Chatham House's in-house research teams in advance of the conference in order to stimulate participants' thinking. Even following an eventful six months since these were written, their insights and proposals retain an important salience for the future.

I would like to thank the institute's Conferences and Events teams, as well as staff from the research departments, all of whom contributed to the success of the conference. I am especially grateful to Catherine O'Keeffe, Deputy Director for Events, and Laurel Louden, Events Manager, who helped develop and organize the inaugural London Conference.

We look forward to hosting the second London Conference on 1–2 June 2015.

Robin Niblett
Director

October 2014

I. The Conference

Programme
Lancaster House, London: Monday 2–Tuesday 3 June 2014

Monday 2 June

1900–2200

Pre-conference dinner and discussion | Current Political Crises and the Global Balance of Power

Panellists

Dr Bassma Kodmani Executive Director, Arab Reform Initiative

Orysia Lutsevych Research Fellow, Russia and Eurasia Programme, Chatham House

James Nixey Head, Russia and Eurasia Programme, Chatham House

Dr Surin Pitsuwan ASEAN Secretary-General (2008–12)

Tuesday 3 June 2014

Session One | Globalization and World Order: 1914 vs 2014

0900–1000

- What is different about globalization in 2014 compared with 1914?
- Is world order now influenced more by economic interdependence than by geopolitical competition and military power? Or is conflict as great a risk as ever?
- Is the rise of the middle class in the emerging economies the most significant global geo-economic shift of our time? How will it affect the global balance of political power?
- What steps can existing and emerging world powers take to focus on the pursuit of opportunities rather than on the defence of national interests?

Panellists

Alyson Bailes Adjunct Professor, University of Iceland

Harold James Professor of History, Princeton University

Ruan Zongze Vice President, China Institute of International Studies

Sam Walsh CEO, Rio Tinto

Moderator: **Robin Niblett** Director, Chatham House

Session Two | Globalization: Winners and Losers

1000–1115

- How can national social contracts be adapted to the changing international division of labour, evolving production networks and trade trends in the developed and emerging economies?
- How can the trade agenda be advanced to encourage well-functioning global markets that support prosperity and reduce inequality? Can regional trade blocs be leveraged to enhance this agenda?
- What could reduce the tension between transnational forces and national politics to help populations adapt to the forces of globalization? To what extent can migration provide a solution?
- How can the systems upon which economic integration relies – international transport, open digital communications, well-regulated financial markets and international law – be reinforced and guarded?

Panellists

Ziad Bahaa-Eldin Former Interim Deputy Prime Minister, Egypt

Obiageli Ezekwesili Senior Economic Adviser, Africa Economic Development Policy Initiative, Open Society Foundations

Leo Puri Managing Director, UTI Asset Management Co

Sir Michael Rake Chairman, BT Group

Moderator: **Jim O'Neill** Economist

Session Three | Power and Governance in the Digital Age

1145–1300

- Can the principle of open and equal access to the internet survive commercial and political pressures for control?
- How can governments shape their use of the internet to enhance good governance and citizenship?
- What is needed to ensure that innovation remains a defining feature of digital life in the face of increasing moves for control?
- What are the best governance models for the internet?

Panellists

Hu Yong Associate Professor, Peking University School of Journalism and Communication

Marietje Schaake Member of the European Parliament

Mark Spelman Managing Director, Accenture

Emily Taylor Emily Taylor Consultancy

Moderator: **Nik Gowing** Television Journalist

1300–1415
Lunch

Session Four | Resource Security and Geopolitics

1415–1530

- How can governments and companies best reduce counterproductive competition over access to critical resources?
- What is the right balance between government-led and market-driven solutions to current resource insecurity?
- What can be done to accelerate the global deployment of resource-efficient, clean technology and resource price reform?
- What forums could be created to act as a counterweight to resource nationalism, strengthen sustainable resource management and mitigate the global effects of their increased consumption? Who should take part in such forums?

Panellists

Suresh Prabhu Chairman, Council on Energy Environment and Water, India

Norbert Röttgen Chairman, Foreign Affairs Committee, German Bundestag

Dev Sanyal Executive Vice-President and Member of the Group Executive Committee, BP plc

Paul Stevens Distinguished Fellow, Chatham House

Moderator: **Bernice Lee** Director, Climate Change, World Economic Forum and Associate Fellow, Chatham House

1550–1630
In conversation with the Rt Hon William Hague, UK Foreign Secretary

Moderator: **Robin Niblett** Director, Chatham House

Session Five | What Now? First Steps Towards a Rebalanced World

1630–1745

- How might current multilateral structures such as the UN and the World Bank adapt to deal successfully with global challenges such as climate change, nuclear proliferation and international trade?
- What other structures could emerge to deal successfully with these challenges? How formal and all-inclusive do they need to be?
- To what extent will non-state actors become better able than states and international organizations to develop a new form of international collaboration? Will they need the legitimization of states to be effective?

Panellists

R Nicholas Burns Professor of International Relations, Harvard Kennedy School of Government

Jan Eliasson Deputy Secretary-General, United Nations

John Kufuor Former President, Ghana and UN Special Representative on Climate Change

Kevin Rudd Former Prime Minister, Australia

Moderator: **Ngaire Woods** Professor of Global Economic Governance Blavatnik School of Government, Oxford University

1745
Conference adjourns

1900
Gala dinner, British Museum

Steering Group Members

Rob Bailey
Acting Research Director, Energy, Environment and Resources, Chatham House

Shumeet Banerji
Non-executive Director, Hewlett-Packard; Chief Executive, Booz & Co (2008–12)

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Manager, International Relations, Chevron

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The Sultan of Oman Professor of International Relations, Harvard Kennedy School; Under Secretary of State for Political Affairs, United States (2005–08)

Ambassador Barry Desker
Dean, S Rajaratnam School of International Studies; non-resident Ambassador to the Vatican (Singapore)

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Vice Chairman, Deutsche Bank; Secretary of State, Federal Ministry of Finance, Germany (1999–2005)

Baron Jay of Ewelme GCMG
Crossbench member, House of Lords, UK; Permanent Under-Secretary of State for Foreign Affairs (2002–06)

Ambassador Jean-David Levitte
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Head, External Relations, Bloomberg

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Director, Chatham House

Ambassador Andres Rozental
President, Rozental y Asociados; Mexican Ambassador to the United Kingdom (1995–97)

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II. Key Conclusions

International Order in 2014: A Loss of Trust
Robin Niblett

Introduction

The inaugural London Conference hosted by Chatham House on 2–3 June 2014 brought together thinkers, government officials and leaders from the public, private and civil society sectors from across the world to debate a question that finds little space at this moment of intense volatility in international affairs: what are the interconnections between the ongoing process of globalization and the status of world order?

The answer that emerged over the course of the conference was clear and worrying. Globalization has helped raise hundreds of millions out of poverty. But it is also forcing states and people to integrate faster economically than their diverse and sometimes clashing interests and values can adapt to politically, socially and institutionally. As a result, levels of trust between nations and governments, and between governments and their citizens, are fraying at an alarming rate.

This essay addresses three sets of challenges that the erosion of trust poses for international security and prosperity. It is followed by a synopsis of some of the key points that were raised during the London Conference, including steps that all of the constituencies represented at the event might pursue in order to ensure that the order upon which peace and welfare depends might be strengthened rather than weakened.

Trust between the world's major powers

The rebalancing of global economic and political power between states that has been taking place for the past decade as a result of globalization poses some of the most pressing challenges to international order. As is often noted, the international economic integration that accompanies globalization is enabling countries around the world to return to a more normal correlation between their demographic size and gross economic wealth. While this offers new opportunities for high-population countries such as China (1.35 billion), India (1.2 billion), Indonesia (250 million) or Brazil (200 million), for which population size was previously a source of economic fragility, the implications are far more mixed for countries with declining or static populations, such as Japan (120 million, but now declining rapidly), Russia (recently declining, but now holding steady at some 144 million) and much of Europe.

Russia's ability to keep exerting international influence relies ever more heavily on its status as a nuclear-armed, permanent, veto-holding member of the UN Security Council; on its ability to manipulate its prodigious resource reserves for political and economic ends; and on sustaining an activist foreign and security policy. President Vladimir Putin appears to fear that if Russia allows the forces of globalization to open up its economy, and if it becomes an open, pluralistic democracy, it will not be able to preserve its great-power status. It would risk becoming a Brazil or Indonesia of the northern hemisphere: regionally significant, but with diminishing control over its domestic and international destiny.

For their part, China's leaders do not trust that the United States will stand idly by while their country's regional political power and international economic influence rise in correlation with its economic size. They demonstrate a persistent fear that the United States is seeking to contain the rise of China, whether by the announced diplomatic and military 'rebalancing' of US power to the Asia-Pacific region or by the economic and technological protectionist measures that seek to exclude many Chinese companies from investing in US markets. Some in China also accuse the United States of seeking to undermine the rule of the Communist Party.

Meanwhile, China's neighbours, all of which have benefited economically from its economic renaissance over the past 20 years, now fear that the government in Beijing wants to extend its control regionally by asserting its historical claims to contested maritime and island interests throughout the South China and East China Seas.

But it is not just the rising powers that do not trust the emerging political order. The same can be said of those countries that are likely to have to relinquish political and economic power in relative terms. European states, the United States, Canada, Australia and, more recently, Japan have been at the top of the pyramid of international order that has been in place since 1945. They do not trust the rising powers to uphold the rules and values upon which the West built its political and economic dominance. Widespread use of cyber espionage, the stealing of intellectual property by Chinese state agencies and private actors, the use of state subsidies and the perceived political motivations of state-owned businesses all raise the fear that Western countries will find it ever harder to prosper in an open, globalized world than they have done in the recent past.

Trust within institutions

The inability of governments to overcome the deficit of mutual trust is affecting their ability to cooperate at an institutional level in order to adapt to the demands and realities of globalization. Numerous initiatives that would otherwise have improved the welfare and security of all countries are stalled.

One of the most glaring examples has been the failure by major governments for the past 20 years to agree on any binding limits on carbon emissions to tackle the escalating dangers from climate change. In a world of global economic competition, the fear of a near-term loss of relative economic advantage outweighs the long-term shared benefits of striking a meaningful agreement. Similarly, as deepening economic integration has increased demand for additional multilateral market-opening measures, rising powers have gained the self-confidence to challenge the US–EU condominium on trade negotiations. As a result, the World Trade Organization (WTO) is in stalemate.

Part of the problem is that rising powers bring an especially sovereign approach to international institutions. Having seen how Western states gained their economic advantage during a period when they had the power to write the rules of globalization in ways that suited their economic interests, rising powers now insist on single-mindedly pursuing their self-interest in multilateral negotiations. India's blocking of the WTO Bali agreement on trade facilitation measures is the latest case in point. Rising powers have also been particularly vociferous in blocking proposals, generally by EU members that are more comfortable with this approach, to enable international institutions to move beyond consensus-based decision-making and adopt a more supranational approach.

In a similar vein, rising powers want to bring state control into hitherto more fluid institutional arrangements, such as those governing the working of the internet, which have been led to date by private actors. Given the predominance of US and European companies in this field, a number of states now argue that only state involvement, via the UN's International Telecommunications Union, can guarantee a level playing-field for non-Western interests in the governance of the internet.

The response of the United States and Europe has been to launch market-opening negotiations between themselves and with their allies, such as the Transatlantic Trade and Investment Partnership (TTIP) and Trans-Pacific Partnership (TPP), before their impact can be negated by competing initiatives from the rising powers. Whether these initiatives will be inclusive or exclusionary remains to be seen.

Trust between governments and citizens

The way in which globalization is exacerbating the lack of trust in international relations is mirrored by the inner workings of states and societies.

In the West, the financial crisis of 2008 and ensuing economic contraction revealed the extent to which governments had lost control of their national economic destinies and lay at the mercy of the forces of globalization. The result has not just been voters punishing governments, but also the rise across the West of populist parties which reject the view that open economies and societies automatically benefit the population at large. Their perception is that only those elite segments of societies able to tap into the global economy – especially those working in the financial sector – benefit from globalization.

Multinational companies, which have served as the epitome of globalization, are no longer trusted to deliver improved social welfare. Popular anger with the off-shoring of lucrative jobs to the cheapest location has been compounded by the ability of nominally national companies to minimize their tax burdens by shopping for the most favourable tax jurisdictions.

For their part, corporate leaders are frustrated that governments are unable to design and adapt national regulations fast enough to sustain a competitive domestic business environment in a globalized market. At the same time, Western technology companies have lost trust in governments whose agencies appear to have taken advantage of the companies' globalized business models in order to develop surveillance techniques that have sometimes gone beyond the agreed judicial structures.

This is by no means a challenge only for the West. Popular protests in Brazil and China are driven in part by the sense that the rewards of impressive gross economic growth rates are not percolating through to all segments of society. And the disintegration of state structures in parts of the Middle East and Africa is driven not just by ethnic and sectarian conflict and environmental stress, but also by the sense that these structures have proved incapable of providing pathways to economic opportunity and personal fulfilment at a time when globalization offers such opportunities in so many other parts of the world.

Conclusion

Today's principal challenges to international order – Russia's revisionist approach to its place in the world, China's reassertion of its historical interests in the Asia-Pacific region, the collapse of states and rise of sectarian and other conflicts across the Middle East, and the inability of the United States and its allies to manage the resultant instability effectively – emanate not just from local, short-term concerns and the tactical responses of leaders, but also from the ways in which the ongoing process of globalization is eroding trust between governments, nations and societies. Considering practical ways to overcome the trust deficit at each of these levels will form one of the central themes of next year's London Conference

Key Points of Discussion

Session One | Globalization and World Order: 1914 vs 2014

The global reorientation from West to East is real and significant. The rise of China, other emerging economies and the developing world, whether steady or volatile, will be a central dynamic of 21st-century international affairs.

There are a number of differences between 1914 and 2014. International economic integration is deeper now, principally as a result of cross-border investments, capital flows, the internet and corporate supply chains. Levels of interdependence are therefore greater.

But not all differences between 1914 and 2014 are a source of comfort. Although the prevailing wisdom is that economic integration promotes international cooperation and stability, it is also the case that a diverse range of threats, from natural disasters to economic crises, can have much wider effects today than they would have had a century ago.

There are also important parallels between 1914 and 2014. The 'tectonic shift' in international affairs caused by the re-emergence of India and China bears comparison with the dislocating effects caused by the rise of Germany and Japan a century ago. As in 1914, today's interconnectedness also risks generating a false feeling of security that could lead governments to test one another's limits with potentially dangerous consequences.

At the same time, current international institutions have not kept pace with economic integration. This positive legacy of the 20th century is a potential source of instability in the 21st.

There are two principal risks to the current world order:

It is increasingly fragile. International institutions have proved incapable of addressing major global challenges and are in need of reform. Even when the right policy responses are known, as global talks on climate change have shown, agreement on implementation has not been reached. Simultaneously, the international community has been unable to address specific problems such as Syria.

Its legitimacy is fading. Most institutions still reflect the post-Second World War settlement and have not kept pace with political, economic and demographic change. There is a need to integrate the rising powers into a reformed international architecture. Present initiatives such as the TTIP and TPP, for example, do not include the BRICS, while the West remains reluctant to reform economic institutions such as International Monetary Fund (IMF). The risk is that current institutional structures could become irrelevant if they continue to prove incapable of reform.

Are China and other emerging economies ready to help underwrite international rules? The West may be reluctant to forgo its present privileged status. But it is also not clear whether rising powers are interested in participating in rule-making beyond their narrow self-interest.

Should old institutions be reformed or entirely new structures created? Is it possible to integrate the rising powers into a liberal world order or will international affairs be structured increasingly around 19th-century concepts of great-power spheres of influence? The desire of the West to advance the former appears to be faltering in the face of the drift of the 'Rest' towards the latter.

Established powers gradually losing relative power in the international system are as likely as rising powers to bend or break international rules. China's government, meanwhile, may not think that the current order is perfect, but is likely to seek to participate in it rather than try to alter it radically.

Reform of international institutions is complicated by a growing sense of popular alienation in domestic politics, afflicting both the West and the Rest. Addressing popular grievances at the national level may be more important to the maintenance of world order at this time of intense economic and political transformation than the search for new international agreement.

Session Two | Globalization: Winners and Losers

Globalization has had varied and uneven effects and cannot be labelled simply as a positive or negative force. Although the real incomes of the majority of the world's population have increased, and the UN Millennium Goal of halving extreme poverty was reached five years ahead of time, the bottom 5% of the global income distribution has seen no increase in real incomes at all.

The continued presence of extreme inequality worldwide is a sign of the uneven effects of globalization. Extreme inequality has a damaging impact on growth, so it is in the interest of business and governments to reduce it. Inequality also has a negative knock-on effect on democracy and social cohesion.

The 'winners' and 'losers' of globalization are not constants. Shifts in global markets can have a particularly dramatic effect on emerging economies which are over-dependent for their welfare on single commodities or industries.

Increasing numbers of people are hostile to the concept and process of globalization. Despite evidence that most have benefited from global economic integration, there is a perception that international rules are bent in favour of the richest countries, companies and individuals. The lack of trust in governments and institutions responsible for managing the process is a major barrier to improving the image of globalization among populations across the world.

This mistrust has been exacerbated by a deterioration of national social contracts in many states following the global financial crisis. Revitalizing national social contracts is a critical prerequisite for future support for global economic integration.

Young people are generally positive about globalization and optimistic about their futures despite being among those who have benefited least from globalization. They are suffering the most through universally high levels of unemployment in developed and developing economies alike. Increased government and corporate investments in skills, training and technology so as to ensure the young have access to opportunities will be essential to sustaining their majority positive outlook.

The highest purpose of national governments is to focus on providing public goods – including access to health, education and basic security. This will enable their citizens to participate more successfully in a globalized economy. Well-developed physical infrastructure, a good education system and transparent, trustworthy institutions play a vital role in helping populations adapt to the forces of globalization.

On the other hand, protectionist policies, such as subsidies that protect populations from the impacts of globalization, can end up cutting people off from the opportunities it offers. At the domestic level, checks should focus more on providing social safety nets than creating barriers to international trade and investment. Business leaders can best play a positive role delivering widespread improvements in welfare in such a context.

Emerging countries that are most integrated into global trade have grown the quickest and have made the greatest progress in reducing domestic levels of inequality. However, in order to make globalization more inclusive, politicians and business leaders need to increase levels of economic transparency and support greater consistency worldwide on issues such as taxation, labour standards and environmental protection.

International institutions need to be more transparent and provide more effective checks and balances on the rougher edges of global capitalism.

Session Three | Power and Governance in the Digital Age

To a large extent, digital innovation is occurring faster than policy and governance are adapting. Many policy-makers do not fully grasp the impact that new technologies have on their ability to protect citizens from economic disruption or infringements of their individual rights; those that do often find themselves unable to bring about the necessary changes in policy.

The digital economy has brought uneven benefits. The growth of digital innovation in a particular sector can further concentrate corporate wealth and power. Women and those with low education levels are often disproportionately marginalized or unable to participate in the digital economy.

New digital technologies have the potential to empower individual citizens, but this does not always translate into real political influence. For example, social media activists in Egypt were too isolated following the overthrow of President Hosni Mubarak to be influential in the political process of helping transform the state. The Chinese government is adapting to new technologies and using them to sustain centralized political control while trying to make government more responsive to growing social grievances.

Citizens are more likely to distrust government surveillance than they are to be concerned about companies using their private information. This is despite the fact that private enterprises often have more interest in accessing and using citizens' private data than governments, which focus on security threats.

Citizens, governments and companies need to work together to build trust over the rules of internet use. Despite the challenges, some policy-makers have chosen to protect citizens from unregulated uses of the internet, whether by governments or private actors. Other governments are winning for now in their battle for control over internet freedom.

Global internet governance is necessary because national boundaries and controls have less relevance in a globalized digital world.

Agreeing principles for internet governance, access and behaviour will help to keep the internet from further fragmenting, as well as rebuilding trust between its users. Ideally, principles could include net neutrality (preventing the ability to pay for privileged access to the internet); freedom of expression; privacy protections; coordinated parameters and mechanisms for internet control and governance; and preserving the internet's economic value.

However, complacency that technology will somehow overcome government restrictions is preventing sufficient action to protect internet freedom. It is not predetermined that the internet will remain free or cost-neutral, and at present there are no internationally agreed principles for its governance. It will take deliberate and concerted effort, along with an increase in internet policy-making capacity, to establish such principles and implement them successfully.

US attempts to lead the cause of global internet freedom have been undermined by the Snowden revelations about US government surveillance operations. At present, Western governments still do not reveal enough about what kind of information they collect and retain. Greater transparency is needed.

Solutions for internet governance should avoid undermining the enormous economic value of the internet. Personal data sold for commercial use enable many basic services such as Google to be free. However, it is not clear whether the public is prepared to defend this principle. And governments are looking for new business models that will manage and utilize the increasing amounts of data they are making available. Principles for internet governance must therefore balance requirements for privacy, security and trust against the potentially transformative uses of digital technology and data in areas such as public health and agricultural productivity.

Companies face the challenge of complying with different ethical standards and regulatory environments depending on the local context. Sometimes organizations choose to adhere to local standards that contradict principles of freedom of expression or privacy to retain access to a market. Western policy-makers should support companies that are addressing the challenges of working in different regulatory environments or politically charged situations, for example in the cases of the Twitter ban in Turkey and the internet shutdown in Egypt during the 2011 uprising.

Governments will increasingly be held to higher standards in their provision of digital services, and can learn from private businesses how to engage better with citizens over digital platforms.

Session Four | Resource Security and Geopolitics

The conflict in Ukraine has put energy security firmly back on the geopolitical agenda, but this development needs to be seen in the context of persistent and deepening global energy interdependencies. All countries are dependent on global systems and supply chains for energy and other resources – and producer and consumer countries alike are vulnerable to potential shocks and price swings in shared global markets.

The technology revolutions in shale and renewables are redefining the geopolitical landscape for energy. The prospect of North American energy self-sufficiency has raised fears over economic competitiveness elsewhere. **Rapid cost reductions in and the mass deployment of renewable energy, however, may prove just as important in the medium term.**

Narratives about scarcity have been replaced by the perception of plenty, yet formidable constraints continue to hamper increases in resource production. Differences in resource ownership frameworks, the lack of a cluster of flexible smaller operators and the absence of economies of scale have, for example, made it difficult to replicate the US shale-gas revolution in other parts of the world.

There are growing concerns among investors and regulators about the systemic risks posed by large-scale investments in carbon-intensive energy sources. As the world intensifies efforts to reduce greenhouse gas emissions, the medium-term risks to carbon-intensive business models are not currently reflected in financial markets.

Oil prices have stabilized recently, but there are questions over how long this new equilibrium is likely to last. There is uncertainty about future demand in emerging economies. Many OPEC countries now face a dilemma: they require high oil prices to balance their budgets, but sustained high prices encourage the expansion of non-OPEC production and, eventually, the destruction of demand.This could lead to future price volatility, potentially undermining political stability in producer countries.

Governments must strike the difficult balance between long-term priorities and short-term pressures. Countries that rely on fossil fuels today face the challenge of incentivizing investment in low-carbon technologies for competitiveness tomorrow. For countries investing heavily in new technologies, the challenge is to remain economically competitive while delivering on the transition to a sustainable energy system. New types of horizontal and vertical partnerships will be vital to unlock investment in sustainable solutions, develop technology and enhance global energy governance.

Despite renewed urgency, it remains difficult to forge a single voice on energy policy among European governments. Variations in the domestic energy mix, energy sources and import dependence are among the factors that pull European governments in different directions. Overall, the EU depends on Russia for a quarter of its gas needs, but some central and east European countries are close to 100% dependent on Russia.

Dependence on fossil fuel imports is also a challenge for many emerging economies. India's coal imports have risen to 200 million tonnes per year, eroding its trade balance, increasing inflation and raising its subsidy bill. China remains highly dependent on oil imports.

A step-change in efficiency is needed to address climate change but will also contribute to energy security. China, for example, could avoid $130 billion of energy imports in 2035 through efficiency measures, according to the International Energy Agency. Globally, investments in efficiency need to quadruple, reaching $550 billion by 2035. Despite the short return on investments, the scale of the challenges will require new and innovative financing models. In Europe, completing the single market for electricity would result in savings of at least €27 billion each year for consumers through enhanced efficiencies.

Providing the poorest with access to modern energy services should remain a global priority. Worldwide there are 1.2 billion people without access to electricity, and 2.6 billion depending on traditional biomass for cooking. Rolling out cost-effective renewable energy could play a key role in providing energy access for economic and social development, but also contain the escalating fossil fuel import bills of many developing countries.

Taking action to tackle perverse fossil fuel subsidies remains critical. Globally, subsidies stand at about $544 billion. In producer states such as Iran, Saudi Arabia, Russia and Venezuela, subsidized domestic demand reduces export potential and incurs huge costs. For large developing countries, subsidies can be a significant drag on the economy.

Session Five | What Now? First Steps Towards a Rebalanced World

Although the great hopes for international cooperation that followed the end of the Cold War have been disappointed, cooperation through international organizations has a crucial role to play and has achieved some notable successes, for example in promoting development in Africa.

The UN remains the sole forum for global cooperation at the start of the 21st century, delivering concrete measures for international security and welfare. It provides food to 90 million people every day in 73 countries; vaccinates 58% of the world's children, saving 2.5 million lives per year; assists 36 million refugees; has 120,000 peacekeepers serving in 16 operations across the world; and is currently mobilizing $12.4 billion in humanitarian assistance to help people affected by emergencies.

However, the UN needs to undertake a programme of new initiatives lest it be bypassed by the profound changes debated earlier in the conference. For example, it needs to:

- Introduce successor goals to the Millennium Development Goals, containing solid commitments on poverty eradication and sustainability;
- Undertake targeted reforms of the UN Security Council, such as the French proposal to abolish the veto of permanent members where there is a risk of genocide or mass atrocities being perpetrated;
- Introduce a new programme, 'Rights Up Front', which will enable the UN to intervene early when human rights violations take place, given that these are often the precursors to conflict; and
- Strike a deal at the Paris Climate Change Conference in 2015. China's recalcitrance had contributed to the failure of the 2009 Climate Change Conference in Copenhagen, but its change of position now offers an opportunity to resuscitate American leadership on this topic, which remains also essential for progress.

A strong UN can play a crucial role in partnering with regional bodies, as it did in the collaboration between the UN, the African Union and the Economic Community of West African States (ECOWAS) in the peacekeeping missions in Côte d'Ivoire, Guinea-Bissau, Liberia and Sierra Leone. The UN played a crucial role by bringing in its own troops and encouraging the other institutions to play their part, while ECOWAS focused on mediating negotiations.

However, the principal challenges to international peace and prosperity appear to be emerging from the decisions being taken in the capitals of the world's major powers. The pressures of globalization are eroding levels of mutual trust and sharpening areas of disagreement.

President Vladimir Putin's determination to reassert Russia's national interests and regional influence, if necessary at the expense of the interests of its neighbours, feeds a zero-sum revisionist Russian posture which is manifested most explicitly in Russia's aggressive actions in Ukraine during 2014.

The role of China raises interesting parallels and differences with Russia. China is acting in a responsible manner on many issues, for example in its approach to

North Korea and the new willingness to engage on climate change. However, its recent actions in the South and East China Seas have unsettled China's neighbours and prompted them to engage American support in ways that may raise rather than diminish the risk of unplanned conflict.

The aftermath of the wars in Iraq and Afghanistan has imposed a premium in the US on the value of restraint. However, the results of US reluctance to intervene further in Iraq, or decisively in Syria, including the meteoric rise of ISIL, raise the question of whether President Barack Obama has pulled back too far on the throttle of American leadership.

The US leadership now faces a number of tests. These include: (1) containing Russian power in Europe, which requires a renewed US focus on NATO and motivating West European members to increase their contributions to shared security goals; (2) ensuring that China's rise remains peaceful, aided by strengthening America's network of allies in Asia; (3) preventing a further unravelling of security in the Middle East; and (4) tackling climate change, which requires the United States to stop dragging its feet and collaborate with other countries under the leadership of the UN.

The growing competition between the Unted States and China is the determining feature of the new world order. This competition will involve each side seeking to contain the other's power while trying to develop a better understanding of its motivations, interests and objectives. Europe will need to work out where it fits into this picture.

There is often a false dichotomy between national interests and institutional cooperation; what is crucial is that international institutions should be sufficiently well-ordered so as to achieve positive results, meaning that it is in the national interest of individual states to work within and through them.

However, international cooperation tends to work best in times of crisis. At the London G20 summit in April 2009, for instance, world leaders, staring into the abyss of the global financial crisis, were willing to compromise rather than coming to the table with a pre-prepared agenda. Since then, the G20 has failed to establish a robust system of international economic cooperation, including by turning itself into a shareholder committee of the IMF.

A growing risk to world order arises from the fissures opening up in the state system, with separatist movements gaining strength in Europe, Asia, the Middle East and Africa. For example, the UK referendum on Scottish independence could embolden independence movements across Europe at the precise time that Europe needs to come together to respond to a host of internal and external challenges. This will add to the constraints that disjointed democratic cycles of competitive elections already impose on European leaders.

Leadership is essential for global order – not so much in terms of individual capability and personality, but rather in terms of whether the right political systems and institutions are in place to enable the leaders the world has today to confront the shared challenges that they face.

III. Background Papers

1. Globalization and World Order: 1914 vs 2014

Summary

- The world in 2014 is undergoing a profound rebalancing of economic power and wealth. Not surprisingly, it is witnessing many of the same insecurities as it did 100 years ago. A critical difference from 1914, however, is the nature of today's economic globalization. Foreign investment and global supply chains are interconnecting governments and nations as much as markets.
- The structural vulnerabilities of today's rising powers are another major dissimilarity. For example, China and India have yet to overcome the looming middle-income trap. Existing powers are in turn holding on to much of their economic and political status – not least the United States with its abundant resource endowments.
- Totalitarian or populist ideologies have likewise not emerged as a dominant alternative to the existing order, while international treaties, organizations and alliances that provided much of the infrastructure of international security in the 20th century continue to operate at the start of the 21st.
- The risks to international order are real, however. Rising economic power has reawakened sovereign claims backed by large-scale military build-ups. Nationalism is a potent force around the world. It is also unclear whether the information and communications revolution will diffuse or sharpen the emotional drivers of conflict.
- Building a durable international order for a rebalanced world will not be easy. Western governments need to engage rising powers more as equal partners in institutions such as the International Monetary Fund and International Energy Agency. New regional agreements, such as the Trans-Pacific Partnership and Transatlantic Trade and Investment Partnership, should remain open to other countries willing to sign up to their rules.
- At the same time, Western states must continue investing in their own security if they are to thrive in what is still a highly competitive if increasingly interdependent world.

Introduction

The centenary of the outbreak of the First World War has inevitably emerged as a year to revisit the question of world order.[1] The rise of new powers, China in particular, together with the seeming decline of the world's leading power, the United States, carries echoes of the geopolitical transition that occurred at the outset of the 20th century: Britain beginning its relative decline; China the sick man of Asia; and Germany, Japan and the US on the rise. Whereas Europe was the centre of the First World War with East Asia as a side stage, East Asia is now the focus of concerns about an outbreak of inter-state conflict, as China's leaders seek to regain the country's position as regional hegemon. Europe, however, is still haunted by its past, with President Vladimir Putin seeking to reassert Russian influence westwards, much as Soviet leaders created the Soviet Union after 1918 in the chaos that followed the First World War.

Seen through the lens of hindsight, the world may be entering a period of serious insecurity, but using historical analogies is a risky business. It is not preordained that today's decision-makers will follow a course similar to that of their 20th-century counterparts. And the world in 2014 is very different from that in 1914, 1938 or 1954.

This paper looks first at the difference between the changing balance of economic power in 1914 and 2014. It explores the risks that this change poses to international order, and assesses the structural differences that separate the two eras. In the final section, it offers some thoughts on how leaders and societies can benefit from the lessons of the past in order to manage this period of geopolitical transition.

The changing balance of world power

The world is undergoing a profound rebalancing in terms of the relative weight key countries and regions carry in the global economy. In 2000 the US, Japan and EU accounted respectively for 31%, 14% and 26% of world GDP, while China and the Association of Southeast Asian Nations (ASEAN) and Latin America and the Caribbean accounted for 3.7%, 1.5% and 6.6%. Figures for share of world exports were similar. In contrast, by 2018 the US, Japan and EU will

[1] Margaret MacMillan, '1914 and 2014: Should We be Worried?', and Harold James, 'Cosmos, Chaos: Finance, Power and Conflict', *International Affairs,* January 2014; Richard Evans, 'What can 1914 tell us about 2014? The disturbing parallels between pre-World War I and today', *New Statesman*, January 2014; Niall Ferguson, 'Why Obama must stop history repeating itself', *The Sunday Times*, 23 February 2014.

shrink to 21.6%, 6% and 20% of world GDP, while China, ASEAN and Latin America will grow to 15.3%, 3.3% and 8.3% respectively.[2]

Globalization – the opening of national markets to trade, international capital and foreign investment, and the resultant global flows of technology – has been the engine of this economic rebalancing. Globalization is re-establishing the connection between the size of a country's population and the size of its GDP across large swathes of the world, potentially leading to the recovery by China and India of the relative shares of world economic output that they enjoyed for hundreds of years until the mid-19th century.

Globalization means countries are interconnected to an extent never before experienced. The idea that the globalization of 2014 resembles that of 1914 is misleading. World trade as a percentage of world GDP in 2010, at 27.7%,[3] was indeed similar to its level in 1914, when it stood at 21%. But in 1914 the terms of trade were fundamentally different. Britain, France, the Netherlands and others used their industrial 'first-mover' advantage to create empires and dominate markets, ensuring they remained at the top of the wealth pyramid. Trade and mercantilism went hand in hand.[4] Now, companies from Britain, the US, Japan and elsewhere have invested across the world to create complex global supply chains, taking advantage of wage differentials, proximity to markets and resource considerations to make their operations truly international. The value of sales by US and European subsidiaries in their respective markets is five times greater than the value of transatlantic trade. The drive by Germany and Japan in the first half of the 20th century to create captive markets in their neighbourhoods, in an attempt to match the economic advantages Britain and France enjoyed through their empires, bears no meaning for rising powers such as China, Brazil or India.

In addition, the globalization of the last 30 years has had a dramatic impact on the wealth of individuals in those economies that have opened up to its effects: GDP per capita in China grew from $314 in 1990 to $6,091 in 2012,[5] while in sub-Saharan Africa GDP per capita grew from $627 in 2004 to $1,349 in 2012.[6] Multinational companies from emerging economies are now among the biggest in the world, trading and investing not only with developed economies in the West but, increasingly, also across the South. For example, a quarter of world merchandise exports in 2012 comprised exports among developing countries – so-called 'South-South' trade.[7] And the world's new economic powers are using sovereign wealth funds to invest their countries' recent gains into those regions and sectors that offer the best returns globally. These aspects of 21st-century economic globalization create new opportunities but also new constraints on governments, which need to maintain their international connectivity to continue delivering the rates of economic growth their citizens expect.

Globalization is a brutal process. Societies accustomed to being at the top of the pyramid are being forced to make harsh structural adjustments.

Two other related factors reveal the dissimilarity between 2014 and 1914: the vulnerability of today's rising powers, which must overcome the middle-income trap if they are to convert industrialization into sustainable welfare domestically and influence internationally; and the seeming resilience of existing powers, such as the US and Germany, where both corporate and social organization (as well as abundant resource endowments in the US case) appear to make up for apparent weaknesses in domestic governance.

Risks to international order

Does this global hyper-interdependence of countries and societies mean the end of large-scale conflict of the sort the world witnessed 100 years ago and 60 years ago? Globalization is a brutal process. Societies accustomed to being at the top of the pyramid are being forced to make harsh structural adjustments. The longer the delay, the more brutal the adjustment – as southern countries in the EU have discovered. This has led to popular frustration, demands for economic protection and the rise of populist parties and sentiment more broadly in the US, Europe, Japan and Russia.

It does not appear that this adjustment will trigger a new rise of totalitarian ideologies. Despite their frustrations, most European voters continue to focus on which parties will offer the most effective national governance. Emerging powers appear to face the same constraint. China's focus on disciplined if authoritarian economic governance has propelled its growth ahead of that of India. Chile and Brazil have demonstrated the benefits of relatively open markets,

[2] Figures derived from IMF World Economic Outlook database, GDP (current US$).
[3] Ratio of world exports of merchandize and commercial services to world GDP in current US$ values. Figure from WTO report, *Trade Developments in 2012 and Early 2013,* http://www.wto.org/english/res_e/booksp_e/wtr13-1_e.pdf.
[4] Richard Baldwin and Philippe Martin, 'Two Waves of Globalization: Superficial Similarities, Fundamental Differences', NBER Working Paper, January 1999.
[5] Francis Fukuyama, 'The middle class revolution', *Wall Street Journal*, June 2013.
[6] In current US dollars. Figure from WTO data bank, GDP per capita (current US$).
[7] *UNCTAD Handbook of Statistics*, 2013.

in contrast to Venezuela and Cuba. And whereas Poland's GDP per head has quadrupled in the past 20 years, Ukraine's has barely changed.

Instead, 21st century interdependence creates its own vulnerabilities. First, interdependence to some can mean dependence to others. Japanese leaders highlight the illogic of rising tensions with China by pointing to the extensive investments they have made in China and the growth in bilateral trade. From a Chinese perspective, however, Japan – with its weakening domestic drivers of growth – has made itself dependent on China and potentially open to economic coercion. In a similar vein, President Vladimir Putin hopes that European dependence on Russian oil and gas will outweigh Russia's dependence on the income from its sales of both, allowing Russia to subjugate Ukraine.

Second, the growth being delivered by globalization is awakening the sovereign aspirations of formerly weak powers. Rather than integrating into mutually supportive structures of the sort developed by EU members over the past 55 years, emerging powers continue to prioritize promoting and defending their sovereign rights. This is manifested by the dramatic rise in global military spending, with China, India, Saudi Arabia and Russia spending an average extra US$22.5 billion over the past five years.[8]

The capacity to enforce or repel claims to contested resource-rich territories remains a core driver of military spending for governments concerned that they will not be able to sustain the economic growth their citizens expect without reliable access to natural resources at competitive prices. But pursuit of sovereign claims can also be promoted by powerful interest groups clustered around newly empowered military leaderships, growing indigenous defence sectors and supportive politicians.

Third, countries in relative decline, often as a result of their detachment from globalization, have less to lose from challenging the emerging order. From Russia and Pakistan to North Korea, decision-makers can interpret their position as 'outsiders' as giving them more rather than less strategic flexibility to pursue their own national interests relative to their neighbours.

Fourth, the persistent pull of history and emotion sharpens the risk of conflict. Nationalism remains a powerful force in international affairs. As countries regain influence or sense relative decline, unresolved aspects of national identity can surface. The propaganda used by Russian leaders over Crimea and Ukraine bears witness to the political power of revisionist narratives. The same dynamic is at play in East Asia, where Chinese leaders are using rising economic and military power to assert their claims to islands in the South and East China Seas that they believe were unjustly taken from them in the first half of the 20th century.

Managing risk and opportunity

Given the ongoing struggle between the integrating forces of 21st-century globalization and the persistent risks of 20th-century competition and conflict, what are some of the mediating forces that will influence future prospects for peace and security?

First, the world today remains connected by an institutional infrastructure that has no historical parallels. Institutions created in the 1940s and 1950s as an antidote to world-scale inter-state violence have demonstrated a remarkable resilience. The UN's Security Council, General Assembly and agencies from the International Court of Justice to the Human Rights Council expose the infractions of member states even if they are rarely able to sanction them effectively. Although the UN Security Council has done little to end some of the world's most persistent unresolved conflicts, it appears to serve as a brake on their potential escalation to outright conflict among its permanent members.

Second, the fact that we now live in a nuclear-armed world continues to serve as a restraint on major conflict, although it has not prevented intra-state conflict. To date, the Nuclear Non-Proliferation Treaty (NPT) and the International Atomic Energy Agency have been able to hold back the broader military nuclearization of the world that some had feared in the 1960s and 1970s, although there is a serious risk of nuclear break-outs in the Middle East and East Asia.

Third, Western nations have not forgotten the importance of deterrence and alliances. The US has sustained its military presence and treaty commitments from Europe to the Middle East and East Asia for 65 years. NATO still exists, despite predictions that it would collapse after the end of the Cold War and despite ambivalence among its members about its strategic purpose and the need to invest in strengthening its capabilities. And the European Union has continued to deepen the connections between its members, even after the global financial crisis. These institutions have provided an element of stability in international relations that was largely absent before the Second World War.

Other countries have sought to imitate aspects of the European model to gain similar economic and political benefits: ASEAN, the African Union, the Economic

[8] Military expenditure in constant (2011) US$ in 2008 and 2012, from SIPRI Military Expenditures Database. However, between 2008 and 2012, military expenditure as a share of GDP *decreased* in India (from 2.6% to 2.5%), *stagnated* in China (at 2.0%) and *increased* in Russia (from 3.7% to 4.4%) and Saudi Arabia (from 8.0% to 8.9%).

Community of West African States (ECOWAS), the Pacific Alliance and the Gulf Cooperation Council are unlikely ever to achieve the EU's level of integration, but they have each made smaller countries feel safer and imposed constraints upon the actions of larger ones, inside or outside these regional groupings.

Today, the creation of the G20 reflects a gradual rebalancing of world institutions away from Western dominance via the G7, while providing a new avenue for the G7 to promote its perspectives at a global level.

A fourth phenomenon that mitigates the rise of sovereign competition has been the emergence of politically influential non-state actors. Companies and individuals whose wealth is connected to global supply chains have interests that are increasingly detached from notions of 'national interest' (making targeted sanctions an important tool of 21st-century diplomacy). Cross-border civil society groups also challenge the interests of national governments or serve as partners in the delivery of international public goods (humanitarian crisis response and internet governance, for example) and local welfare (such as the provision of health care and environmental improvement).

On the other hand, while interdependent societies offer opportunities for wealth creation and broader prosperity, they are also more vulnerable to disruption from perennial risks such as natural disasters and pandemics, and new ones such as terrorist attacks, cyber warfare and climate change.

The big unresolved question for governments that need to cooperate in confronting these challenges is whether the increasing interconnectivity of individuals through the web and social media and the concurrent 'global political awakening' will act as an accelerant or a diffuser of nationalist sentiment in the 21st century.

Conclusions

The world order during the 21st century will be determined by whether governments and societies can find together a productive balance between the simultaneous increase in levels of state competition and transnational interdependence. They will have to do so without formal structures of global governance or the hegemonic leadership that the US provided across much of the Western world in the second half of the 20th century.

It will be important, therefore, to engage rising powers inside existing international institutions as equal partners. Some institutions and agreements, such as the UN Security Council and Non-Proliferation Treaty, are probably unreformable, given the vested interests of their privileged members. But others, such as the International Energy Agency, the World Bank and the IMF, can be reformed, with the G20 often playing an enabling role.

Western governments need to invest in the resources necessary to deter aggression and manage security threats, just as rising powers are doing.

In addition, groups of countries that share interests and are willing to act together can contribute to a thickening of the rules for international economic and, ultimately, political order. This is the driving philosophy behind the negotiation of the Trans-Pacific Partnership and the Transatlantic Trade and Investment Partnership. But their contribution to international order will depend on their openness to other countries joining in the future.

Nevertheless, given the changing balance of political power across the world and the risks this poses to international order, Western governments need to invest in the resources necessary to deter aggression and manage security threats, just as rising powers are doing. With confidence in their capabilities for mutual deterrence Western and emerging powers might find it easier to work together to confront global security threats that pose risks to the security and prosperity of all nations. Anti-piracy operations and joint responses to natural disasters have already offered some positive examples, but more ambitious international cooperation could be explored, from the governance of space to fighting organized crime, international terrorism and pandemics to promoting energy efficiency and collaborative standards for renewable energy.

The lessons of history must not be forgotten, but nor should they blind nations to the growing benefits from international cooperation in a more interdependent world.

2. Globalization: Winners and Losers

Summary

- The past two decades have seen a huge increase in global trade and wealth, a changing distribution of global GDP and a redrawing of the industrial landscape. China's rise is the defining economic feature of the age.
- It is difficult to measure the effects of globalization on inequality. In terms of individual incomes, the biggest 'winners' from globalization are the very wealthy – the 1% – and the emerging global middle class, based mainly in emerging economies.
- The biggest losers are the very poor and those between the 75% and the 90% percentile – spread between former communist states, Latin America and the poor in advanced economies – whose real incomes have not increased at all.
- Globalization poses challenges to traditional forms of political order. There is tension between global markets and the nation-states that are the regulators and legitimate political authorities over those markets.

Introduction

Few concepts in international affairs are used as frequently or as loosely as globalization. Martin Wolf has called it a 'hideous term of obscure meaning' and its use, perhaps because of its ambiguity, seems to be in decline.[9] Despite that, the term still serves as shorthand for a number of long-term trends in economics, technology and culture that have enhanced the interconnections between people, politics and production and reduced the importance of the boundaries between them.

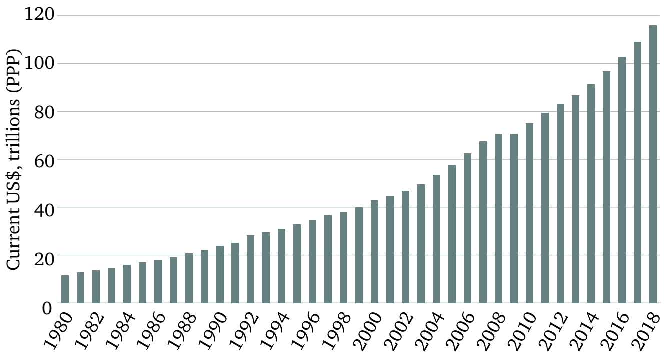
Global economic integration has had profound and varied effects on the economies of developed and developing states. Some of these effects are welcomed and some are resisted. This is perhaps the inevitable response to the contradictions created by the integrating global economy: greater overall wealth, but often greater societal inequality; economic growth but environmental degradation; cheaper products, but a race to the bottom on wages in certain sectors; a bulging middle class alongside stubborn poverty; a strengthening of the political legitimacy of authoritarian governments that use globalization to deliver higher rates of economic growth alongside the undermining of democracy in parts of the world where squeezed incomes are linked to a loss of national sovereignty.

This paper will briefly discuss the positive and negative effects of globalization. It will conclude with a synopsis of some of the issues that may shape the character of globalization over the coming decade.

Some characteristics of global economic integration

- *The past two decades have seen a huge increase in global wealth*. For example, gross world product has more than trebled between 1988 and 2008.

Figure 2.1: Gross world product 1980–2018

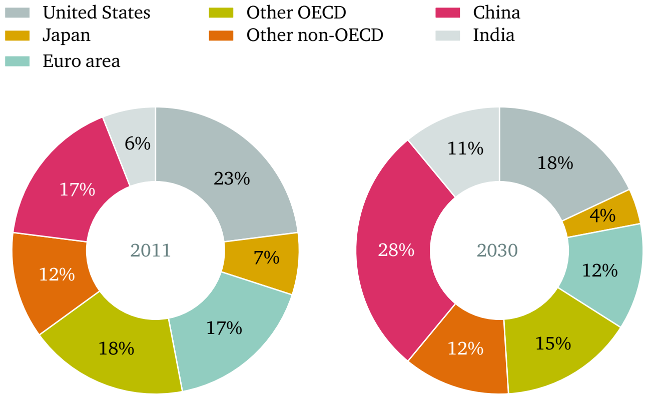


Source: IMF, 2014.
(2014–18 estimated)

- *Emerging economies account for an ever-growing share of world output.* The growth of emerging economies, in particular China and India, is radically changing the distribution of global economic power. By some projections the OECD countries may constitute a minority of the world economy by 2030.[10]
- *China's rise is the defining economic feature of the age.* China's economy grew from 5% of global GDP in 1978 to 17% in 2011,[11] and is set to become the world's largest at some point within the next 15 years.[12]

[9] Martin Wolf, *Why Globalization Works* (New Haven: Yale University Press, 2004), p. 13.
[10] OECD, *Looking to 2060: Long-term Global Growth Prospects* (Paris: OECD, 2012).
[11] Angus Maddison, 'Statistics on World Population, GDP and Per Capita GDP, 1–2008 AD', Groningen Growth and Development Centre, 2008.
[12] Estimates vary on the date at which China will overtake the US to become the world's largest economy. The Centre for Economics and Business Research estimates 2028. The US National Intelligence Council has forecast 2030 at the latest. *The Economist* has predicted 2019.

Figure 2.2: Projected change in share of global GDP, 2011–30



Source: OECD, 2012.

- *There has been a huge rise in global trade*. Despite the financial crisis, there has been an almost 50% increase in traded resources in the last decade. Rising prices for resources mean that the value of these trades has more than trebled in the same period.[13]
- *The industrial landscape has been redrawn*. Economic integration has accelerated changes in economic activity in the West. The service sector has grown to almost 80% of several major Western economies while industry has declined as a share of the economy across the OECD. In the UK, industry has declined from about half of the economy in the 1950s to about a fifth today.[14] Manufacturing accounts for about a tenth.[15]
- *Patterns of trade are changing*. 30% of global trade in resources, is now 'South-South', overtaking in 2010 the volume flowing South-North. Meanwhile, South-South trade in merchandise is almost on a par with North-North trade.[16] Major industrialized economies such as Australia, the United States and Canada are exporting large quantities of raw materials to emerging economies.
- *Supply chains are becoming global*. Trade in intermediate products is estimated to constitute 56% of total trade in goods and 73% of total trade in services. Most of what is traded is used to produce other things, rather than for consumption.[17]

Globalization and inequality

Advocates of globalization say it produces a rising economic tide that lifts all boats, and that consumers have benefited from falling prices. Critics say it increases inequality and serves the wealthiest at the expense of the poor.

It is difficult to measure inequality internationally or to determine the extent to which economic globalization is responsible. An IMF study suggested that clear recent rises in inequality within states were driven more by changes in technology than by global economic integration. It also concluded that different aspects of economic integration have contradictory effects on inequality: trade liberalization tends to equalize, while financial globalization and foreign direct investment (FDI) flows in particular tend to have the opposite effect. The effects also varied between countries.[18]

In a recent study on global inequality, the World Bank showed that different measures of inequality tend to lead to different conclusions about globalization's distributional effects:

- Inequality between states measured by the Gini coefficient of average incomes increased steadily between 1980 and the 2000s before beginning to decline;
- Inequality between states adjusted for population size shows a marked decline in inequality, fuelled predominantly by high growth in populous China and India; and
- Global inequality based on individual incomes rather than state averages is persistently high, but appears to be on a slightly downward trend, decreasing by 1.4 Gini points between 2002 and 2008.[19]

Efforts to measure the effects of the last two decades of global economic integration on global income distribution show the remarkably uneven effects of globalization:

- The biggest 'winners' were the very wealthy – the top 1% of the global income distribution – and the middle classes of emerging economies; the 50th and 60th percentile of global income distribution saw the biggest rise of all (almost 80%).

[13] Giovanni Grevi, Daniel Keohane, Bernice Lee and Patricia Lewis, *Empowering Europe's Future: Governance, Power and Options for the EU in a Changing World* (Brussels: Chatham House/FRIDE, 2013), p. 25.
[14] Bart van Ark, 'Sectoral Growth Accounting and Structural Change in Post-war Europe', Research Memorandum GD-23 (December 1995); World Bank, World Development Indicators, 2014.
[15] 'Manufacturing', House of Commons Library, Standard Note SN/EP/1942, January 2014.
[16] Grevi et al., *Empowering Europe's Future*.
[17] S. Miroudot, R. Lanz and A. Ragoussis (2009), *Trade in Intermediate Goods and Services*, OECD Trade Policy Papers, No. 93, OECD Publishing.
[18] *World Economic Outlook: Globalization and Inequality* (Washington, DC: International Monetary Fund, October 2007), Chapter 4.
[19] Branko Milanovic, 'Global Income Inequality by the Numbers: In History and Now – an Overview', Policy Research Working Paper No. WPS 6259 (Washington DC: World Bank, 2012).

- The biggest losers were the very poor (bottom 5%) and those between the 75th and 90th percentile – spread between former communist states, Latin America and the poor in advanced economies, whose real incomes did not increase at all, and in some cases actually shrank.
- However, with the exception of these two groups, there was a general increase in the real incomes of the majority of the world's population, including the poorest third of the world's population (above the bottom 5%).[20]

Figure 2.3: Change in real income between 1988 and 2008 at various percentiles of global income distribution (in 2005 international dollars)

Source: World Bank, 2012.

In short, although globalization has benefited most individual incomes, the effects are uneven and many people have not benefited at all. This indicates a number of challenges:

- Support for aspects of globalization that reduce inequality might be undermined by perceptions that the process is unfair and disruptive.
- Growth of the services sector in developed economies in particular and, eventually, in the East and South, may lead to a structural divergence between the incomes of people in the tradeable and non-tradeable sectors. For example, the incomes of hairdressers or carpenters can be depressed by their limited pools of customers and the arrival of immigrants who will accept lower wages for these jobs. Meanwhile, the salaries of workers in the financial and legal sectors can benefit from high barriers to entry and global pools of customers.
- Improving education will be a key factor in enabling citizens to adjust to the un-equalizing aspects of global economic integration.
- Managing these uneven effects is difficult, partly because of the divide between national politics and international economics.

Globalization and the nation-state

A core feature of global economic integration is the tension between transnational economic forces and global markets, and the nation-states that are the principal regulators and legitimate political authorities over those markets. Critics argue that global economic forces constrain the ability of governments to tax, spend, regulate or run deficits as they would choose. Capital mobility and competition on tax rates pit countries against one another in a way that benefits companies more than individuals; the liberal goal to reduce barriers to trade and capital flows undermines the ability of states to regulate what happens on their own territory. Instead, interest groups capture the process of globalization.

The nation-state is hostage to the fluctuation of international markets and the constraints of international lenders, and exposed to the effects of environmental degradation and global warming.

Defenders of globalization say this tension is exaggerated. The state remains essential as the deliverer of the 'public goods' – such as security, the rule of law and social protection for the disadvantaged – that allow the benefits of global economic integration to be realized. Some have even argued that the constraints on states and the narrowing of pursuable fiscal and monetary policies serve the interests of citizens.[21] The technocrats' response is that well-run states have nothing to fear.

But the tension is real. Descriptions of the world as 'borderless' or 'flat' by so-called 'hyper-globalists'[22] may capture aspects of international economic integration, but they do not change the continuing fact that the state is the basic bloc of political organization. States function on the basis that their governments can control what happens within their borders. However, the nation-state is hostage to the fluctuation of international markets and the constraints of international lenders, and exposed

[20] Ibid.
[21] Wolf, *Why Globalization Works*, p. 276.
[22] Thomas Friedman, *The World is Flat: A Brief History of the Twenty-First Century* (New York: Farrar, Straus and Giroux, 2005); Keniche Ohmae, *The Next Global Stage: Challenges and Opportunities in Our Borderless World* (Philadelphia: Wharton School Publishing, 2005).

to the effects of environmental degradation and global warming. What is the basis of self-government if transnational forces cannot be controlled or regulated according to the preferences of citizens?

These issues pose a particular challenge for democratic governments, which can be held accountable for forces beyond their control. In contrast, many international institutions – including the IMF, WTO and World Bank or multinational corporations – have influence without democratic responsibility, control without accountability. The EU – the world's most advanced experiment in regional governance – has the most democratically developed institutions of any supranational body, yet suffers from persistent criticisms over its lack of democratic legitimacy.

There are challenges for non-democratic states too. In many emerging economies, rapid economic growth has legitimized governments. In China, for example, successful economic stewardship rather than a democratic mandate is the foundation of the Communist Party's legitimacy. But transnational forces also challenge authoritarian governments.

Demographics may accelerate the challenge of globalization to the nation-state. Social contracts in democratic states rest in part upon solidarity expressed through welfare provisions and redistributive taxation. Falling worker–dependency ratios, rising life expectancy and declining fertility rates may change the relationship between state and citizen, as states with dwindling resources struggle to provide for an ageing population.

Many states in East Asia and Eastern Europe are reaching the point where they no longer benefit from the demographic dividend and their age profile will inhibit growth. Rapidly ageing populations may hold back transitions in middle-income countries. Antipathy towards immigration may prevent demographic relief.

These challenges to the state have implications that may become more pronounced in future.

Policy proposals

The challenge for international policy-makers is to make globalization serve the interests of a clear majority of their citizens, if not all. If globalization continues its inexorable advance, the real challenge may be to create structures that incentivize international cooperation in economic management over competition. There are at least four areas where this will be important:

- **Advancing the global trade agenda.** Well-functioning markets can support prosperity and reduce inequality. Developed and emerging economies will need to work together. In the meantime, bilateral and regional trade agreements can reduce barriers to trade, but they also have distorting effects.[23]
- **Bridging between the national and international.** The tension between transnational forces and national politics does not have an obvious resolution. Mitigation is likely to come through international institutions becoming more representative of global economic changes; and through greater international cooperation in areas where it is currently underdeveloped, for example in the trade in resources. Institutionalized regional blocs may perhaps improve international cooperation.
- **Mitigate the effects of global ageing.** Global economic integration may alleviate some of its own worst effects through increased migration, outsourcing and productivity growth via international divisions of labour.[24] However, this process may be hamstrung politically by citizens putting societal preferences above national economic efficiency.
- **Managing systemic risks.** Growing interdependence has generated wealth but also enhanced global vulnerability to shocks, be they economic, political or natural. For globalization to be resilient, the systems upon which economic integration relies – international transport, open digital communications, well-regulated financial markets, and international law – must be reinforced and safeguarded. This will require greater cooperation between states, based on transparency and mutual responsibility.

[23] United Nations, *World Economic Situation and Prospects* (New York: UN, 2011).
[24] Richard Jackson, Neil Howe and Keisuke Nakashima, *Global Ageing and the Future of Emerging Markets* (Washington, DC: Center for Strategic and International Studies).

3. Power and Governance in the Digital Age

Summary

- Initially, new technologies tend to disrupt the status quo and threaten the establishment's hold on power. As these technologies mature, however, elites eventually learn how to harness them for their own gain. The question is whether the internet will follow this same pattern. The battle for control is currently under way.
- At present, internet governance follows a 'multi-stakeholder model' that involves input from a variety of interest groups. However, splits are emerging between states favouring 'national sovereignty models' (more state control over their populations' access to information) and states wanting to broaden the current multi-stakeholder model.
- Many developing countires have not yet determined which model of internet governance they prefer. Dialogue and debate with and within these countries will be essential if they are to support an open internet that will contribute to economic growth.
- Upholding 'net neutrality' – the principle that all internet traffic should be treated equally – can prevent large-scale corporations from gaining dominance over the internet. This will be vital to preserve innovation and prosperity – helping start-ups and entrepreneurs in poorer communities to compete with these larger companies.

Introduction

> Just as steel can be used to build hospitals or machine guns and nuclear energy can power a city or destroy it, modern information networks and the technologies they support can be harnessed for good or ill.[25]

The internet has already facilitated citizen economies, greater international understanding and democratic uprisings by making communication and the spread of information ubiquitous and economical around the globe. By 2020, 10 times as many devices will be connected to the 'internet of things' than at present, including the industrial internet, driving new levels of economic efficiency. However, the internet has also enabled terrorists to coordinate attacks with greater reach and efficacy, and authoritarian regimes to monitor and crack down on dissidents more effectively. Moreover, critical infrastructure is increasingly at risk from cyberattack, and in the future common household appliances such as refrigerators could potentially be weaponized.

Impact of the digital revolution on government, corporations and political power

Will the digital revolution break the hold of government and established bodies on political power, or are information societies likely to be easier to control? And what do these trends mean for the future of internet governance? In their initial stages, new technologies tend to disrupt the status quo and threaten the established hold on power. The invention of the printing press enabled reformers such as Martin Luther to spread their ideas more rapidly, effectively and affordably than ever before, thus giving impetus to the Reformation and breaking the omnipotence of the Roman Catholic Church. The mechanization of weaving and steel production likewise upended societies, and new technologies have had a significant impact on the conduct of war – and the survival of empires – throughout history.

Online discussions are far more challenging to the political hold on power in authoritarian states than they are in liberal democracies. If people have increased connectivity to the world beyond their borders – as in the case of East Germans, who had access to West German television – then they learn how other people live and think, and what other people have that they lack. Ideas can spread rapidly and people can connect and organize. The Arab uprisings showed how citizen activists made effective use of social media to coordinate, bringing down the governments of Tunisia, Egypt, Libya and Yemen in what have been called 'Twitter Revolutions'.

The equality of opportunity afforded by the internet has also enabled small start-up companies to compete successfully with corporate giants and is already beginning to lessen inequalities between the developed and developing world. New communication and information technologies have – at least at the outset – lowered costs and other barriers to entry, allowing more stakeholders to participate in governance and commerce.

[25] Speech by then US Secretary of State Hillary Clinton on 'Internet Freedoms' at the Newseum, Washington DC, 21 January 2010. Clinton described 'a new information curtain [that] is descending across much of the world'. See http://www.foreignpolicy.com/articles/2010/01/21/internet_freedom.

As a technology matures, however, the very elites whose existence it initially threatened learn how to harness and control it for their own gain. The cost savings and other benefits generated by digital technologies have created opportunities for all: from workers and nascent companies to governments and big business. Data gathering and mass surveillance by governments and commerce have entered a new era of unimagined opportunities, both for human development and for exploitation.

From the telephone to television,[26] the pattern for new communications technologies has been a progression from the promise of initial openness and innovation to domination by monopolies or cartels. Indeed, conglomerates have already tried to gain control of the internet. Several major internet service providers (ISPs) have suggested that websites and applications should have the option of paying for preferential (faster) delivery of their content. This has led to serious opposition from advocates of 'net neutrality' – the principle that all internet traffic should be treated equally – who fear that this will create a 'tiered' internet. It would also allow ISPs to discriminate against traffic from websites and applications that do not pay, which would make it harder for start-ups and entrepreneurs in poorer communities to compete with big business.

Another concern is the increase in 'tethered applications' that can only be modified by their original developers. These not only have the potential to stifle innovation but are also easier for governments to control.[27] The promise of open access for all has thus far been the aspirational hallmark of the web. Is the internet doomed to evolve into a closed cost-based system, or will innovation and the spread of new, disruptive technology ensure that it remains open, accessible and empowering for all?

The evidence is mixed when it comes to government censorship of the internet.[28] Shutting down connectivity may affect ordinary people who do not know their way around the barriers or are frightened to break the rules, but it will not stop disruptive activists: more likely it will spur them to further action. They will find ways to circumvent these obstacles and become adept at cyber subterfuge, as non-state armed groups have done. For example, during the 2010–11 Arab uprisings, the Egyptian regime shut down the internet for five days at the height of the protests in Tahrir Square, while in Libya Colonel Muammar Gaddafi ordered sites such as Facebook to be blocked. In response, Egyptian protesters used satellite technologies to access the web, and Libyan protesters turned to dating sites to communicate, arranging 'dates' and sharing passionate poems as coded language to coordinate the protests.

However, in other Arab countries the arrest – and alleged killing – of bloggers critical of the regimes has so far been effective in subduing protest. The government of President Bashar al-Assad in Syria is known as a 'tech-savvy foe' whose use of false Facebook login pages to steal the passwords of online dissidents allows it to monitor their activities closely.[29] It thus remains to be seen whether activists or governments will retain the technological advantage.

As regards liberal democratic regimes, the internet has facilitated 'open government' and made a number of political processes more accessible to citizens. Some politicians – such as Carl Bildt, the Swedish foreign minister, and Marietje Schaake, a Dutch member of the European Parliament, have made effective use of online tools such as Twitter to foster greater direct engagement with citizens. The internet has also encouraged participatory mechanisms such as e-petitions. This is likely to increase as younger generations of digital natives reach adulthood. On the more disruptive side of the ledger, this phenomenon is eroding the membership base of traditional political parties, as individuals engage politically issue by issue rather than by supporting multi-year party platforms.

Concerning individual behaviour, people do not suddenly become a new species when they go online: what they do in cyberspace is an extension of what they do in their physical lives. People lie in real life and deceive online. People cheat in real life and swindle online. People bully in real life and torment online. However, on the internet people may feel more anonymous and are thus readier to behave badly, not realizing that the web can also open up new opportunities for law enforcement to identify and punish criminal behaviour – and indeed recent arrests for racist abuse show the power and the pitfalls of social media. Although people may feel more empowered, they can also be more easily manipulated through targeted advertisements and fake identities. Whether it is a force for good or ill, what is clear is that the battle for control of the internet is fully under way.

Current challenges to internet governance

The internet is already fragmented, be it in terms of language, national firewalls or political censorship. And it is at risk of fragmenting further still. The debate over whether the functions of the Internet Corporation for Assigned

[26] Tim Wu, *The Master Switch: The Rise and Fall of Information Empires*, Atlantic Books, 2010.
[27] Jonathan Zittrain, *The Future of the Internet: And How to Stop It*, Penguin Books, 2008.
[28] Ronald Deibert, John Palfrey, Rafal Rohozinski and Jonathan Zittrain (eds), *Access Controlled: The Shaping of Power, Rights, and Rule in Cyberspace*, MIT Press, 2010.
[29] Evgeny Morozov, *The Net Delusion: How Not to Liberate the World*, Penguin Books, 2012.

Names and Numbers (ICANN) should be transferred to the International Telecommunication Union (ITU) is one example of discord. The current internet governance system is a 'multi-stakeholder model' in that it involves input from a variety of interest groups. It evolved organically and, owing to the primal role of the United States in developing the internet, the US retains considerable influence: ICANN, the body that currently manages IP addresses and the domain name system, is a private non-profit corporation that is based in California, is subject to Californian law and operates under a Memorandum of Understanding with the US Department of Commerce.[30]

Although the United States was for many years the country with the highest number of internet users, today almost half are in Asia and most future internet growth is forecast to take place in Africa and South America. There is therefore a need for what we might call a 'broadened multi-stakeholder model' – or a more inclusive model that features participation by an even larger (and ever-growing) number of stakeholders. US President Barack Obama has recently indicated a willingness to cede control over ICANN, but under what conditions this will occur remains to be seen.

The internet is already fragmented, be it in terms of language, national firewalls or political censorship. And it is at risk of fragmenting further still.

The attempt to shift ICANN governance to the ITU, the UN's specialized agency for information and communication technologies in Geneva,[31] has also revealed splits between states favouring 'national sovereignty models' of internet governance and those wanting to broaden the current multi-stakeholder model. The countries that have led the push for the shift to the ITU – notably Russia, China and several states in the Middle East – also tend to be ones that desire more state control over the internet and their populations' access to information. Because the UN is based on the principle of 'one state, one vote', critics of the proposed shift contend that if enough states wanted to curtail internet freedoms in the ITU, it could lead to a 'race to the bottom' – resulting in an internet that reduces access, constrains economic activity and disempowers people throughout the world.[32]

The way forward

Last century, Aldous Huxley recognized that technological progress was ushering in a period of profound societal change, and with outstanding prescience he envisioned two futures. *Brave New World*,[33] published in 1932, set out a post-industrial planet in which a unified World State maintains its hold over the population by promoting a culture of consumerism and hedonism supported through genetically engineered castes. Thirty years later, just before his death, in *Island*,[34] Huxley imagined a completely different world on the island of Pala, where the forces of technology could be harnessed to create an enlightened and open society.

What will the digital revolution mean for the non-fictional world of tomorrow? Shall we see a preponderance of authoritarian regimes? Or shall we witness a growth in democratic societies, where freedom of expression and economic empowerment are allowed to flourish? Much will depend on whether, over the next few years, we can reconcile the diverging attempts to control the soul of the internet and achieve consensus on a practical way forward for global internet governance.

A large number of actors – including liberal governments, authoritarian governments, individual citizens, political activists, small companies, established corporations and existing engineering bodies – all claim a stake in the governance of the internet. Can we reconcile the different global visions for the future of internet governance? And if we cannot, are we likely to witness the emergence of a set of competing internets and governance models?

Policy proposals

1. **Involve all stakeholders in the decision-making process.** An accessible, legitimate and inclusive mechanism for internet governance must take account of the needs and concerns of all stakeholders. The problem is that the costs and mechanics of engagement limit participation by those without corporate resources behind them, without corporate or national interests to advocate, and without English-language skills. At present, participation in ICANN working groups tends to comprise approximately 70% US representation, 20% EU delegates, and just 10% from other regions.

[30] For more details, see https://www.icann.org/.
[31] For more details, see http://www.itu.int/.
[32] Laura DeNardis, *The Global War for Internet Governance*, Yale University Press, 2014.
[33] Aldous Huxley, *Brave New World*, Everyman Classics, 2013.
[34] Aldous Huxley, *Island*, Vintage Classics, 2005.

Emerging economies – especially in Africa and South America – that are rapidly acquiring and adapting internet connectivity should also be part of the conversation. Many developing nations are 'swing states,' countries that have not yet determined whether they prefer the national sovereignty model or a broadened multi-stakeholder model – or a combination of both. Dialogue and debate with and within those countries will be essential if they are to support the sort of open internet that can contribute most effectively to future prosperity.

2. **Rebuild trust**. The revelations in 2013 by Edward Snowden, the US National Security Agency whistleblower, have opened up divisions between the United States and many of its long-term allies, who were not only shocked by the extent of US spying on their activities but also now perceive fundamental differences in their approaches to data and privacy protection and the oversight of intelligence activities. This loss of trust has cast doubt on the future of a reformed model of multi-stakeholder internet governance.

   Snowden's revelations have also had a detrimental impact on commerce, with countries increasingly concerned about buying IT equipment, including security products, from international companies for fear that it might contain the means for espionage. US citizens as much as those of other countries have lost trust in the internet because of fears that their data are being used by governments and commercial entities in ways they never agreed to and do not fully understand. President Obama's address on 17 January 2014 regarding the review of the US signals intelligence programmes is an important start,[35] but further confidence-building measures will be needed in order to restore faith in the efficacy of the current multi-stakeholder approach to internet governance. One positive step would be to increase international cooperative efforts to tackle cyber crime, which is also eroding trust in the internet and poses important risks to citizens and governments from all corners of the world.

3. **Uphold net neutrality principles**. By upholding the principles of net neutrality that have been at the core of the internet, big business can be prevented from gaining dominance over the internet, and the evolution towards a tiered system with privileged, gated communities only for the wealthy can be halted. This will be vital in order to preserve the innovation and prosperity that the internet has enabled.

4. **Improve accountability and transparency of institutions**. The way decisions about internet governance are made also needs to be more transparent and comprehensible. If governance of the internet is to remain within ICANN, the corporation could, for instance, open the meetings of its Governmental Advisory Committee to outside observers. Moreover, communications on internet governance from governments and commercial bodies need to be more intelligible to all stakeholders; too often they are written in acronym-riddled technical language that makes them inaccessible to those without an engineering background.

[35] See White House press site: http://www.whitehouse.gov/the-press-office/2014/01/17/fact-sheet-review-us-signals-intelligence.

4. Resource Security and Geopolitics

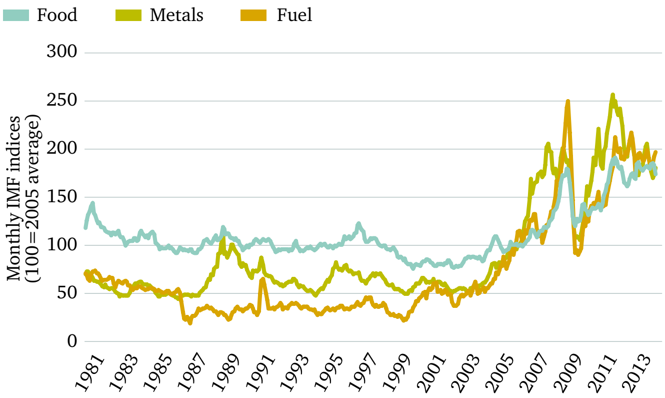
Summary

- Although resources remain abundant, resource security has risen up the agendas of governments and businesses following a prolonged period of high and volatile commodity prices.
- Underinvestment in extraction and infrastructure, and the migration of resource production to more challenging environments have contributed to higher prices and more sluggish supply, but the politicization of resources has been a key contributor to resource insecurity.
- Resources can act as a lightning rod for wider geopolitical tensions. Other issues include resource nationalism, the use of export controls and instability within key producing countries.
- The risks posed by politicization of resources are multiplied by a lack of international rules and institutions for resource governance, and by climate change which will become an increasing source of market instability and may contribute to heightened tensions over resources.
- Governments and businesses can reduce vulnerability through measures to enhance resource efficiency, increasing competitiveness and reducing pollution as they do so. Pricing resources appropriately – by removing subsidies and pricing-in environmental externalities such as greenhouse gas emissions – is central to driving efficiency gains and accelerating innovation.

Insecurity in a world of plenty

The spectre of resource insecurity has returned to haunt global commodity markets. Resource prices have increased (Figure 4.1) and the years 2005 to 2012 saw volatility reach unprecedented levels. Many countries have seen protests against rising food and fuel bills, while governments struggled to contain ballooning consumer subsidies.

Figure 4.1: International commodity prices (1980–2013)

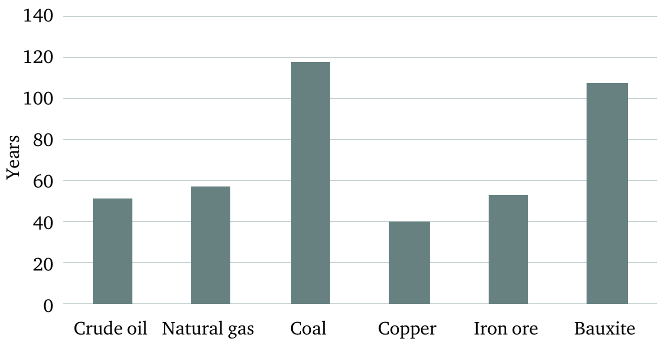


Source: Chatham House calculations based on IMF commodity price data.

Despite first appearances, this is not a neo-Malthusian scenario of resource exhaustion. Global agriculture produces more than enough food to feed a growing population.[36] Known resources of most fuels, metals and minerals have risen, not fallen, over the past decade. Even if no new reserves were added, at current consumption levels there are sufficient resources for 50 years or more (see Figure 4.2).

The case of shale gas shows how quickly resources can expand with innovation and investment. Worldwide, shale reserves have added an estimated 47% to total gas resources, since the US 'shale gas revolution' took off in 2007.[37] Many people now believe we have entered a 'golden age for gas'. Indeed, the real challenge presented to policy-makers by fossil energy resources is one of abundance. Estimates suggest that to keep global warming below 2 degrees Celsius – the internationally agreed target – most fossil reserves cannot continue to be burned unabatedly,[38] posing a major threat to the current models of coal, oil and gas producers.

Figure 4.2: Global reserve ranges for major fossil fuels and metals



Source: Chatham House calculations based on data from the US Geological Service and BP.

[36] Global agriculture in 2010 is estimated to have produced 5,359 kcal per person, more than double the 2,500 needed.
[37] Technically recoverable proved and unproved reserves. EIA (2013), www.eia.gov/analysis/studies/worldshalegas/.
[38] See LSE (2013), 'Unburnable Carbon 2013: Wasted Capital and Stranded Assets', Carbon Tracker and the Grantham Research Institute, LSE, www.lse.ac.uk/GranthamInstitute/publications/Policy/docs/PB-unburnable-carbon-2013-wasted-capital-stranded-assets.pdf.

Concern about the accessibility of resources, rather than physical scarcity, is the primary driver of resource insecurity. Resources may be abundant, but can they be delivered on time and at an affordable price? Underinvestment in extraction, processing and transport infrastructure and the migration of resource production to more challenging environments have contributed to higher prices and more sluggish supply. But access is increasingly a political question. A handful of countries supply international markets. Whether resources are delivered on time and at an affordable price is often a function of the domestic politics within these countries, and the geopolitics that shape their relations with the rest of the world.

Resource politics and trade

Resource politics in key exporters can have major implications for trade. During the 2007–08 global food price crisis more than 30 governments imposed agricultural export controls in attempts to contain domestic prices and placate restive populations. Rice markets almost dried up as big producers such as India, Pakistan and Vietnam stopped exporting.

In energy and metals markets industries may oppose exports in order to keep domestic prices down and boost competitiveness. For example, US manufacturers, benefiting from the low energy prices of the shale gas revolution, have recently opposed liquefied natural gas (LNG) exports.

Resource nationalism has increased, as producer countries have sought more control over their resources and a greater share of the economic rents. This trend is unlikely to lead to direct inter-state confrontation (such as happened during the 1956 Suez crisis), but it may erode trust between states and increase the possibility of reprisals.[39]

Domestic resource politics are rarely divorced from wider geopolitics. The US national debate about LNG exports has been heavily influenced by Russia's annexation of Crimea and its threat to stop gas supplies to Ukraine. With onward supplies to Europe implicitly threated, export proponents argue that American LNG could reduce European reliance on Russian gas.[40] Meanwhile, the resource implications of the Ukraine crisis continue to play out in Eurasia. EU discussions about future energy policy, which had emphasized competitiveness after the US shale revolution, now prioritize the development of alternative sources of energy. In response, Russia is looking to establish new markets for its gas, in particular in China, with which it is now close to agreeing a pipeline deal – after more than a decade of false starts.

Political unrest in producer regions can disrupt exports and destabilize international markets. As an extreme example, the collapse of Libya into civil war in 2011 saw international oil prices reach their highest levels since the 2008 spike. In general, resource production is migrating to countries with weak governance or unstable politics, or both; a significant proportion of the new reserves is in countries with low political stability, including 37% of oil, 19% of gas and 49% of copper.[41]

Tensions in the Middle East remain a particular concern. Some form of regional conflict could seriously curtail global oil production, but shipping routes are also highly insecure. Iran has occasionally threatened to close the Strait of Hormuz – the shipping artery through which about a third of global oil exports passes[42] – and in 2013, militants in Egypt attempted to close the Suez Canal by firing rocket-propelled grenades at a container ship in transit.[43] A strong US naval presence in the region has helped maintain maritime security, but since the White House failed to gain approval for military intervention in Syria in 2013 America's regional allies have been concerned that domestic support for its engagement may weaken, especially now US dependence on Middle Eastern oil is waning.

China, the world's largest importer of resources, also has a major stake in keeping sea lanes open and is rapidly developing its naval capacity in order to secure shipping routes in the South China Sea. This may lead to increased tension, with the Pacific's major naval power, the United States, currently 'pivoting' towards Asia. Yet secure maritime trade is a global benefit and should thus offer an opportunity for cooperation.

Despite the common interest in trade safety, the South China Sea remains a flashpoint for resource-related conflict. The seabed may be rich in oil and gas, contributing to competing claims over exclusive economic zones (the offshore area in which a country has exclusive resource rights) and territorial disputes over tiny islands with waters rich in fish and mineral deposits. Similar dynamics exist

[39] B. Lee et al. (2012), *Resources Futures*, Chatham House, http://www.chathamhouse.org/sites/default/files/public/Research/Energy,%20Environment%20and%20Development/1212r_resourcesfutures.pdf.
[40] The extent to which this would happen in practice is debatable. The EU would have to compete for shipments in a global marketplace, and US gas is likely to be more expensive than the Russian equivalent. Nor are exports likely to begin any time soon; the first LNG export terminal is not due to be completed until 2015.
[41] McKinsey Global Institute (2011), *Resource Revolution: Meeting the World's Energy, Materials, Food, and Water Needs*, p. 65, November, http://www.mckinsey.com/insights/energy_resources_materials/resource_revolution [accessed 13 February 2014].
[42] C. Emmerson and P. Stevens (2012), *Maritime Choke Points and the Global Energy System: Charting a Way Forward*, Chatham House Briefing Paper.
[43] R. Bailey (2013), *Edible Oil: Food Security in the Gulf*, Chatham House, http://www.chathamhouse.org/sites/default/files/public/Research/Energy,%20Environment%20and%20Development/bp1113edibleoil.pdf.

in the East China Sea and are also evident in the Arctic, although less sensitive relations among the Arctic states mean the risk of confrontation is lower.

Linkages between water and other resources

Linkages between resources complicate the challenge facing government and business; food and energy prices have become coupled as agriculture has become more dependent on fertilizers and as biofuel crops have become substitutes for petroleum. Water is often the common link and water scarcity the common vulnerability (Box 4.1).

Water resources that cross or straddle borders can provide a lightning rod for wider regional tensions, particularly where water demand is growing. Potential flashpoints include the Nile, the Euphrates, the Indus, the Ganges and the Mekong.

Box 4.1: The food–water–energy nexus in India

India's self-sufficiency target in food staples means feeding 17% of the world's population with 4% of its freshwater resources. Agriculture accounts for 90% of freshwater withdrawals, but collapsing water tables and increasing demand from urban and industrial users suggest this is not sustainable. Irrigation accounts for 40–60% of electricity use in key agricultural regions.

Meanwhile, power generation is expanding. Coal plants account for about 60% of Indian electricity supply and are water intensive – a 1,000 MW plant consumes enough water to irrigate 7,000 hectares. Hydropower provides most of the remainder, followed by gas and nuclear (both needing water for cooling).

These stresses came to a head in 2012 when 650 million people were left without electricity in the world's largest blackout. A weak monsoon led to an excessive pumping load for rice irrigation, hydro-power collapsed and a lack of cooling water forced thermal plants to close.

Climate change is a risk multiplier

Climate change multiplies the risks posed by politicization of resources. Tensions over freshwater resources may increase within and between countries as the risk of water scarcity increases. Wheat and maize yields are already thought to have been affected by climate change.[44] Extreme weather is becoming more common[45] and poses a major threat to food systems.[46] The 2010 Russian heat wave and the 2012 US drought provide a glimpse of the potential impacts on international food markets.

Targeted measures to protect vulnerable consumers and transparency within government contribute to legitimacy and increase the likelihood of acceptance.

Global trade and key production sites for fuels, metals and other resources may also be seriously affected.[47] The cost of flooding, for example, at 136 major port cities could increase from $6 billion in 2005 to $60 billion in 2050, owing to storms, rising sea levels and subsidence.[48] Extreme weather could lead to the breakdown of infrastructure networks, electricity networks and water supplies.[49]

Technology and resource efficiency

As the US shale revolution shows, technology has the potential to reduce dependency and disrupt resource geopolitics. But the hydraulic fracturing and horizontal drilling technologies behind the US shale revolution are the result of decades of support from successive federal governments as America sought to increase its energy independence. Solar photovoltaic is another technology that has benefited from strong and sustained government support. Its costs are falling precipitously, and solar energy is now at or approaching grid parity in many countries.[50]

[44] IPCC (2014), 'Working Group II on Impacts, Adaptation and Vulnerability, Fifth Assessment Report: Summary for Policymakers', Intergovernmental Panel on Climate Change, http://ipcc-wg2.gov/AR5/images/uploads/IPCC_WG2AR5_SPM_Approved.pdf.
[45] Many types of extreme events have become more common since 1950. In most regions both precipitation and heat events are likely to become more common than today in the 2046–81 time horizon, with an even clearer signal by 2100. See Intergovernmental Panel on Climate Change (IPCC) (2012), 'Summary for Policymakers', in C.B. Field, V. Barros, T.F. Stocker, D. Qin et al. (eds), *Managing the Risks of Extreme Events and Disasters to Advance Climate Change Adaptation* (Cambridge University Press), pp. 1–19 (future trends) and p. 111 (historical trends), http://www.ipcc-wg2.gov/SREX/images/uploads/SREX-All_FINAL.pdf. See also WMO (2014), 'WMO Statement on the Status of the Global Climate in 2013', World Meteorological Organisation.
[46] IPCC (2014).
[47] C. Paskal (2010), *Global Warring: How Environmental, Economic, and Political Crises will Redraw the World Map* (New York: Palgrave Macmillan).
[48] S. Hallegatte, C. Green, R.J. Nicholls and J. Corfee-Morlot (2013), 'Future Flood Losses in Major Coastal Cities', *Nature Climate Change* 3, pp. 802–06.
[49] IPCC (2014).
[50] R. Bailey and F. Preston (2014), *Stuck in Transition: Managing the Political Economy of Low-carbon Development*, Chatham House Briefing Paper, http://www.chathamhouse.org/sites/default/files/home/chatham/public_html/sites/default/files/20140200LowCarbonBaileyPreston.pdf.

Picking winners is, however, a risky endeavour for governments. Arguably the most useful thing they can do to spur innovation is to ensure resource prices reflect scarcity and environmental costs. This is rarely the case. Fossil fuel subsidies worldwide were estimated at $544 billion in 2012,[51] about six times the sum spent on renewable energy subsidies. Appropriate resource prices would also enable greater efficiency, reducing dependency on imports and increasing competitiveness. Implementing efficiency measures could reduce resource needs by 13–29% and save $2.9 trillion per year by 2030.[52]

Yet resource price reform is fraught with political risk, as governments have to overcome opposition from domestic industries and populations. Successful strategies are likely to entail campaigns to explain the benefits of reform, such as creating jobs, redirecting resources towards public services, tackling inequality (subsidies are usually regressive), or reducing pollution and waste. Targeted measures to protect vulnerable consumers and transparency within government contribute to legitimacy and increase the likelihood of acceptance.

Gaps in global governance

There is a lack of internationally accepted rules and institutions for resource governance. The International Energy Agency (IEA) is limited to industrialized energy consumers and excludes emerging consumers such as China and India, and major producers. The World Trade Organization effectively deals only with import restrictions, not export controls. Attempts at the G20 to agree a framework to define and phase out fossil fuel subsidies have met with little success. There are no international rules to prevent or limit export cartels, nor universally agreed frameworks for cooperation on 'transboundary' water. There is no regime governing maritime choke points and strategic sea lanes,[53] and no global deal to reduce greenhouse gas emissions – which remains one of the most urgent deficiencies, not least owing to the threat that climate change poses to resource security.

Policy proposals

Politicization of markets threatens resource security. Governments and businesses can reduce vulnerability by enhancing resource efficiency, which also improves competitiveness and lowers pollution. Pricing resources appropriately – by removing subsidies and pricing-in environmental costs such as greenhouse gas emissions – is central to driving efficiency gains and accelerating innovation.

Although issues such as trade, investment and resource governance are difficult to divorce from geopolitics, and the appetite for multilateralism remains low, a functioning global resource system represents a common good and governments should work to address gaps in international governance. Opportunities for progress include:

- New producer-consumer dialogues to address key governance gaps and resolve disputes. One option might be an informal 'Resources 30' or R30 club comprising the major producing, consuming, importing or exporting countries. Most ambitiously, this could provide a forum to depoliticize resource governance by removing discussions from wider geopolitics.
- Politically smart strategies for resource price reform that justify and explain the approach to key constituencies, ensure appropriate compensation for the vulnerable, and phase reforms over time. Competitiveness concerns may be partially offset by tackling reform in cooperation with regional neighbours or through international forums such as an R30.
- New models of trilateral international cooperation, to be developed with developing countries by donors and emerging economies to accelerate deployment of resource-efficient, clean technology. This could form a part of the post-2015 development agenda.

[51] It should be noted that the 'price gap' methodology used by the IEA to estimate subsidies to consumed products is controversial in some producer countries. See 'The Cost of Domestic Energy Prices to Saudi Arabia', *Energy Policy,* Vol. 31, No. 11, pp. 6900–05.
[52] This calculation is based on 2011 prices for natural resources and a 10% discount rate, compared with a 'business as usual' scenario. These savings could further increase significantly if water and carbon emissions were to be priced efficiently. See McKinsey Global Institute (2011).
[53] See, for example, Emmerson and Stevens (2012).

5. What Now? First Steps towards a Rebalanced World

Summary

- Many of the pillars of the 20th-century international order are struggling to meet the challenges of the 21st century, suffering from structural weaknesses such as unrepresentative membership, inflexible design and too great a focus on state actors.
- Some reform of existing international organizations may be possible, including pruning obsolete forums, but any genuine revival would require widespread recognition of the nature and urgency of international problems, supported by domestic political opinion. Structural reform of international organizations will follow rather than bring about such a consensus.
- Ad hoc groupings of states united by interest or region will operate as caucuses or advance guards within existing international structures. The role of large organizations will increasingly be to provide the institutional framework for such caucuses rather than to mobilize joint action by the full membership.
- Such ad hoc groupings may, however, lack the legitimacy of larger organizations, may not be as resilient in unexpected crises, and may undercut the ability of smaller and weaker nations to have their voices heard.
- States, and state-based organizations, will find it increasingly difficult to do more than merely respond to changes triggered by technological and commercial developments. A new form of hybrid international organization may become necessary, involving state governments, transnational corporations and civil society groups. In the long term, any joint effort to deal with global problems may be based more on informal networks within or across borders, may be issue-focused and may be more commercial, cultural or religious than governmental.

Criticisms and problems

Is the post-1945 multilateral order waxing or waning? Is the world returning to a disordered state of relatively unrestrained competition, or can some new configuration provide a more effective framework for cooperation?

Some pillars of the 20th-century order such as the United Nations, the Bretton Woods financial institutions and the World Trade Organization have struggled to meet the challenges of the 21st century. Critics complain of organizational inefficiency and policy failure, pointing (among other disappointments) to:

- A UN Security Council whose permanent members block joint action, overstep mandates or bypass the council when rulings do not suit their interests;
- A moribund international arms control regime, apparently unable to prevent proliferation or uphold commitment to disarm;
- A stuttering international trade round, largely driven by deals between small numbers of like-minded nations;
- Global environmental talks unable to agree a credible pathway to limiting climate change;
- The erosion of collective commitment in organizations such as NATO and the EU, with members taking differing positions on the organization's aims and demonstrating differing levels of commitment to its activities; and
- International regulation and policy lagging behind fast-moving developments with wide impact, especially in finance and information technology.

Not all such criticisms are justified. A mixed performance is often the most that can be expected from such complex organizations. Nor is cooperation outside the established institutional architecture necessarily a sign that the big organizations are doomed; they have never had a monopoly on international policy and have often worked intimately with national and multilateral efforts.

Moreover, some of the challenges such bodies now face are the direct product of their past successes; notably, recent global economic growth, which is in part the result of efforts by organizations such as the UN, NATO and the WTO to build a secure and free-trading world. Some organizations also continue to outperform national alternatives, especially where they are seen as a source of international legitimacy or a repository of neutral and authoritative technical expertise.

Nevertheless, many of the established international organizations suffer from some clear structural problems, which – taken together with their mixed performance record – suggest that something is wrong.

- Membership and institutional power seem not to reflect current international economic power (UN Security Council membership is the most prominent case).
- Many of the big organizations – the UN, the International Monetary Fund/International Bank for Reconstruction and Development, and NATO – were designed for a particular purpose and may now have lost that focus or be unable to adapt their structures and processes to new challenges.
- Organizations made up solely of national governments are poorly positioned to foresee and shape global changes driven by non-state actors, including large corporations and financial institutions, technology-enabled individuals and networks, and – an especially powerful mixture of the two – private organizations that can shape, adopt and exploit very rapid technological changes to profit from information flows.

Identifying the causes

Much of the debate about reforming or replacing international organizations focuses on structure. It seems right to tackle outstanding anomalies such as unrepresentative membership, and there is an obvious need in many cases to improve procedures, finance and internal management. But while such reforms may be necessary, they are not sufficient to ensure success. The key to real change lies not with the structure of international organizations but with their purpose – not with their hardware but with their software.

The future shape of 'global governance' will therefore depend on whether it is possible to build a new consensus and how far it would be shared.

The institutions of 'global governance' are not an independent structure distinct from states, and they cannot independently resolve or manage the problems of globalization. Despite their separate bureaucracies and the prestige that sometimes attaches to their institutional identities and leadership, they are groupings of national member states. This is sometimes forgotten in discussions about 'global governance' (a formulation that contributes to this confusion), which is surprising given the way national policies are so often to blame for the very inefficiencies and failures of these organizations.

It follows, therefore, that the key question is not whether organizations such as the UN Security Council can be reformed, but whether there is sufficient international agreement as to what the problems are, what needs to be done and what role any international organization might play. In many cases, the answer seems to be that there is not sufficient agreement.

From this perspective, the difficulties of the UN, WTO and the international financial institutions are not a cause of rising international uncertainty and disorder but a symptom of a much wider and more profound problem: a disturbing decline of consensus about what is going on in the world, and how to manage the problems that disagreement will bring.

Can the problem be fixed?

The future shape of 'global governance' will therefore depend on whether it is possible to build a new consensus and how far it would be shared. This is to a large extent a matter of national attitudes and politics, and any solution will have to be based as much on developments within states as between them.

In effect this means determining how far states are able domestically to recognize and support some of the principal elements that make cooperation through international organizations possible, such as the belief that:

- International arbitration or collective action is necessary to deal with international problems;
- International agreement may imply some limitation of national freedom of action;
- Compromise is necessary, both to achieve direct benefits in exchange and to keep the international process alive; and
- Member states must not only defend their narrow national interest but also engage actively with the agenda of the organization to support or enforce the collective interest.

Some prominent members of existing organizations have a mixed record in their support of such principles, at least in practice. In some important cases, the domestic political debate seems hostile or uninterested; these include the apparently increasing polarization and obstructionism of US national politics, the nationalist tone of much Chinese political rhetoric; the lack of strong and consistent international political engagement from some of the world's major emerging economic powers; apparently unresolvable tensions between some of the principal regional powers;

and questions as to whether middle-sized powers such as France and the United Kingdom have the appetite and resources to maintain their international engagement.

A further complicating factor is that the relationship is no longer solely between international organizations and their member states. It has now expanded to include individuals or groups whose interests are transnational – for example, reflecting religious, cultural, ethnic, economic or moral concerns – but who may not wish to be represented by their national governments or are actively hostile to the state. Civil society organizations are already taking part in international forums, notably on issues of human rights, the environment and arms control, but new communications technology is giving individuals the opportunity to organize and express themselves without formal or physical structures, and without engaging with established international organizations.

The transnational impacts of globalization and technological advances together make this expanding input an area of increasing interest. However, established international organizations lack both the experience and the flexible structures to engage seriously with this decentralized and inchoate form of opinion.

Possible first steps to a solution

International organizations are poorly placed to take the lead in reforming themselves, given their dependence on the authority and support of member states which are themselves the cause of some of the principal problems. It follows that nation-states will have the key role in any attempt at reform, involving national governments as well as the domestic political process that shapes and constrains them.

But although nation-states may be the principal actors in rebuilding the international structure, they are not well equipped for a more radical reshaping. Many of the greatest current and likely future challenges are attributable to non-state actors, or flow from the withdrawal of state power through deregulation or state failure. National governments are often unable or unwilling to roll back this loss of power, or to respond as fast as technology or commerce develops. International organizations based on states will continue to share these structural weaknesses.

The open question is whether non-state actors will become better able than states and international organizations to develop a new form of international collaboration, either by bypassing existing structures or by engaging with them. It is currently difficult to imagine any coherent and legitimate form of action based entirely on a virtual network of individuals operating without some form of structure and without an element of government support, for example to provide security or a legal framework.

A hybrid of current structures may be the most likely development, adapted to enable new forms of individual engagement. But in the long term it is possible that an entirely separate system of global cooperation may emerge, based on a community of interests unmediated by national governments, a network of organizations that are no longer ‘international’ but rather ‘intercommunity’ in character. In this context, the principal role of governments and state-led institutions will be to provide regulatory consistency and the essential public good of security.

To sum up, a number of observations can be made:

1. Established international institutions are likely to continue in formal existence, although perhaps through inertia rather than because they are widely seen as relevant. However, it may be time to start discussing whether, for example, all the UN bodies are still useful, and whether some could be abolished or combined. Radical pruning is unlikely to be possible, but the discussion might be useful as a way of restating and refocusing the agenda and checking the balance of resources across the various UN arms.
2. Any revival of large-membership international organizations would require widespread and concurrent international recognition of the nature and urgency of global problems; and any structural redesigning to boost their legitimacy and efficiency is more likely to be the result than the cause of such a new consensus. Such a revival would depend on changes in the domestic political debate in major countries such as the United States and China, to portray international engagement as a means for delivering national interest.
3. Established regional organizations might seem a more attractive option than larger international ones, as they have smaller membership and apparently greater identity of interest, but they are as likely as larger groupings to include a variety of agendas and competition between neighbours. Common geography does not necessarily signify common interest. Nevertheless, a less assertive US international position might mean that countries in, for instance, Europe or Latin America had to cooperate more closely with one another, particularly in areas such as security, where the US role has been dominant.

4. There will be an increase in the number of ad hoc groupings of states with similar interests, limited to specific issues or events. These may help build trust and habits of cooperation, but without an institutional structure they will not be resilient in the face of unexpected crises. They may explore ways to entrench cooperative relationships without institutions or fixed cycles of summits or meetings, for example by adopting joint regulatory or legal codes, or by pooling their state resources (such as elements of their armed forces).
5. Such ad hoc groupings may operate as caucuses within larger organizations, ready to move further than the membership as a whole through some form of 'enhanced cooperation'. The role of the larger organizations may increasingly be to provide the institutional framework for each caucus, rather than to mobilize joint action by the full membership. Organizations such as NATO could focus on providing a toolkit of regulations, resources and forums for members or groups of members to draw on as required.
6. Neither ad hoc interest-based groupings nor regional organizations could provide as strong a foundation of international legitimacy and law as the established large international organizations. Some alternative source of legitimacy might be necessary, for example through some new democratic mechanism for more directly consulting the citizens of the states involved, or some way of formally associating such ad hoc cooperation with the established structures, which is perhaps easier. The role of organizations such as the WTO or UN would then be to ratify agreements made elsewhere, rather than being the primary negotiating forums themselves.
7. Smaller and weaker nations would be particularly at risk if ad hoc interest-based organizations replace large international ones. Smaller nations are guaranteed a (limited) voice in existing international forums, but they would be at a disadvantage in a more competitive and uncertain environment. Although this might benefit larger states in the short term, it is likely to store up discontent and instability. Larger states have a long-term interest to find ways to enhance the voice of smaller states, including by supporting effective and well-resourced diplomatic services for them.
8. States and state-based organizations will increasingly struggle to do more than merely respond to changes triggered by technological and commercial developments. Attempts to shape or regulate such changes by states acting individually would be ineffective or economically disruptive. Some new form of international organization may become necessary, involving state governments and transnational corporations, and representing their voters and shareholders.
9. In the long term, therefore, any joint effort to deal with global problems may have to be based on more informal networks within or across borders, and may be issue-focused, commercial, cultural or religious in character rather than governmental. International businesses, cultural or sporting organizations and indeed religions may prove better able to influence the behaviour of the billions of individuals both empowered and threatened by globalization. An organization such as the International Olympic Committee may, despite the controversy surrounding it, offer a potentially useful model for such a mix of governmental, commercial and popular engagement.

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Charity Registration Number: 208223

ISBN 978-1-78413-023-7