Hybrid CoE Working Paper 16

Financial geopolitics and hybrid conflict: Strategic competition in a financialized world

Hybrid CoE

Elmar Hellendoorn – April 2022

Hybrid CoE Working Papers cover work in progress: they develop and share ideas on Hybrid CoE's ongoing research/workstrand themes or analyze actors, events or concepts that are relevant from the point of view of hybrid threats. They cover a wide range of topics related to the constantly evolving security environment.

This paper has been made possible by NLD MoD. The author takes full responsibility for the content of the paper, and the views expressed represent his personal views, not those of any of the organizations he has worked for or with.

The European Centre of Excellence for Countering Hybrid Threats
tel. +358 400 253800 | www.hybridcoe.fi

ISBN (web) 978-952-7472-24-8
ISBN (print) 978-952-7472-25-5
ISSN 2670-160X

April 2022

Cover photo: Kanyapak Lim / Shutterstock.com

Hybrid CoE's mission is to strengthen its Participating States' security by providing expertise and training for countering hybrid threats, and by enhancing EU-NATO cooperation in this respect. The Centre is an autonomous hub for practitioners and experts, located in Helsinki, Finland.

Contents

Preface

The Western use of financial sanctions against Russia in the wake of the Russo-Ukrainian War has alerted the wider public to the importance of finance in geopolitics. This Working Paper was written well before the outbreak of the Russo-Ukrainian War, and does not refer to the recent financial sanctions against Russia. The Western financial relationship with China has not – yet – fundamentally changed, however. The involvement of Western finance in China's financial markets remains of great geopolitical importance. Financial geopolitics is thus about more than sanctions. It is about the way that international finance and geopolitics interact in the short term and the long term, shaping and structuring market dynamics, technological and industrial development, and national security and diplomacy. As a consequence of the current Russo-Ukrainian War, international financial relations may undergo significant restructuring. The geopolitical and national security implications thereof for the EU, NATO, and Western partners are likely to be wide-ranging and require further attention.

Introduction: The need to integrate finance and geopolitics

The Atlantic Alliance, namely Europe and North America, currently finds itself engaged in a 'strategic competition' with China and Russia which still eludes a convincing, integral strategic concept. The Chinese leadership commands the world's second biggest economy, competes at the edge of the technological frontier, and is building increasing influence in international finance. While Russia plays a more marginal role in the techno-economic financial sphere, it shares with China the intellectual spirit, willingness, and ability to make use of this sphere to advance its own strategic interests, and undermine or disrupt those of the EU and the Atlantic Alliance.[1]

Finance and geopolitical competition have become increasingly intertwined in the decade since the 2008 global financial crisis. Hence, Western policymakers and strategists need to consider how financial markets, institutions, and players relate to 'hybrid conflict' or 'grey-zone operations'. While EU and NATO partners see China and Russia as 'strategic competitors' or 'systemic rivals' today, these autocratic powers are at the same time seen as economic – and thus financial – partners.

But while Western governments have sought economic ties largely for commercial reasons, especially in more recent decades, China and Russia are often seen to actively use economic and financial means to further their strategic objectives.[2] Such use of non-military means for strategic objectives is sometimes called a 'hybrid approach' to foreign policy and warfare. As a result, tensions between democracies and autocracies are not limited to the traditional military-strategic sphere; financial dynamics and policies have become increasingly explicitly tied to geopolitics and national security.

The central idea or hypothesis of this Hybrid CoE Working Paper is that the national security of EU and NATO countries increasingly depends on finance, and that international finance can be increasingly influenced by the West's state capitalist competitors. Essentially, the global financial system is being drawn into geopolitical dynamics or great-power politics.[3] Foreign Direct Investment (FDI) screenings appear to fracture capital markets, as do US delistings of Chinese shares, as well as financial sanctions against countries like Iran and Russia. The Chinese global economic rise is accompanied by the global expansion of Chinese state banks, in both emerging and advanced economies.[4] Central bank policies are increasingly bound up

1 E.g. Mark Galeotti, *Russian Political War. Moving Beyond the Hybrid* (London, Routledge, 2019); David Kilcullen, *The Dragons and the Snakes. How the Rest Learned to Fight the West* (Oxford, Oxford University Press, 2020), 115–166; Seth Jones, *Three Dangerous Men. Russia, China, Iran, and the Rise of Irregular Warfare* (New York, WW Norton, 2021).

2 Robert Blackwill and Jennifer Harris, *War by Other Means. Geoeconomics and Statecraft* (Cambridge, M.A., Harvard University Press, 2016); William Norris, *Chinese Economic Statecraft. Commercial Actors, Grand Strategy, and State Control* (Ithaca, Cornell University Press, 2016).

3 The EU, Hybrid CoE and Bruegel paper was an earlier example of this being done, but this work focused mainly on technical and operational issues, less on broader, strategic trends: Aleksi Aho, Arnis Šnore, and Catarina Midões, 'Hybrid threats in the financial system,' Hybrid CoE Working Paper 8, June 2020, https://www.hybridcoe.fi/wp-content/uploads/2020/07/20200630_Working-Paper-8_Web-1.pdf. [All links were last accessed on 14.04.2022.]

4 Eugenio Cerutti, Catherine Casanova and Swapan-Kumar Pradhan, 'Banking across borders: Are Chinese banks different?,' *BIS Working Paper*, no 892, 14–10–2020, https://www.bis.org/publ/work892.pdf.

with geopolitical motives.[5] Added to this, banks and financial institutions are regularly subjected to increasingly sophisticated cyberattacks.[6]

Clearly, there is an increasing overlap between financial and security policy issues in international affairs. Nonetheless, a conceptual framework as a basis for developing new policy approaches to the intersection of 'financial geopolitics' and 'hybrid conflict' appears to be lacking for the most part. Instead, policies and analysis largely focus on the more technical level and immediate issues. This Working Paper duly seeks to fill this gap by developing a conceptual framework for the nexus between finance and geopolitics in the context of full-spectrum or 'hybrid' conflict.

Policymakers and analysts focusing on the immediate issues and seeking a practical approach may benefit from this paper, which offers a perspective on the broader context within which policymaking and policies have to operate. This may be crucial given that vulnerabilities may emerge if policy and context are not in harmony. Policies are often designed in a linear way, seeking the shortest route from A to B, while neglecting to take into account that in a confrontational context, reality is often non-linear, chaotic, and complex.[7]

The weakening of the multilateral international order makes the world less stable and thus less predictable as rules appear to lose much of their strength. Due to this weakened international order as well as other factors like technological change, military-strategic and financial-economic aspects have become increasingly intertwined. However, both Western bureaucratic structures and policymakers' mental maps, as well as academic research tend to focus on specialization instead of integration of security and economic issues.

This Working Paper tries to overcome the artificial separation of financial-economic and strategic aspects by looking at how these parts interlock. First, the paper will explore the separation of economy from strategy in Western policymaking. Second, it will discuss some Chinese and Russian ideas and approaches to 'financial warfare'. Third, the paper will address why finance may have become a centre of gravity of contemporary geopolitics. Fourth, the role of finance in public-private relations underpinning national security will be addressed. Fifth, the paper will discuss how finance and the struggle for control over finance may prove to be shaping the geopolitical context.

Some caveats need to be addressed at the outset. This is not an academic research paper, nor a regular think-tank piece, but seeks instead to present a 'strategic essay' and basis for further discussion and research. As a consequence of the limited space, many issues are not covered, including the role of multilateral financial institutions like the International Monetary Fund and the Asian Infrastructure Investment Bank. The objective here is to provide a sketch of the strategic environment, and hence further analysis, details and refinement may subsequently be required.

5 E.g. Johnathan D. Falcone, 'The People's Bank of China's Monetary Armament Capabilities and Limitations of Evolving Institutional Power,' *Military Review*, vol. 100, no. 4 (July-August 2020), 70–85; https://www.armyupress.army.mil/Portals/7/military-review/Archives/English/JA-20/Falcone-China-Monetary-Armament-1.pdf.

6 Juan Zarate, 'The Cyber Financial Wars on the Horizon. The Convergence of Financial and Cyber Warfare and the Need for a 21st Century National Security Response,' in Samantha Ravich (ed.), *Cyber-Enabled Economic Warfare: An Evolving Challenge* (Washington DC, Hudson Institute, 2015), 93–120.

7 E.g. Edward Luttwak, *Strategy. The Logic of War and Peace* (Cambridge, MA, Harvard University Press, 2001 2nd Edn [1987]), 1–86.

Finance and geopolitics in the West

Most Western policymakers have been shaped in a context in which finance did not play a significant role in international conflict. Also intellectually, economic and strategic issues developed in separate – academic – realms. These are not new observations. The historian Paul Kennedy, author of *The Rise and Fall of the Great Powers*, noted back in the 1980s that "financial and business matters have generally been kept apart from the world of strategy and diplomacy, just as the *laissez-faire* (…) men and Whitehall mandarins preferred".[8] However, this has not always been the case: there are many historical examples of Western rulers and thinkers understanding the potential of finance in diplomacy and war, but after 1945, the separation of financial and economic aspects from geopolitical conflict was standard.

Historically, the ancient Greeks and Romans already understood the decisive importance of money and finance. Roman Senator Cicero famously quipped that endless money forms the sinews of war.[9] From the late Middle Ages onwards, kings and rulers became dependent upon bankers and financiers, who would provide them with the necessary loans to maintain functioning governments, conduct diplomacy, and wage wars.[10] This gave bankers and financial dynamics influence over the course of European politics and diplomacy. As bankers and financial markets would turn away from, or even against, the kings and rulers they had previously supported, they also changed the pattern of European wars and diplomacy, time and again.[11]

In the decades leading up to the First World War, strategic thinkers began to actively contemplate manipulating financial markets as a part of power politics and as an objective of military operations. The French *Jeune École* of naval thinkers suggested attacking British commercial shipping in order to cause the London maritime insurance market to crash, which would lead to severe financial losses in the City of London, which would then pressure Whitehall to give in to French diplomatic demands. This scenario inspired the UK to subsequently implement its own version of financial warfare against the German Empire.[12] Imperial Germany itself had sought to limit Russia's military

8 Paul Kennedy, 'Strategy versus Finance in Twentieth-century Britain,' in *Strategy and Diplomacy, 1870–1945* (Fontana Press, 1989 [1983]), 87.

9 The sinews of war, unlimited money. Cicero, Fifth Philippic ch. 5.

10 Jacques Le Goff, *Marchands et banquiers du Moyen Âge* [Medieval merchants and bankers] (Paris, Presses Universitaires de France [PUF], 1956), 61–69; Richard Kaeuper, *Bankers to the Crown. The Riccardi of Lucca and Edward I* (Princeton, Princeton University Press, 1973), 173–191.

11 Fernand Braudel, *Civilisation matérielle, économie et capitalisme, XVe-XVIIIe siècle. Tome 3* [Material civilization, economy and capitalism, 15th-18th century] (Paris, Armand Colin, 1979), 130–144 ; J. H. Elliot, *Europe Divided, 1559–1598* (Ithaca, Cornell University Press, 1982 [1968 1st edn.], 43–69; Charles Kindleberger, *A Financial History of Western Europe* (Oxford, OUP, 1993, [2nd edn.]).

12 Nicholas Lambert, *Planning Armageddon. British Economic Warfare and the First World War* (Cambridge, MA., Harvard University Press, 2012), 23–24; Geoffrey Till, *Maritime Strategy and the Nuclear Age* (London, Macmillan, 1982), 37.

buildup by prohibiting German financiers to lend to the Czar.[13]

However, in the decades after the Second World War, European and Allied policymakers did not experience a situation in which their financial system was tied up with or dependent upon that of the – potential – adversary. During the Cold War, finance mattered greatly to the Alliance, but as an internal issue – concerning financial stability and European reconstruction, allied defence spending, and intra-allied monetary relations.[14] For NATO, the East-West relationship had an important economic component in preventing access by the Communist Bloc to sensitive Western technologies.[15] While Communist Bloc countries did have banks in the West, mainly to finance trade, it was only after 1982, when Western countries briefly imposed a 'credit boycott' on Warsaw Pact countries, that financial conflict between East and West began to affect the course of the Cold War.[16]

In the post-Cold War era, the focus on 'geopolitics' or great-power conflict became marginal, and the idea of global financial and economic integration seemed dominant in the West. Thus, finance and economics were considered a field for cooperation, not outright competition, and few believed that financial and economic tools would or could be used in a 'hypothetical conflict' between China and the United States, for example. China was believed and – famously – called upon to become a 'responsible stakeholder' in the liberal order.[17]

This Western sense of a post-Cold War era has been replaced by the view that the world is now dominated by 'a new era of great-power

13 'Lombardverbot': Ulrich Lappenküper, 'Die deutsch-russischen Beziehungen nach der Reichsgründung (1871–1890)' [German-Russian relations after the founding of the empire, 1871–1890] in idem (ed.), *Otto von Bismarck und das „lange 19. Jahrhundert"* [Otto von Bismarck and the 'long 19th century'] (Leiden, Brill, 2017), 251–260.

14 On economic reconstruction, see Benn Steil, *The Marshall Plan. Dawn of the Cold War* (New York, Simon and Schuster, 2019); on allied defence spending and monetary relations, Francis Gavin, *Gold, Dollars, and Power. The Politics of International Monetary Relations, 195801971* (Chapel Hill, University of North Carolina Press, 2004).

15 E.g. Ian Jackson, *The Economic Cold War. America, Britain and East-West Trade, 1948–1963* (Houndmills, Palgrave Macmillan, 2001); Frank Cain, *Economic Statecraft during the Cold War. European Responses to the US Trade Embargo* (Routledge, 2007).

16 However, this 'credit boycott' does not seem to have been a NATO decision, but rather a coordination decision made by several allies, most importantly Germany. For some background on Soviet banks in the West, see Daniel DeMatos, 'The Soviet Union's Global Bank,' blog, *The Tontine Coffee House*, 9 March 2020, https://thetchblog.com/2020/03/09/the-soviet-unions-global-bank/. On credit boycott: Maximilian Graf, 'Before Strauß: The East German Struggle to Avoid Bankruptcy During the Debt Crisis Revisited,' *International History Review*, vol. 42, no. 4, (2020): 737–754, https://www.tandfonline.com/doi/pdf/10.1080/07075332.2019.1641542; Franciszek Tyszka, *Foreign debt, crisis management, systemic transformation. Poland 1989–1994*, EUI PhD thesis (Florence, European University Institute, 2019), https://cadmus.eui.eu/handle/1814/63085.

17 Robert Zoellick, 'Whither China? From Membership to Responsibility', Remarks to the National Committee on U.S.-China Relations, 21 September 2005, https://2001–2009.state.gov/s/d/former/zoellick/rem/53682.htm.

competition' and 'systemic rivalry'.[18] In this context, the 2017 US National Security Strategy underscored that "economic security is national security", and that strategic competition transcends the military-strategic and politico-ideological conflict of the Cold War.[19] It remains to be seen whether EU member states and NATO partners will be successful in integrating financial-economic policies at all levels of their approach into geopolitics and strategic competition.

18 Uri Friedman, 'The New Concept Everyone in Washington Is Talking About,' *The Atlantic*, 6 August 2019, https://www.theatlantic.com/politics/archive/2019/08/what-genesis-great-power-competition/595405/; EU Commission and HR/VP, 'EU-China – A strategic outlook,' JOIN(2019), Strasbourg, 12 March 2019, https://ec.europa.eu/info/sites/default/files/communication-eu-china-a-strategic-outlook.pdf.

19 Donald Trump White House, 'US National Security Strategy,' Washington D.C., December 2017, https://trumpwhitehouse.archives.gov/wp-content/uploads/2017/12/NSS-Final-12-18-2017-0905.pdf.

The new era of financial warfare

In early 2009, some months after the fall of Lehman Brothers, the US Director of National Intelligence, Dennis C. Blair, delivered a statement on the financial crisis to Congress. He considered that the global financial crisis and its geopolitical implications were then *the* key national security threat.[20] At the time, both Russia and China had been thinking about ways to use financial instruments to advance their interests in support of geopolitical conflict with the West. Similarly, the United States itself was actively applying and developing new ideas about financial sanctions to complement more conventional economic sanctions. It was, in the words of a former US Treasury official, 'a new era of financial warfare' in which geopolitics is 'a game best played with financial and commercial weapons'.[21]

The shape of things to come became clear during the financial crisis of 2008. In August 2008, as Russia invaded Georgia, Chinese officials informed US Treasury Secretary Hank Paulson that they had discussed selling and shorting Freddie Mac and Fannie May with Russian counterparts.[22] Russian officials reportedly proposed a financial attack not to make money, but to wreak financial havoc. While the Russian military advanced in Georgia, the United States would be busy at home. China declined the Russian suggestion for financial warfare. However, some financial analysts noted that by tightening credit facilities from late 2007 onwards, the Chinese central bank had forced Chinese investors to buy American assets, reducing liquidity in the US markets. This squeeze in liquidity may have triggered the ensuing financial crisis.[23] There's no indication that the People's Bank of China's (PBOC) tightening was calculated to trigger a financial crisis on Wall Street, but this observation indicates what is possible.

Both Chinese and Russian strategists have been considering using financial means not only to make money, but also to advance their geopolitical objectives. Reportedly, during the 1980s, the Soviet KGB's leadership regarded financial markets as a new battlefield, replacing or complementing military conflict. The KBG allegedly perceived that the future conflict between Russia and the West would be about controlling the markets, which required Russian infiltration of the Western financial system. By affecting capital flows and infiltrating financial centres, Russia would be able to politically manipulate the West.[24] Such deliberations would be in keeping with the longer tradition of Soviet and Russian strategic thinking, which emphasized economic exhaustion of the opponent over its physical destruction.[25] During the 1990s, Russian strategists thought that firing barrages of missiles at the enemy's financial and

20 'The primary near-term security concern of the United States is the global economic crisis and its geopolitical implications.' US Director of National Intelligence, Dennis C. Blair, Annual Threat Assessment of the Intelligence Community, Testimony to Senate Select Committee on Intelligence, 12 February 2009.

21 Juan Zarate, *Treasury's War. The Unleashing of a New Era of Financial Warfare* (New York, Public Affairs, 2013), 384.

22 Hank Paulson, *Dealing with China. An Insider Unmasks the New Economic Superpower* (New York, Twelve/Hachette Book Group, 2015), 246–250.

23 Michael Howell, *Capital Wars. The Rise of Global Liquidity* (Palgrave Macmillan, 2020), 7–8.

24 Catherine Belton, *Putin's People. How the KGB Took Back Russia and Then Took on the West* (New York, Strauss, Farrar, and Giroux, 2020), 16, 32–33, 75.

25 Andrei Kokoshin, *Soviet Strategic Thought, 1917–1991 (Cambridge, MIT Press, 1993), 71–72.*

industrial centres could bring about a speedy end to a war.[26] And in the run-up to the Russian 2008 intervention in Georgia, they thought that an 'economic war' could be fought mainly with non-kinetic means.[27] Valery Gerasimov's seminal article on 'non-linear' warfare, which emphasized the integration of military and non-military instruments, expressed similar ideas.[28]

Among the Chinese leadership there is a tradition of seeing finance as a geopolitical tool. During the nineteenth century, when China partially lost its sovereignty, the expansion of European and American business in China was facilitated by Western high finance.[29] China's 'century of humiliation' was thus, from the Chinese Communist Party's (CCP) perspective, caused by Western financial power. Such ideas remain current. A popular book in the late 2000s, for example, was *Currency Wars*, which described how the Rothschild banking house used capital markets to contain China's rise. Such conspiracy-style thinking about finance was not just popular in China, but also accepted by the CCP leadership.[30] This appreciation of finance as an instrument of power sometimes translates into Chinese strategic thinking. Some thinkers called upon the People's Liberation Army to combine 'orthodox' with 'unorthodox' strategies, that is classical military-against-military approaches with non-military approaches against the integral power base of the adversary.[31] In this context the concept of 'unrestricted warfare' emerged, which explicitly mentions financial-economic assets as a means and target in war.[32]

While it is difficult to assess the extent to which both Russian and Chinese officials and strategists think about 'waging financial war', the most important thing to remember is that they *do* think about it; moreover, these countries have instruments at their disposal to conduct acts of 'financial war'.

The United States has expanded its use of financial tools to further national security objectives. There has been a notable shift from 'traditional' economic to financial sanctions.

26 Vladimir Slipchenko, 'The Strategic Content of The State's Military Reform (A Prognostic View),' *Vooruzheniye. Politika. Konversiya, 7 July 2003 [FBIS Translated Text CEP20031229000123], cited in: Andrei Shoumikhin, 'Wars of the Future. Implications for the Reform of the Russian Armed Forces' (Fairfax, Va., National Institute for Public Policy, April 2004), 3–4.*

27 Interview, Viktor Litovkin, 'Général Gareev: "la Russie sera l'arbitre géopolitique des conflits à venir"' [Russia will be the geopolitical arbiter of future conflicts] *Voltairenet*, 26–01–2007, http://www.voltairenet.org/article144842.html.

28 Valery Gerasimov cited in: Mark Galeotti, 'The "Gerasimov Doctrine" and Russian Non-Linear War,' *In Moscow's Shadows (blog), 6 July 2014,* https://inmoscowsshadows.wordpress.com/2014/07/06/the-gerasimov-doctrine-and-russian-non-linear-war/.

29 Youssef Cassis, *Capital of Capitals. The Rise and Fall of International Financial Centres, 1780–2009* (Cambridge, Cambridge University Press, 2010 [2006]), 134–135.

30 Richard McGregor, 'Chinese buy into conspiracy theory,' *Financial Times*, 25 September 2007, https://www.ft.com/content/70f2a23c-6b83-11dc-863b-0000779fd2ac.

31 Gao Heng, 'Future Military Trends,' in Michael Pillsbury (ed.), *Chinese Views of Future Warfare* (Honolulu, University Press of the Pacific, 2002), 85–94; 86–87.

32 Qiao Liang and Wang Xiangsui, *Unrestricted Warfare. China's Master Plan to Destroy America (Dehradun, Natraj, 2007 [Beijing, PLA, 1999]), 32.*

Furthermore, the application of US foreign direct investment screening has widened, duly imposing further limits on the capital markets, and seeking to limit undesirable takeovers of strategically relevant US companies and their supply chains abroad. In a more classical military way, in its anti-ISIL operations, the US military launches strikes against the financial infrastructure of IS, including its key finance officials or bankers, and physical dollar holdings, as well as against the oil refineries which have produced the greatest revenue for the group. In the anti-ISIL financial warfare, kinetic and non-kinetic means were combined, in that air strikes, cyber operations, and targeted sanctions were jointly executed.[33] This military-financial approach, first applied against ISIL, may set a pattern for the future.

There's a profound difference between the Russian and Chinese approach on the one hand, and the US – and European – approach to 'the new era of financial warfare' on the other. The former, 'state capitalist' powers, seem ready to use financial and monetary instruments for geopolitical purposes, while the US and the EU tend to keep financial and monetary policy instruments separate from national security and explicit geopolitical objectives. Financial markets, institutions, and players are still believed to be separate from geopolitics and national security in Western capitals.

Yet finance can thus clearly become a target of 'hybrid' or 'grey zone' conflict strategies. While much of the debate about the relationship between finance, security, and geopolitics centres on the more immediate and visible issues such as sanctions, cyber operations, and military attacks, the deeper and longer-term issue of financial pre-eminence or even dominance in relation to geopolitical dynamics and techno-industrial policy requires more attention. How this works will be explored in the next section.

33 Rebecca Kheel, 'ISIS finance minister, other leaders killed in airstrikes,' *The Hill*, 10 December 2015, https://thehill.com/policy/defense/262800-isis-finance-minister-two-other-leaders-killed-in-airstrikes; Yeganeh Torbati and Brett Wolf, 'In taking economic war to Islamic State, U.S. developing new tools,' *Reuters*, 24 November 2015, https://www.reuters.com/article/us-france-shooting-usa-sanctions-insight-idUSKBN0TD0BJ20151124; 'ISIS video shows destruction from U.S. airstrike on Mosul bank,' *Reuters*, 12 January 2016, https://www.reuters.com/article/us-mideast-crisis-usa-cash-idUSKCN0UQ13V20160112.

Territory, techno-industrial heartlands and capital

The process of financialization, namely the increased role of financial markets, institutions and players in the economy, has also spilled over, by extension, to national security and geopolitics. This needs to be unpacked in several steps. First, it is necessary to briefly comment on the 'return of geopolitics'. Second, the geopolitical struggle is intertwined with geo-economics, or the struggle for control over wealth, as national security depends on economic security, or access to and control over strategic economic means. These comprise the so-called 'industrial heartlands' and 'business ecosystems'. Third, financial dynamics dominate much of the economic resources and wealth upon which national security and geopolitics depend.

The geopolitical struggle is widely recognized to have returned after a 25-year-long post-Cold War era, which many believed marked 'The End of History'. The relative absence of struggle between great powers seemed to allow for a trend towards a rules-based international order, which set the boundaries for global trade and capital flows. However, around 2014, after Russia's annexation of Crimea and China's island-building in the South China Sea, many Western observers believed that they were witnessing 'the return of geopolitics'.

During the post-Cold War 'End of History' phase, it was widely held that ideological differences between democracy and autocracy would be superseded by a common search for ever-greater wealth in a globalized world.[34] There was a perceived shift from geopolitics to geo-economics, from the struggle for control over territory to the struggle for control over wealth.[35] Conflict would no longer be about politics and territories, but about economics and technologies. And such economic conflicts would not be fought with tanks on the battlefield, but with technocrats and lobbyists in neutral office buildings. 'Geo-economics' actually seems a somewhat problematic concept, considering that states have always struggled for economic resources as a means to acquire power and wealth, and to obtain wealth as a means to acquire more power.

Even though military tensions over territories have become more visible again since 2014, the struggle for control over the structure of the world economy has not subsided. Actually, the struggle for techno-industrial advances only intensified, in part as a function of renewed military tensions. Thus, the 'return of geopolitics', and the increased chance of large- scale military conflict, does *not* mean that 'geo-economics is out'.

Both the 'geo-economic' struggle for markets and the 'geopolitical' conflict over territory have continued to become ever more intertwined. In other words, classical military-strategic and national security issues and politico-economic issues seem increasingly related, as both interact at the high strategic 'macro level', as well as at the lower technical 'micro level'. For example, at the macro level, the growth of Chinese military power is intertwined with Chinese economic growth. At the explicit micro level, the struggle for future dominance in microchips is seen to affect both who will become economically as well as militarily the most advanced. Moreover, at the more intermediate, tactical level, Western concerns that vital infrastructure such as harbours and telecommunications

34 Walter Russell Mead, 'The Return of Geopolitics,' *Foreign Affairs*, vol. 93, no. 4 (May 2014): 69–79.
35 Edward Luttwak, 'From Geopolitics to Geo-Economics. Logic of Conflict, Grammar of Commerce,' *The National Interest*, no. 20 (Summer 1990):17–23.

infrastructure are controlled by Chinese parties indicate that what seems of economic importance on the surface may also be militarily relevant. Additionally, the technological spin-off and spin-on between military and civilian technologies indicate that dual-use is increasingly the name of the game.[36]

This nexus of 'territorial' and 'techno-industrial' struggles was pointed out by mid-century strategic thinker Robert Strausz-Hupé. Writing during the Second World War, he foresaw that future conflicts would be decided by those powers which controlled most of the 'industrial heartlands', back then the Detroit Area, the German Ruhr, and the Soviet Urals.[37] Some might contend that these heartlands have been replaced by global supply chains, and that geography does not matter to economics.[38] However, contemporary business ecosystems like Silicon Valley and Shenzhen are limited geographical areas where high-tech industries, technological innovation, and cutting-edge research, as well as finance come together.[39] Both the classical industrial heartlands as well as the modern high-tech business ecosystems often interact with military production and military R&D programmes. The main point to note is that geopolitics is not only about (military) control over certain key geographic areas, such as the 'heartlands and rimlands', or the 'sea lines of communication', but also about controlling techno-industrial heartlands.

These techno-industrial heartlands were once controlled and actively managed by an alliance of corporate and political leaders. The corporate leadership controlled the industries, and Western governments regulated and protected their markets. This public-private alliance was a central tenet of the Allied Cold War strategy. The economist J. K. Galbraith observed that a 'technostructure' or network of corporate managers, especially the executive boards, controlled the functioning of 'their' companies.[40]

Writing in the mid-1960s, Galbraith warned that the powerful technostructure could be broken if corporations were to become dependent on outside finance capital – which is exactly what happened. Increasingly, corporations have become dependent on outside sources of capital. Further, since the onset of the 1980s junk bond revolution and the rise of 'corporate raiders', financial players have broken the technostructure.[41] Nowadays, the providers and regulators of finance capital dictate the rules according to which the corporations ought to be run. Very often this happens to imply a focus on

36 'Spin-around' supersedes classical notions of military-to-civilian 'spin-off' and civilian-to-military 'spin-on'. The concept of 'spin-around' is convincingly put forward in Linda Weiss, *America Inc.? Innovation and Enterprise in the National Security State* (Ithaca, Cornell University Press, 2014), esp. 75–95; Mariana Mazzucato, *The Entrepreneurial State. Debunking Public vs. Private Sector Myths* (London, Anthem Press, 2014), 87–112.

37 Robert Strausz-Hupé, *The Balance of Tomorrow. Power and Foreign Policy in the United States* (New York, NY, Putnam's Sons, 1945).

38 E.g. Thomas Friedman, *The Earth is Flat.*

39 James Moore, *The Death of Competition. Leadership and Strategy in the Age of Business Ecosystems* (New York, HarperCollins, 1996).

40 John Kenneth Galbraith, *The New Industrial State* (Boston, M.A., Houghton Mifflin, 1967), 60–85, esp. 80–85 on the power of capital.

41 For the best explanation of this process, see Bryan Burrough and John Helyar, *Barbarians at the Gate. The Fall of RJR Nabisco* (New York, NY, Random House, 1990).

the financial return on capital and risk management policies, and much less the actual industrial productive output, supply and demand dynamics, let alone on maintaining good public-private relations with governments.[42] In parallel, there has also been the rise of powerful tech companies, controlling data flows, upon which governments become increasingly reliant as they embrace digitalization. This leads to new vulnerabilities. In the end, however, these tech companies also respond to financial incentives.

Ultimately, in the same way that finance is crucial for states seeking to debt finance their policies, access to capital is essential for the development of technologies and industries. The extent to which industries can finance themselves, or to which they are dependent upon outside financiers, such as banks, bond and stock markets, as well as private investors, vastly determines by whom and the dynamics by which the industrial heartlands and business ecosystems are 'controlled and shaped'. The role of capital ownership will be further explored in the next section.

To sum up, geopolitics and geo-economics are hard to distinguish and often go hand in hand. This has implications for military and economic policies. The issue of access to and control over strategic economic resources, or 'economic security', is at the core of great-power relations. Having economic security depends greatly on capital markets and finance. In fact, due to the increased role of finance in the economy, and the key importance of economic resources to military-strategic power, who controls finance may control world politics. Time and again throughout history, wars and political schemes were enabled or limited by the role of finance. Moreover, industrial dynamics and technological progress are similarly dependent upon capital markets for investments and transactions. Finance, in other words, has at times been of great politico-strategic and techno-economic importance.

42 Daniel Pinto, *Capital Wars. The New East-West Challenge for Entrepreneurial Leadership and Economic Success* (London, Bloomsbury, 2014 [2013]).

Finance breaking the technostructure

Ownership of the industries that made up the technological and economic backbone of the West's geopolitical position has shifted from industry to finance. Today, the main shareholders of key companies are financial players who follow – and make – financial market dynamics. This shift in power, or the process of 'financialization', has broken the technostructure, namely the corporate managerial groups which controlled business and industry.

Financialization took off in the 1970s and 1980s and continues as a result of many complex factors, including increased foreign exchange volatility, export surpluses, financial regulations, quantitative easing, as well as stagnating industrial productivity and lagging innovation dynamics.[43] For a multitude of reasons, industrial companies sold increasing numbers of their shares and borrowed on the bond markets, which transferred control from company boards to financial actors. The technostructure crumbled, and financial markets and players began to rule over the Western industrial heartlands. During the Cold War, NATO's military forces had been preparing to fight, even a nuclear conflict, to prevent Soviet-Russian control over the German 'Ruhrgebiet'. But a decade after the Cold War, Russian and Chinese investors, controlling excess dollars from their export surpluses, bought partial financial control over parts of the Western industrial and technological heartlands. In 2006, Russia's Vneshtorgbank (VTB) bought a five percent stake in the European Aeronautic Defence and Space Company (EADS). Within a year, Russian aircraft manufacturers gained access to Airbus's production lines.[44] After the German steel industry had been hit by global competition, in 2002, a Chinese company bought an entire steel factory from Thyssen Krupp and completely transferred the plant from Dortmund along the Ruhr to Shagang along the Yangtze.[45] Similarly, China bought dozens if not hundreds of steel mills from formerly industrialized countries. In doing so, China acquired its industrial backbone from abroad.[46] Equally important, selling off their assets seemed the right decision from the financial point of view. While German steel production

43 For background on the process of financialization, see Peter Drucker, 'The Changing Multinational,' and 'Managing Currency Exposure,' in *The Frontiers of Management. Where Tomorrow's Decisions Are Being Shaped Today* (New York, Truman Talley, 1986), 61–70; Susan Strange, *Mad Money. When Markets Outgrow Governments* (Ann Arbor, MI, University of Michigan Press, 1998); John Kay, *Other People's Money. The Real Business of Money* (New York, Public Affairs, 2016); Rana Foroohar, *Makers and Takers. The Rise of Finance and the Fall of American Business* (New York, Crown Business, 2016).

44 Nicola Clark and Andrew E. Kramer, 'State-Owned Russian Bank Buys a 5% Stake in EADS,' *New York Times*, 12 September 2006, https://www.nytimes.com/2006/09/12/business/worldbusiness/12eads.html; Nicola Clark, 'Russian companies win right to work on A350,' *International Herald Tribune*, 22 March 2007, https://www.nytimes.com/2007/03/22/business/worldbusiness/22iht-rusair.4998291.html.

45 James Kynge, *China Shakes the World. A Titan's Rise and Troubled Future – And the Challenge for America* (New York, Houghton Mifflin, 2006), 1–11; Joseph Kahn and Mark Landler, 'China Grabs West's Smoke-Spewing Factories,' *New York Times*, 21 December 2007, https://www.nytimes.com/2007/12/21/world/asia/21transfer.html.

46 Michael Komerasoff, 'Make the Foreign Serve China: How Foreign Science and Technology Helped China Dominate Global Metallurgical Industries,' Washington DC, CSIS Occasional Paper Series, 1 March 2017, https://www.csis.org/analysis/make-foreign-serve-china-how-foreign-science-and-technology-helped-china-dominate-global.

did not structurally decline, China has come to dominate the steel industry, with all of the geopolitical benefits, and in an apparent position to threaten the future of the Western steel industry.[47] During the subsequent fifteen years, Chinese investors bought increasingly technologically advanced companies in Germany and elsewhere in Europe, including robot producer Kuka in 2016.[48]

Even though European authorities set up foreign investment control mechanisms, Chinese acquisitions continued under the radar.[49] For example, Morgan Stanley and Bank of America reportedly helped Chinese car manufacturer Geely to silently acquire an almost controlling stake in Daimler, using more financial tools like dark pools, complex derivatives and legal structures called 'collars'.[50] This makes it seem like 'Western' financial institutions duly assisted Chinese foreign investors to legally circumvent Western security policies.

In Western industrial societies during most of the Cold War, political leaders and corporate leaders knew how to find each other, thanks, in part, to the 'technostructure'. As a result of financialization, it no longer suffices for governments to simply call 'their' industrial or technology companies like General Motors or Google, ThyssenKrupp or Kuka. The financial players appear to rule the capital markets which underpin many aspects of national security. Thus, for their economic security, governments today need to work with investment banks, asset managers, and private equity firms. However, while Western governments may seek to influence these financial players, their interests and loyalties may not correspond.

To recap, the rule of the 'technostructure' over the West's industrial heartlands has gradually been replaced by the rule of finance over industry and technology. In the end, the shareholders and bondholders rule over their capital investments in this or that company. The shift of power from industry to finance puts finance capital, and the influence and control thereover, at the centre of geopolitical dynamics and national security. The more dependent both governments and economies are on external financing, the more vulnerable they become, both in the short and the longer term, to financial dynamics. The interests of those who provide that external financing, as well as the

47 Such concerns have not materialized. 'German Steel Industry Faces Competition from China,' *Deutsche Welle*, 9 October 2007, https://p.dw.com/p/LsSh; Nicole Goebel, 'Steel industry urges tough action on China amid overcapacity,' *Deutsche Welle*, 15 February 2016, https://p.dw.com/p/1HvjN.

48 Lucy Hornby, 'Kuka wins concessions as Midea moves to soothe concerns,' *Financial Times*, 29 June 2016, https://www.ft.com/content/99e46166-3db2-11e6-9f2c-36b487ebd80a.

49 Daniel Michaels, 'Behind China's Decade of European Deals, State Investors Evade Notice,' *Wall Street Journal*, 30 September 2020, https://www.wsj.com/articles/behind-chinas-decade-of-european-deals-state-investors-evade-notice-11601458202?page=1. Interestingly, some Western academics even called upon Chinese investors to invest 'under the radar'; Peter Williamson, 'Staying under the radar,' *China Daily*, 30 January 2019, https://www.chinadaily.com.cn/global/2019-01/30/content_37433452.htm.

50 Adam Jourdan and Norihiko Shirouzu, 'How Geely's Li Shufu spent months stealthily building a $9 billion stake in Daimler,' *Reuters*, 1 March 2018, https://www.reuters.com/article/us-daimler-geely-shell-insight-idUSKCN1GD5ST; Ruth David, Dinesh Nair, Jonathan Browning, 'Geely Is Said to Use $9 Billion Collar Trade on Daimler Deal,' *BloombergQuint*, 28 February 2018, https://www.bloombergquint.com/business/geely-is-said-to-use-9-billion-collar-trade-on-daimler-purchase.

financial market structures which shape capital flows, thus become the objective of power politics, national security, 'hybrid conflict', and 'grey zone operations'. Eventual counter-measures and policy programmes may follow this analysis.

Financial crises, structures and sovereignty problems

National security can be affected by financial markets, both immediately and in the longer run. The more a country relies on financial markets, the more vulnerable it becomes both to short-term shocks as well as to longer-term trends in finance. The consequence for national security is that the more a country depends on finance, the more its national security policymakers should be concerned about financial dynamics, be thinking about adequate responses, and discussing how to maintain long-term financial stability. From the mid-1980s until the time of the global financial crisis in 2008, many believed that, following deregulation, markets were 'ruling themselves' and outgrowing state power.[51] From the mid-2000s onwards, some countries which ran huge export surpluses, like China, pooled their surplus capital in sovereign wealth funds and their central bank accounts. This led to the rise of 'state capitalism' from the mid-2000s onwards or, more precisely, the emergence of direct state control over, and management of, hundreds of billions of dollars in relatively liquid assets.[52]

During the last three decades, the century-old pattern of financial crises causing deep political disturbances has been reaffirmed. Most interestingly, some of these recent crises were triggered, albeit not caused, by the individual agency of powerful speculators or central bank decisions. For example, when George Soros's *Quantum Fund* shorted the British pound in 1992, the UK dropped out of the 'European Exchange Rate Mechanism' – deeply affecting the European integration process and UK foreign policy.[53] Subsequently, during the 1997 Asian Financial Crisis, Soros's speculations appeared to have contributed to the downfall of the Thai and Indonesian governments,[54] with the Malaysian Prime Minister, Mahatir Mohamed, accusing Soros of 'financial warfare'. Under financial distress, East Asian countries seemed forced to adopt economic programmes they would otherwise not have adopted.[55] This leads to the question of whether strategically motivated actors, perhaps working together with financially motivated players, may seek to cause financial crises.

Some European governments perceived the Eurozone crisis as a danger to their sovereignty, or as a key security issue. The Spanish and Greek intelligence services were reportedly tasked with investigating whether speculators were spreading rumours negatively affecting the markets for their debt. And the French intelligence service seems to have sought insight

51 This is the central argument in Eric Helleiner, *States and the Reemergence of Global Finance. From Bretton Woods to the 1990s* (Ithaca, NY, Cornell University Press, 1994).

52 Eric Helleiner and Troy Lundblad, 'States, Markets, and Sovereign Wealth Funds,' *German Policy Studies*, Vol. 4, No. 3 (2008): 59–82; Ian Bremmer, *The End of the Free Market. Who Wins the War Between States and Corporations?* (New York, NY, Portfolio/Penguin, 2010); Eric Weiner, *The Shadow Market. How Sovereign Wealth Funds Secretly Dominate the Global Economy* (New York, NY, OneWorld/Simon & Schuster, 2011 [2010]).

53 Soros himself argues that the pound would have dropped out of the ERM sooner or later. He certainly accelerated it. George Soros, *Soros on Soros. Staying Ahead of the Curve* (New York, Wiley, 1995), 79–86.

54 James Kynge, 'China was the real victor of Asia's financial crisis,' *Financial Times*, 3 July 2017, https://www.ft.com/content/5cf22564-5f2a-11e7-8814-0ac7eb84e5f1.

55 David Wessel and Darren McDermott, 'Mahathir Attacks Speculation And Soros, Who Returns Fire,' *Wall Street Journal*, 22 September 1997, https://www.wsj.com/articles/SB874869702799623500.

into the analysis and moves of American banks in Europe.[56] Actually, the rumour that the China Investment Corporation, China's main sovereign wealth fund, would stop buying European assets caused an immediate and brief collapse of the market for Southern European government bonds.[57] While Chinese officials quickly indicated that they would keep buying Eurozone debt, the brief collapse of the market gives an indication of the Chinese power over the Euromarket at the time.

These episodes of acute financial crisis not only indicate the political impact of such a crisis, but also the potential impact of a single or a few financial players. The signals that Russia and China actively considered financial warfare against the United States contributed to the US national security establishment's more explicit attention to financial markets.[58] As the global financial crisis evolved, the Pentagon organized a 'financial war game', during which a few hedge funds succeeded in breaking the US dollar.[59] It is still a topic of debate whether China's holdings of US Treasury Bonds are a useful instrument of financial warfare, or whether the US and China are locked in a relationship of 'mutually assured financial destruction'.[60] However, as noted above, some analysts believe that PBOC decisions in the autumn of 2007 – inadvertently – led to or contributed to the collapse of Lehman Brothers in 2008.[61]

National security is also affected by the somewhat less visible and less immediate shaping of the structure of the global capital markets. The structure or mechanics of global capital markets are to a significant extent in

56 Maxime Renahy, *Là où est l'argent* [Where the money is] (Paris, Les Arènes, 2019); 'La inteligencia griega identifica a los autores del ataque a su deuda' [Greek intelligence identifies the authors of the attack on its debt], *El Pais*, 19 February 2010, http://economia.elpais.com/economia/2010/02/19/actualidad/1266568382_850215.html; '[P]ara prevenir cualquier riesgo o amenaza que afecte a la independencia e integridad de España' [to prevent any risk or threat that affects the independence and integrity of Spain] e 'intentando dar mejor respuesta a los retos que plantea la actual economía global' [trying to respond better to the challenges posed by the current global economy], Claudi Pérez, 'El CNI investiga las presiones especulativas sobre España' [National Intelligence Centre investigates the speculative pressures on Spain], *El País*, 14 February 2010, http://elpais.com/diario/2010/02/14/economia/1266102005_850215.html.

57 Jamil Anderlini and David Oakley, 'China reviews eurozone bond holdings,' *Financial Times*, 26 May 2010, https://www.ft.com/content/7049ad6e-68ea-11df-910b-00144feab49a, 'China fund "very concerned" on shaky eurozone,' *Financial Times*, 27 May 2010, https://www.ft.com/content/3b23c824–6983–11df-8ae3–00144feab49a; Joseph Quinlan, *The Last Economic Superpower. The Retreat of Globalization, the End of American Dominance, and What We Can Do about It* (New York, McGraw-Hill, 2011), 37–138.

58 'The primary near-term security concern of the United States is the global economic crisis and its geopolitical implications.' US Director of National Intelligence, Dennis C. Blair, Annual Threat Assessment of the Intelligence Community, Testimony to Senate Select Committee on Intelligence, 12 February 2009.

59 The Pentagon hosted the two-day event on 17 and 18 March 2009 at the Warfare Analysis Laboratory in Ft. Meade, Laurel, Maryland. Among the participants were, among others, bankers from UBS; Steven Halliwell, managing director of a hedge fund called River Capital Management; Paul Bracken; James Rickards. See Eamon Javers, 'Pentagon preps for economic warfare,' *Politico, 9 April 2009*, http://www.politico.com/news/stories/0409/21053.html.

60 E.g. Michael Pettis, 'China Cannot Weaponize Its U.S. Treasury Bonds,' CIEP Financial Markets Blog, 29 May 2020, https://carnegieendowment.org/chinafinancialmarkets/79218.

61 Michael Howell, *Capital Wars. The Rise of Global Liquidity* (Palgrave Macmillan, 2020), 7–8.

the hands of private actors, like rating agencies, index providers, as well as numerous other players. For example, the rating agencies Moody's and Fitch had a huge influence on the perspective that multilateral institutions adopted on sovereign debt.[62] Such influential 'private' actors can be subject to political pressure and manipulation, including from governments.

The allocation of trillions of dollars of portfolio investment has been outsourced to index providers, rendering them extremely influential. In 2018, MSCI, formerly the Morgan Stanley Composite Index, included China in its emerging market index. The inclusion of China in the MSCI caused hundreds of billions of dollars to flow nearly automatically into Chinese stocks. In subsequent years, other bond index providers followed MSCI's example, and they included Chinese government bonds.[63] In 2021, BlackRock, the world's largest asset manager, called for China's 'emerging market' status to be lifted and for a tripling of portfolio investor inflows into China's capital markets.[64] This near-automatic flow of Western investment amounting to hundreds of billions of dollars into Chinese government bonds and corporate stock strengthens China's economy and weakens the economies of other countries which receive relatively less.

The decision by MSCI and BlackRock's recent call may also have been coloured by a long-running Chinese influence campaign. Chinese authorities and Western investors with interests in China reportedly pressured MSCI to include China.[65] It is seemingly normal that financial players like BlackRock have a longstanding relationship with China's leadership. Other Western financial players, including hedge funds, private equity firms, and investment banks have been active in China for years, and they tend to maintain contact with China's political class. These Western financial parties hope to increase their market size in China and wield significant political influence in Western capitals. The long-term relationship between the Chinese government and Goldman Sachs, and between Goldman Sachs and the US government is exemplary.[66] The Chinese state has actually held large and sometimes controlling stakes in several Western financial firms like Blackstone, HSBC, and

62 Rawi Abdelal, *Capital Rules. The Construction of Global Finance*, (Cambridge, MA, Harvard University Press, 2007), 162–195.

63 Thomas Hale and Hudson Lockett, 'FTSE gives China bonds green light for influential index Hudson Lockett,' *Financial Times*, 25 September 2020, https://www.ft.com/content/993d8154-f479-4412-954c-c9165c107c53; 'Bloomberg adds Chinese government bonds to flagship index,' *Financial Times*, 1 April 2019, https://www.ft.com/content/51562f9e-540f-11e9-91f9-b6515a54c5b1.

64 Steve Johnson, 'BlackRock calls for investors to lift allocations to China's markets,' *Financial Times*, 17 August 2021, https://www.ft.com/content/f876fb63-1823-4f4b-a28f-faa7797aa49c.

65 Christopher Balding, 'Buyer beware – MSCI is not a quality guarantee,' *Asian Nikkei Review*, 1 June 2018, https://asia.nikkei.com/Opinion/Buyer-beware-MSCI-is-not-a-quality-guarantee; Mike Bird, 'How China Pressured MSCI to Add Its Market to Major Benchmark,' *Wall Street Journal*, 3 February 2019, https://www.wsj.com/articles/how-china-pressured-msci-to-add-its-market-to-major-benchmark-11549195201.

66 Hank Paulson, *Dealing with China. An Insider Unmasks the New Economic Superpower* (New York, Twelve/Hachette Book Group, 2015); William Cohan, *Money and Power: How Goldman Sachs Came to Rule the World* (New York, Allen Lane, 2012).

Deutsche Bank.[67] Whether and how this translated into detectable Chinese political influence in these financial actors remains open to debate.

Nevertheless, such Western financial institutions and players can wield influence over the structure of the capital markets through political connections and lobbying. Such political influencing by financial sector parties could be economically beneficial if it were only conducted from a narrow market-efficiency perspective. However, if the lobbying of financial sector players also affects geopolitical dynamics disadvantageously to the national security of Western countries, such political influence of the financial sector is much less beneficial. The greater Western private financial interests in China become, the more dependent Western financial stability becomes on decisions made by the Chinese regime.

67 Sumeet Chatterjee and Matthew Miller, 'China sovereign fund exits Blackstone investment after 11 years,' *Reuters*, 14 March 2018, https://www.reuters.com/article/us-blackstone-group-cic-idUSKCN1GQ09T; Alec Macfarlane, 'Chinese firm becomes Deutsche Bank's biggest shareholder,' *CNN Money*, 3 May 2017, https://money.cnn.com/2017/05/03/investing/china-hna-deutsche-bank/index.html; Julie Steinberg and Stella Yiefang Xie, 'HNA, Under Pressure From Beijing, to Sell Its Overseas Empire,' *Wall Street Journal*, 7 September 2018, https://www.wsj.com/articles/chinas-hna-to-exit-deutsche-bank-stake-under-pressure-from-beijing-1536307095; Primrose Riordan, Hudson Lockett, Henny Sender, and Stephen Morris, 'HSBC shares rebound after China's Ping An increases its stake,' *Financial Times*, 28 September 2020, https://www.ft.com/content/5f6ca31f-310b-45e6–97fa-1db3bbcc8849.

Conclusion

This Working Paper sought to develop an idea about the interaction between financial, strategic, and geopolitical dynamics, especially in the context of contemporary 'great-power competition' or 'systemic rivalry' and 'hybrid conflict'. The key idea presented here is that countries have always been dependent on finance for their national security, but that the process of financialization has exacerbated the role of finance in the economy, and therefore also – indirectly – in national security. Furthermore, in recent years, it seems that the financial importance of China has increased, potentially giving Beijing greater influence, if not control, over international finance. Lastly, in countries like China and Russia, some strategists seem to have been actively pondering how to use finance as an instrument of power, going beyond the Western use of sanctions.

In most Western academic and policy approaches, financial-economic and strategic or geopolitical issues are kept separate. Thus, the current situation in which finance and geopolitical confrontation intertwine is 'new' in the sense that it differs from most of the more recent experiences and memories of the post-1945 and especially post-1989 eras. However, many elements of an older or historical pattern, stretching back to the rise of banking during the late Middle Ages, may be returning. That may not be good news, but it is a reality that must be dealt with and taken advantage of. Powers like Russia and China, which have less of a tradition of technocratic economic management, seem intellectually and structurally better prepared than most Western liberal capitalist countries to operate in a world where financial-economic and military-strategic or geopolitical issues are not separate, but merged.

The insights in this paper are preliminary and require further refinement, research and analysis to serve as a solid basis for policymaking and academic debate. Nonetheless, it should be clear that from a logical as well as an empirical perspective, financial-economic and geopolitical-strategic issues should be approached as being deeply interconnected, both in academic work and in policy. Not doing so may place Western countries at a significant strategic disadvantage in the face of competitors pursuing 'hybrid conflict' approaches.

The EU and NATO, as well as their member state and partner governments, should consider how they can move forward as finance and security dynamics become so intertwined.

First, this begins with further knowledge and capacity-building within governments and with academic and think-tank institutions, as well with relevant private sector parties. Adequate policies and responses to risks and threats depend on having a strong grasp of what is happening. Attention to operational issues like sanctions and FDI screening is crucial, but this should be coupled with a sustained effort to understand the broader dynamics.

Second, within governments, the defence and security parts and financial-economic parts of bureaucracy should develop strong communication channels with each other at all levels of policymaking, to facilitate both knowledge transfer as well as decisive policy responses.

Third, Western countries should calibrate their public-private relations with an eye to strengthening their financial, and economic, security. This includes renewed attention to the process and impact of financialization on the Western geopolitical position.

Overall, the EU and NATO are natural partners in the face of 'hybrid conflict' and financial geopolitics. The EU internal market, trade policy and the Eurozone give European policymakers economic, commercial, and monetary leverage at the global level. However, the stability of the European economy, and therefore the European economic leverage, is embedded in a military-strategic context over which the EU and its member states have very little leverage themselves – especially when it comes to more large-scale and intense conflict. Therefore, the EU's financial-economic leverage cannot do without NATO's military clout.

For NATO, as a predominantly military-strategic alliance, financial geopolitics seems crucial. Within NATO, the relationship between military-strategic and financial issues often centres upon the question of defence expenditure. While the financial sustainability of defence expenditure is a major part of the equation, NATO's relative military-strategic position depends on a broader set of financial dynamics, also affecting its technological edge as well as its broader military-industrial backbone. NATO's superiority is thus affected by public-private financing of innovation and technologies, the business dynamics in the defence industry, as well as spin-on effects between civilian and military technologies.

Ultimately, NATO's military potential and the US's global position are interconnected with Europe's economic relationship with China and Russia. One of the crucial questions is whether and how the politico-strategic relationship between the US and the EU will be affected by their economic and financial relationship with China and, to a lesser degree, with Russia. Europe and North America form the Atlantic Alliance, and this is also a necessary alliance of military and economic potential. If the European and North American economic paths diverge too much, or become dependent upon financing controlled by adversarial powers, the long-term consequences for the Alliance may be very negative. As the EU and the US seem to agree on many politico-strategic challenges and as they are searching for a common approach to them, they should seek to bring financial-economic aspects into line with the overall approach to hybrid conflict, security strategy, and geopolitical change.

Author

Dr Elmar Hellendoorn provides strategic advice and analysis on the interaction of geopolitics, global markets, and national security. For over a decade, he has been working for and with the Dutch government. He has also worked as a consultant across the public sector, and advises financial sector clients. Hellendoorn is a Senior Fellow at the Atlantic Council in Washington D.C. Previously, he has worked as an academic researcher at the Harvard Kennedy School's Belfer Center, the NATO Defence College, the European University Institute, Clingendael, and at Utrecht University.

Hybrid CoE

The European Centre of Excellence
for Countering Hybrid Threats