The Chinese Journal of International Politics, 2018, 237–270
doi: 10.1093/cjip/poy010
Advance Access Publication Date: 24 July 2018
Article

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Economic Openness and Great Power Competition: Lessons for China and the United States

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Abstract

The United States–China relationship is more likely than not to slide into economic and military competition, despite the perhaps best intentions of both states. This new bipolar competition is not inevitable. The key question is whether both governments have the self-restraint to limit domestic rent-seeking interests who will undoubtedly demand protection at home and exclusivity in their spheres of influence abroad. If not, the new superpowers will, like great powers in the past, 'race' for economic privileges that can quickly divide the world up into exclusive blocs. Like the security dilemma, great powers need not actually exclude one another from their economic zones; the fear of exclusion alone is enough to ignite the process of division. There was always some likelihood of a competitive economic spiral given China's close business–government relations in a 'state-capitalist' economy. Now, for the first time in seven decades, there is a chance that the United States, in the grips of economic nationalism, might abandon its historic policy of free trade and ignite a new race for economic privilege as well.

The debate about China's rise has focused largely on whether it is or will be a revisionist power.[1] Examining Beijing's actions and strategies for signals about its

1 For a review of the recent literature on US–China relations, see Yuen Foong Khong, 'Primacy or World Order? The United States and China's Rise—a Review Essay', *International Security*, Vol. 38, No. 3 (2013/14), pp. 153–75. On the debate on China's new assertiveness, see Alastair Iain Johnston, 'How New and Assertive Is China's New Assertiveness?', *International Security*, Vol. 37, No. 4 (2013), pp. 7–48; Dingding Chen, Xiaoyu Pu and Alastair Iain Johnston, 'Debating China's Assertiveness', *International Security*, Vol. 38, No. 3 (2013/14), pp. 176–83. On China and world order, see Randall L. Schweller and Xiaoyu Pu, 'After Unipolarity: China's Visions of International Order in an Era of U.S. Decline', *International*

future intentions is important. What it does today may suggest something about its plans for tomorrow. Too often, however, the issues over which China might challenge the current international order are left ambiguous or even undefined. The *purpose* to which China's rising power will be put is as much a question of theory as empirics. Without some analytic foundation that suggests when, where, and especially why we might expect China to challenge the existing regime, it is difficult to interpret current actions and policies. Moreover, since China's future policies will interact with the policies of the United States and others, we must take these actions into account as well. While there has been remarkable consistency in US policy during China's rise, relations are now being disrupted by the new administration of President Donald J. Trump with its economic nationalism and more assertive demand of 'America First!' Both sides of the coin need to be examined.

Drawing on a long history of theories and cases of imperialism, this article outlines an open economy politics (OEP) approach to great power competition that suggests the United States–China relationship is more likely than not to slide into economic and military competition, despite the perhaps best intentions of both peoples.[2] This new bipolar competition is not inevitable, contrary to the views of structural realists.[3] Structure is not destiny. Rather, if and when it happens, competition between the United States and China will be the result of decisions that could have been different. The key question is whether both governments have the self-restraint to limit domestic rent-seeking interests who will undoubtedly demand economic protections at home and special privileges in their international spheres of influence. There was always some likelihood of this in China, given close business–government relations in the state-capitalist economy. Now, for the first time in seven decades, there is a real chance that the United States, in the grips of economic nationalism, might abandon free trade in pursuit not only of

Security, Vol. 36, No. 1 (2011), pp. 41–72. For an assessment of how near term crises may derail a successful transition, see Avery Goldstein, 'First Things First: The Pressing Danger of Crisis Instability in U.S.-China Relations', *International Security*, Vol. 37, No. 4 (2013), pp. 49–89. On possible accommodation, see Charles L. Glaser, 'A U.S.–China Grand Bargain? The Hard Choice between Military Competition and Accommodation', *International Security*, Vol. 39, No. 4 (2015), pp. 49–90. On China's rise from a Chinese view, see Xiaoyu Pu, 'Controversial Identity of a Rising China', *Chinese Journal of International Politics*, Vol. 10, No. 2 (2017), pp. 131–49.

2 On OEP, see Jeffry A. Frieden and Ronald Rogowski, 'The Impact of the International Economy on National Policies: An Analytical Overview', in Robert O. Keohane and Helen V. Milner, eds., *Internationalization and Domestic Politics* (New York: Cambridge University Press, 1996), pp. 25–47; Robert H. Bates, *Open-Economy Politics: The Political Economy of the World Coffee Trade* (Princeton: Princeton University Press, 1997); David A. Lake, 'Open Economy Politics: A Critical Review', *Review of International Organization*, Vol. 4, No. 3 (2009), pp. 219–44.

3 Kenneth N. Waltz, *Theory of International Politics* (Reading: Addison-Wesley, 1979); John J. Mearsheimer, *The Tragedy of Great Power Politics* (New York: W. W. Norton, 2001).

protection for domestic industries but also preferential trade blocs. All it may take is for one of the two sides to move toward closure at home and in its sphere of influence for the entire geoeconomic system to fall. Indeed, given the Trump administration's recently enacted tariffs on Chinese goods, it appears that we are presently teetering on the edge of a precipice.[4] One wrong move by either party or both could result in a major trade war.

I develop two central arguments. First, historically, great power competition has been driven primarily by exclusion or fears of exclusion from each power's international economic zone, including its domestic market. Great powers in the past have often used their international influence to build zones in which subordinate polities—whether these be colonies or simply states within a sphere of influence—are integrated into their economies. These economic zones, in turn, are typically biased in favor of the great power's firms and investors, with the effect of excluding (in whole or part) the economic agents of other great powers. These other great powers, in response, are then compelled to develop or expand their own exclusive economic zones. The 'race' for economic privilege can quickly divide the world up into economic blocs. Like the security dilemma, great powers need not actually exclude one another from their zones; the fear of exclusion alone is enough to ignite the process of division.[5]

The race for privilege then draws great powers into overexpanding into unprofitable regions and, more important, militarized competition, which, in turn, leads to economic nationalism and closure.[6] Like chickens-and-eggs, economic and military competitions are linked, with each driving the other. The most significant military crises have, historically, been over where to draw the boundaries between economic zones and subsequent challenges to those boundaries. Economic closure and fear of closure have been consistent sources of great power conflict in the past—and possibly will be in the future. The major exception to this trend was the peaceful transfer of dominance in Latin America from Britain to the United States in the late 19th century. In this case, two potentially rival hegemons remained open to trade and avoided the economic and, then, geopolitical competition found in other cases of great power transition. This suggests that economic closure is a necessary if not sufficient condition for great power competition and that geopolitical conflict is not inevitable. Rather, competition is a choice made by the great powers at least in part through their economic policies.

4 Steven Lee Myers, 'Reply from Beijing Could Rattle Global Economy', *The New York Times*, 28 March, 2018.

5 On the security dilemma, see Robert Jervis, 'Cooperation under the Security Dilemma', *World Politics*, Vol. 30, No. 2 (1978), pp. 167–214. On how this dilemma can unfold through economic competition, see Dale Copeland, *Economic Interdependence and War* (Princeton: Princeton University Press, 2015).

6 On over-extension, see Paul Kennedy, *The Rise and Fall of the Great Powers: Economic Change and Military Power from 1500 to 2000* (New York: Random House, 1987); Jack Snyder, *Myths of Empire: Domestic Politics and International Ambition* (Ithaca: Cornell University Press, 1991).

Second, this international competition is driven, in turn, by domestic, rent-seeking groups and their economic interests. In all countries, including autocracies, scarce factors of production, import competing sectors, and domestically oriented firms have concentrated and intense preferences for market-restricting policies, including tariffs and the formation of exclusive economic zones. These intensive interests give protectionists stronger incentives to press for favorable policies regardless of regime type. Consumers and free trade-oriented groups have diffuse preferences for market enhancing policies and, thus, tend to have less influence in the making of national policy. This inequality in preference intensity does not mean protectionists always win; after 1934, the United States insulated itself by shifting authority to the executive and negotiating reductions through broad, multiproduct international agreements.[7] Yet, as the recent return to economic nationalism of the Trump administration suggests, protectionism often wins out. Rent-seeking is a central tendency, not an inevitable success.

Contemporary great power relations are at a critical juncture. As China's influence expands, the role of special economic interests in China is especially worrisome, manifested in state subsidies for high-tech industries of the future in which China is, otherwise, currently uncompetitive. In pursuit of stability, political support, or private gains, the government will always be tempted to create economic policies and, in turn, exclusive economic zones that favor its nationals. In this way, China will be no different than the majority of great powers before it. But, given the expansive role of the state in the Chinese economy, especially its backing of outward foreign investments by its state-owned enterprises (SOEs), and the close ties between business elites and its authoritarian political leaders, however, it will be even harder for China to resist biasing any future economic zone to benefit its own firms. Although China has gained greatly from economic openness, its domestic political system will be prone to rent-seeking demands by important constituents in areas of future influence.

Critically, the United States is also moving toward economic closure with the election of President Trump on a platform of economic nationalism. Demands for protection against Chinese goods have been growing over time.[8] The 'China shock' that followed Beijing's joining the World Trade Organization was a huge disruption to the international division of labor, US comparative advantage, and

7 Michael J. Hiscox, 'The Magic Bullet? The Rtaa, Institutional Reform, and Trade Liberalization', *International Organization*, Vol. 53, No. 4 (1999), pp. 669–98; Michael A. Bailey, Judith Goldstein and Barry R. Weingast, 'The Institutional Roots of American Trade Policy: Politics, Coalitions, and International Trade', *World Politics*, Vol. 49, No. 3 (1997), pp. 309–38.

8 Even a recent bipartisan working group on US–Chinese relations acknowledges the need for some reform and recalibration of the economic relationship. See Orville Schell and Susan Shirk, 'U.S. Policy toward China: Recomendations for a New Administration', Asia Society Center on US–China Relations and 21st Century China Center, School of Global Policy and Strategy, University of California, 2017.

especially US industry.[9] The Trans-Pacific Partnership, although now defunct, was promoted by President Barak Obama as a means of containing China, both economically and militarily, but was opposed by virtually all of the candidates in the 2016 presidential election for its trade-enhancing potential. President Trump has clearly adopted a more hostile and protectionist stance toward China—as well as calling for the repeal of NAFTA and even questioning the utility of the European Union. He has imposed tariffs on washing machines, solar panels, steel, and aluminum, dangerously declaring the latter two issues of national security.[10] Implicitly targeting China, these protectionist moves by the administration risk creating preferential trading blocs not seen since the 1930s. He has also now imposed punitive tariffs on over $50 billions of imports from China into the United States.[11] Acknowledging his inconsistencies on many policy issues, Trump's economic nationalism has remained the core of his political agenda. The threat to the liberal international economy is not only that China might seek an economic bloc in the future but also that the United States itself is turning more protectionist.

For each great power to fear that the other might seek to exclude it from its economic zone is not unreasonable. If so, great power competition could break out in the 21st century not because of bipolarity or any inevitable tendency toward conflict but because neither great power can control its own protectionist forces nor signal to the other that it would not exclude it from its economic zone. The British–United States case, again, suggests that exclusion and competition are not inevitable but the current danger of economic closure is real and increasing.

This article is synthetic in its theory and merely suggestive in its use of historical evidence. The theory aims to integrate current work on political economy and national security, not to develop a completely original take on this relationship. In turn, rather than testing the theory in any rigorous sense or delving into particular cases to show the theoretical mechanisms at work, so to speak, it surveys selected historical episodes to illustrate central tendencies. It is the recurring pattern across multiple cases which suggests why we should worry today. The rest of this article is divided in three primary sections. Section I briefly outlines the analytics of economic openness and great power competition. Section II focuses on historical instances of great power competition, highlighting the role of economic openness as a central cleavage in international politics. Section III examines contemporary policies in and between China and the United States. The conclusion suggests ways that the potential for conflict may be mitigated.

9 David H. Autor, David Dorn and Gordon H. Hanson, 'The China Shock: Learning from Labor-Market Adjustment to Large Changes in Trade', *Annual Review of Economics*, Vol. 8 (2016), pp. 205–40.

10 Jim Tankersley and Natalie Kitroeff, 'Shifting Strategy of Tariffs: Trump Administration Exempts Some Allies, but May Opt for Quotas', *The New York Times*, 23 March, 2018.

11 Mark Landler and Jim Tankersley, 'US Sets $60 Billion in Punitive Tariffs on Chinese Goods: Strong Trade Action Yet vs. "Economic Enemy"', *The New York Times*, 23 March, 2018.

The Open Economy Politics of Great Power Competition

All states have a tendency toward protectionism at home and exclusive economic zones abroad. Yet, a tendency is not an inevitability. The pursuit of protection and economic zones by domestic interests is conditioned by the political coalition in power at any given time and institutions that aggregate and bias the articulation of social groups.[12] The tendency is also influenced, however, by the actions of other countries. Protectionism can sour great power relations, but it is the desire for exclusive economic zones that drives great power competition and, given the possibility of coercion, influences grand strategy. Thus, the theory sketched here integrates insights from international political economy (see further), the literature on domestic politics and grand strategy,[13] and systemic theories of international relations.[14]

The political economy of protectionism within countries is well understood.[15] International exchange always has distributional implications, creating winners and losers. Scarce factors of production and industries that use those factors intensively, import-competing sectors, and small firms that lack economies of scale

12 On institutions and protectionism, see Ronald Rogowski, 'Trade and the Variety of Democratic Institutions', *International Organization*, Vol. 41, No. 2 (1987), pp. 203–23; Ronald Rogowski, 'Institutions as Constraints on Strategic Choice', in David A. Lake and Robert Powell, eds., *Strategic Choice and International Relations* (Princeton: Princeton University Press, 1999), pp. 115–36.

13 See especially Patrick J. McDonald, *The Invisible Hand of Peace: Capitalism, the War Machine, and International Relations Theory* (New York: Cambridge University Press, 2009); Kevin Narizny, *The Political Economy of Grand Strategy* (Ithaca: Cornell University Press, 2007).

14 Relevant here are neorealists who posit that (i) states will limit their dependence, see Mearsheimer, *The Tragedy of Great Power Politics*, or (ii) in ways similar to the trade dynamics explained further, expect states to anticipate trade restrictions, see Copeland, *Economic Interdependence and War*.

15 For an overview of open economy politics, see Frieden and Rogowski, 'The Impact of the International Economy on National Policies'. This synthesis builds off of "endogenous tariff theory" in economics, see Robert E. Baldwin, *The Political Economy of US Import Policy* (Cambridge: MIT Press, 1985); Stephen P. Magee, William A. Brock and Leslie Young, *Black Hole Tariffs and Endogenous Policy Theory: Political Economy in General Equilibrium* (New York: Cambridge University Press, 1989); Gene M. Grossman and Elhanan Helpman, *Interest Groups and Trade Policy* (Princeton: Princeton University Press, 2002). In political science, see Ronald Rogowski, *Commerce and Coalitions: How Trade Affects Domestic Political Alignments* (Princeton: Princeton University Press, 1989); Michael J. Hiscox, *International Trade and Political Conflict: Commerce, Coalitions, and Mobility* (Princeton: Princeton University Press, 2002). On firm-level, new trade theory, see Michael Plouffe, 'The New Political Economy of Trade: Heterogeneous Firms and Trade Policy', University of California, San Diego, 2013.

are the 'losers' from trade and favor economic closure. Consumers who benefit from cheaper imports and abundant factors of production, exporting sectors, and larger firms are the 'winners' and support free trade. With concentrated benefits from restricting exchange, known as 'rents', protectionists are typically more successful in solving their collective action problems than diverse consumers and exporters and are, therefore, better able to bring pressure to bear on their governments. Free trade tends to emerge only when abundant factors of production and export interests are mobilized into politics by the desire for access to foreign markets, especially when those markets are being held hostage to demands by the foreign state for access to the 'home' market.[16] It is the desire of US firms to gain access to Chinese markets, for instance, that has led them until now to weigh in against protectionists in the United States who would restrict imports from China. In league with consumers, free trade-oriented industries can win, but their victory is by no means guaranteed and is, in fact, historically rare. Some states have sustained coalitions of free traders, especially in small economies that must be open to trade.[17] Others have designed institutions to bolster free trade, as did the United States after 1934.[18] Yet, the concentrated benefits of restricting access to markets create a near universal tendency toward protectionism. Even at the height of free trade, for example, industries in the United States such as shoes, textiles, steel, and automobiles, lobbied successfully for international agreements (e.g. the Multifiber Agreement), voluntary export restraints, and other restrictions that limited import competition.

Trade policy has dynamic, long-term implications for political coalitions. Free trade increases the returns to the winners, leading to new investments in those industries and firms, expanding their weight in the national economy, and increasing their political importance and influence. Increased trade has the opposite effect on the losers, eroding their economic presence and political clout. Free trade, in the absence of technological change, leads to a virtuous cycle in which the losers are purged from the economy and, eventually, lose political influence.[19] Protectionism works in reverse, sustaining the size of comparatively disadvantaged sectors and firms and their political influence.

In turn, the openness of foreign markets has a similar effect.[20] As Rogowski has shown, anything that lowers the costs of trade, such as shipping, or foreign

16 Helen V. Milner, *Resisting Protectionism: Global Industries and the Politics of International Trade* (Princeton: Princeton University Press, 1988).

17 Peter J. Katzenstein, *Small States in World Markets: Industrial Policy in Europe* (Ithaca: Cornell University Press, 1985).

18 Hiscox, 'The Magic Bullet?'; Bailey, Goldstein and Weingast, 'The Institutional Roots of American Trade Policy'.

19 Oona Hathaway, 'Positive Feedback: The Impact of Trade Liberalization on Industry Demands for Protection', *International Organization*, Vol. 52, No. 3 (1998), pp. 575–612.

20 Scott James and David A. Lake, 'The Second Face of Hegemony: Britain's Repeal of the Corn Laws and the American Walker Tariff of 1846', *Internatonal Organization*, Vol. 43, No. 1 (1989), pp. 1–29.

barriers to trade will expand comparatively advantaged factors, sectors, and firms, and contract comparatively disadvantaged economics actors, and that anything that raises the costs of trade or foreign barriers to trade will shrink the comparatively advantaged sectors from what they might otherwise have been and expand the comparatively disadvantaged sectors.[21] In this way, the openness of foreign markets feeds back, if you will, into the relative strength of the political forces within the home country. When foreign markets are open, free traders benefit more and increase their political clout; when foreign markets are closed, free traders do not gain additional exports nor expand production at home for sale abroad, preserving the current distribution of political power within the society. Thus, the balance of political power within a society is influenced not only by the country's own policies but also the policies of others. This is important today in appreciating that free trade in either the United States or China expands support for free trade in the other, while protectionism will beget greater protectionism.

Less well understood is the desire to create economic zones in which great powers can use their influence to gain favorable trade and investment policies from subordinate states. The purpose of international power here is to gain privileged access to markets or, failing that, at least prevent others from gaining such access. By influencing with whom a foreign country trades and under what terms, a great power can create special access and rights that create rents for its factors, sectors, or firms, embodied in 'imperial preferences'.[22] In the absence of competition (or in the presence of restricted competition) from other countries, producers from the great power can charge higher prices for their exports to the target country or gain other advantages. When the great power and target country differ in comparative advantage—likely when countries differ in income—even import-competing firms in the great power can benefit from privileged market access for their otherwise comparatively disadvantaged goods. If the great power and target markets are sufficiently insulated from one another such that price differentials are not arbitraged away, even consumers in the former may not lose from higher prices; firms can still sell at cheaper prices in their domestic market but markup goods sold in the external economic zone.

With all or most of the great power's society benefiting from favorable access to the subordinate economy, there are strong incentives for national governments to exert influence to establish such zones—regardless of national political institutions. Here too, the benefits of restrictionist policies are concentrated in the less competitive factors, industries, and firms, creating intense interests in favor of and, thus, a central tendency toward exclusive economic zones. The economic

21 Rogowski, *Commerce and Coalitions*.

22 On the British imperial preference system, see David L. Glickman, 'The British Imperial Preference System', *Quarterly Journal of Economics*, Vol. 61, No. 3 (1947), pp. 439–70; Donald Macdougall and Rosemany Hutt, 'Imperial Preference: A Quantitative Analysis', *Economic Journal*, Vol. 64, No. 254 (1954), pp. 250–51.

gains for firms, in turn, may even offset the costs of establishing control over the target in a form of direct or indirect hierarchy.[23] The desire for favorable treatment in foreign markets can be very strong. As explained further, even Britain—the most liberal and democratic country in Europe during the 19th century—led the most aggressive and successful empire in world history.

Exclusive economic zones also affect the constellation of political forces within the home state. Free traders benefit from the opportunity to sell abroad in the exclusive zone but not as much as they might in a wholly open global market. To the extent competitors are excluded from the zone, protectionists may be able to increase exports as well, especially if domestic producers in the zone do not have a comparative advantage in the relevant sectors. This opportunity sustains the protectionists at home relative to a world of freer trade, maintaining a constituency in favor of expansion. This does not imply that countries always prefer exclusive economic zones. If free traders predominate in the political coalition, countries will eschew protectionism at home and exclusivity abroad for opportunities to trade widely with everyone, and when protectionists dominate at home, they will adopt restrictionist policies everywhere. But, in general, exclusive economic zones can be considered an extension of protection at home.

Because exclusive economic zones can benefit domestic constituents, and an exclusive economic zone by definition excludes or at least limits other great powers from trading with the countries of that zone, great powers will compete for these spheres of influence. Between the great powers and their peripheries, at least, trade ceases to be a multisum game and becomes a zero-sum competition. Indeed, given fears of exclusion, great powers may be tempted to preventively seize and close economic zones for their own benefit or to preclude them from being seized by others. Dale Copeland highlights these tendencies toward preemption in his 'trade expectations' theory.[24] If one great power defects and uses its influence to gain favored treatment in one foreign market, other great powers will retaliate and seek privileges in other foreign markets where they perhaps have greater influence. This can have the effect of transforming the world into increasingly exclusive economic blocs, as happened in the 1930s.[25] Indeed, as in the security dilemma, even the fear that a great power might seek to influence a target to give it special privileges can set off a preemptive 'race' for favored access, with each side seeking to lock-in a beneficial position before its rivals. The most famous case, of course, was the European scramble for Africa in the late 19th century

23 On the distributional consequences of the British empire, see Lance E. Davis and Robert A. Huttenback, *Mammon and the Pursuit of Empire: The Political Economy of British Imperialism, 1860–1912* (New York: Cambridge University Press, 1986).

24 Copeland, *Economic Interdependence and War*.

25 Barry Eichengreen and Doublas A. Irwin, 'Trade Blocs, Currency Blocs, and the Reorientation of World Trade in the 1930s', *Journal of International Economics*, Vol. 38, No. 1 (1995), pp. 1–24.

(see further). Although capitalist states that limit rent-seeking may be somewhat less prone to expansionism, as argued by Patrick McDonald, they are not immune from competitive rivalries, as the case of Africa attests.[26] Such preemptive races, in turn, can lead great powers into overextending themselves by grabbing targets in one form or another that are ultimately not worth the effort.

Once ignited, the formation of exclusive economic zones exacerbates all other dimensions of great power competition. Great powers compete for many reasons, including geopolitical influence beyond any economic motivation. My claim here is not that other sources of great power rivalry do not exist or that competition is driven entirely by the desire for exclusive economic zones. Rather, economic competition is a cause, an accelerant, and, perhaps, even a product of great power rivalry. As Jacob Viner posited seven decades ago, power and plenty are irreducibly linked.[27] As a practical matter, it is likely impossible to identify which came first—geopolitical rivalry or economic competition. In this 'chicken-and-egg' problem, protectionists can use nascent geopolitical rivalries to bolster their arguments for economic closure, and tendencies toward protectionism and exclusive economic blocs justify the skepticism of those who think rivalry is inevitable. It is through the pursuit of exclusive economic zones, however, that economic interests influence grand strategy. In competition for exclusive economic zones, which countries belong in which great power's sphere of influence starts to matter because they not only are necessarily valuable allies but also provide privileged access for one's own entrepreneurs or, at least, deny access to that of a rival.

Economic competition influences grand strategy and motivates the militarization of great power relations in three related ways. First, to create an exclusive economic zone requires concessions from subordinate countries. Target states will always want to diversity their economic partners, especially across the great powers. The monopoly rents earned by a great power through its exclusive economic zone come at the expense of the subordinate society. At the very least, the target country benefits by being able to play one great power off against others, giving it outside options that diminish the power imbalance at the negotiating table. The great power must, therefore, impose its will upon the subordinate state through coercive pressure,[28] in the extreme creating colonies it controls directly, as in 19th century European imperialism, or simply through the 'imperialism of free trade', such as that controlled by Britain in Latin America during the same period.[29] As in US imperialism in the early 20th century in Central America,

26 McDonald, *The Invisible Hand of Peace*. On capitalism and empire, see V. I. Lenin, *Imperialism: The Highest Stage of Capitalism* (New York: International Publishers, 1939).

27 Jacob Viner, 'Power Veruss Plenty as Objectives of Foreign Policy in the Seventeenth and Eighteenth Centuries', *World Politics*, Vol. 1, No. 1 (1948), pp. 1–29.

28 The costs of war or the use of coercive force here distinguish between core competition, against other great powers, and peripheral competition, against smaller countries central to Narizny, *The Political Economy of Grand Strategy*.

29 John Gallagher and Ronald Robinson, 'The Imperialism of Free Trade', *Economic History Review (New Series)*, Vol. 6, No. 1 (1953), pp. 1–15.

military interventions may be necessary to solidify its regional dominance through unpopular puppet governments.[30] The need to govern or control the subordinate state is particularly strong when site-specific investments such as plantations, mines, and infrastructure built on borrowed money are at risk.[31] Given the conflict between the great power that wants to control access and subordinate states that want the freedom to trade broadly, power is inherently at play.

Second, in addition to establishing control over local governments, a great power must actively exclude other great powers from the same region. It is not enough just to establish a special relationship with a state from which the great power seeks exclusive access, that power must also displace and deter potential rivals who seek entry.[32] In turn, those great power rivals may occasionally probe and challenge the first power's local control so as to disrupt its exclusive relations. Sometimes, these economic zones are negotiated among the great powers, as in Africa at the Berlin Conference of 1885 or in Europe at the Yalta summit of 1945. More often, however, great powers compete and periodically challenge one another's influence over target states, with the challenge sometimes escalating into military crises—especially during the Cold War. Thus, the great power must be prepared to project power into the region and defend its privileges in the exclusive zone. Without this ability, either the target state will slip from its grasp, as mentioned earlier, or be taken from it by a rival.

Third, a lack of clarity in the boundaries of economic zones and challenges to these boundaries as power and influence evolve make great power competition fraught and potentially dangerous. As theories of war tell us, uncertainty over capabilities, commitment, and resolve can lead to bargaining failures and uses of force.[33] These problems are particularly acute in peripheral areas where the interests of the great powers may be less unclear until challenged. This is an interesting type of conflict where the home government itself might not be fully aware of its stakes in a target until it is challenged, and its domestic firms and investors then lobby the leadership about the extent of their ties.[34] Moreover, the extent of their dependence can change over time as the relationship deepens, thus making it particularly difficult for rivals to assess the home state's resolve. In virtually all

30 A central theme of the Wisconsin school of historiography. See Walter LaFeber, *The New Empire: An Interpretation of American Expansion, 1860–1898* (Ithaca: Cornell University Press, 1963).

31 Jeffry A. Frieden, 'International Investment and Colonial Control: A New Interpretation', *International Organization*, Vol. 48, No. 4 (1994), pp. 559–93. This incentive for control is somewhat mitigated when investments are within integrated firms or global supply chains.

32 A monopoly is always less valuable when it is contestable. See Reinhard Selten, 'The Chain Store Paradox', *Theory and Decision,* Vol. 9, No. 2 (1978), pp. 127–59.

33 James D. Fearon, 'Rationalist Explanations for War', *International Organization*, Vol. 49, No. 3 (1995), pp. 379–414.

34 This is, I recognize, outside the usual bargaining model of war, which assumes each state knows its own costs of fighting relative to the issue in dispute.

historical cases, economic competition has escalated into military competition and crises, if not necessarily to war.

Great Power Competition in History

With the exception of the current period of unipolarity—now waning—there have always been multiple great powers seeking exclusive spheres of influence and privileged access to goods and markets. This section takes up illustrative cases not to test an inexorable law of international politics but to highlight the dangers and risks of economic closure. The focus is not only on the domestic sources of protectionism, documented in detailed histories elsewhere, but also on great power competition for exclusive economic zones.[35]

European Imperialism

The first era of overseas expansion, the so-called Age of Discovery, colonized nearly all of the Western Hemisphere, South and Southeast Asia, and ports along the African coast. This era ended with the American Revolution of 1776, which threw off the yoke of the British Empire, and the collapse of the Spanish Empire in Latin America between 1810 and 1825. Important below, Britain stepped into the void left by Spain's exit from South America, creating its empire of 'free trade'.[36] Most of the Caribbean remained under the control of various European states and locked into a highly mercantilist order until the early 20th century.

The drivers of empire are, of course, much debated.[37] The most comprehensive study of the economics of empire concluded that, at least in the case of Great Britain, it was a losing proposition for the country as a whole. The aggregate costs of empire far exceeded the gains. For particular groups of investors and traders, however, it provided clear benefits which were then shared among the well-connected political elites.[38] For other 19th-century imperial states, these distributional implications were likely magnified, especially as more exclusive economic relationships began to proliferate. Importantly, the British case shows clearly that the push for empire originated in and was made possible by the country's internal politics and institutions and not by any sound 'national interest'.

In the second half of the 19th century, a second wave of overseas expansion swept the globe. France, Germany after unification, tiny Belgium, and, later, Italy,

35 Among other sources, see F. W. Hirst, *From Adam Smith to Philip Snowden: A History of Free Trade in Europe* (New York: Adelphi, 1925); S. B. Saul, *Studies in British Overseas Trade, 1870–1914* (Liverpool: Liverpol University Press, 1960); Albert H. Imlah, *Economic Elements in the Pax Britannica: Studies in British Foreign Trade in The Nineteenth Century* (Cambridge: Harvard University Press, 1958); Percy Ashley, *Modern Tariff History: Germany—United States—France* (New York: Dutton, 1920); and Frank W. Taussig, *The Tariff History of the United States* (New York: Putnam, 1931).

36 Gallagher and Robinson, 'The Imperialism of Free Trade'.

37 See Michael W. Doyle, *Empires* (Ithaca: Cornell University Press, 1986).

38 Davis and Huttenback, *Mammon and the Pursuit of Empire*.

all joined Britain in the race for empire that played out mostly in the previously unclaimed areas of Africa. Although estimates are imprecise, especially for the earliest dates, the British empire grew from roughly 9 million square kilometers and 190 million people in 1826 to 22 million square kilometers and 250 million people in 1876 and to nearly 32 million square kilometers and 390 million people in 1913, on the eve of World War I. France's empire similarly grew from 1 00 000 square kilometers and 1 million people in 1826 to over 10 million square kilometers and 390 million people in 1913. With no colonies at all in 1876, Germany acquired nearly 3 million square kilometers and 12 million people, Belgium seized almost 3 million square kilometers and 7 million people, and Italy grabbed 1.5 million square kilometers and 2 million people by 1913.[39] The only territories outside of Europe that were never colonized are Ethiopia and Siam (presently Thailand). Even China was drawn into its Century of Humiliation and forced to grant 'concessions' in its coastal cities to nearly all the European powers.

The decades before World War I were the most economically interdependent in history, with trade, capital, and people moving across international borders at rates unrivaled until the 1980s.[40] This did not, however, preclude a race for empire. As interdependence expanded, the European powers also sought formal empires with exclusive economic control. This exclusivity, in turn, led to preemptive imperialism. Areas previously ignored by the Europeans because they were not suitable for settlement or lacked easily exploited natural resources or strategic locations were now seized by one state in fear that they would otherwise be grabbed by another.[41] Once incorporated into the exclusive sphere of a rival, it was feared, future access would be denied. Thus, Europeans ran hard to seize largely worthless territories that would be drains on their national treasuries to prevent others from possibly benefitting in the future from some as yet undiscovered value.

As part of these exclusive realms of control, the European powers created monopolies or quasi-monopolies for trade and investment. In part, this process of monopolization was a natural by-product of colonial control. A French entrepreneur, say, could invest in a French colony knowing that the investment was covered under French law: in cases of dispute, any claim would be heard in a French court and—if things went badly—political access to the power of the French state might be used to defend the claim. Even if the colony was in principle open to investors from all countries, national investors still enjoyed special privileges not available to others. This biased investment toward each national empire and, especially, the type of investments that were made.[42] As the race for empire

39 Paul Bairoch, 'European Trade Policy, 1815–1914', in Peter Mathias and Sidney Pollard, eds., *The Cambridge Economic History of Europe,* Vol. 8*: The Industrial Economies: The Development of Economic and Social Policies* (New York: Cambridge University Press, 1989), p. 105.

40 Kevin H. O'Rourke and Jeffrey G. Williamson, *Globalization and History: The Evolution of a Nineteenth Century Atlantic Economy* (Cambridge: MIT Press, 2000).

41 On 'systemic' theories of empire and the race for Africa, see Doyle, *Empires*.

42 Frieden, 'International Investment and Colonial Control'.

unfolded, however, the Europeans also began to demand increasingly attractive versions of imperial preferences on their goods. Where a uniform tariff might have been implemented, colonies increasingly favored their metropole with lower duties on goods, especially if carried on ships from the home country (navigation laws). Previously governed under Britain's policy of free trade, even the so-called White Dominions of Canada, Australia, and South Africa enacted preferential treatment for British goods soon after the turn of the 20th century.[43] Even though Britain did not reciprocate until the Great Depression of the 1930s destroyed the world trading system, even British trade was increasingly biased toward its empire. In 1913, when Britain accounted for approximately 14% of world trade, over 37% of its exports went to its colonies, and over 20% of its imports came from the colonies; the colonies, in turn, sent 42% of their exports to Britain and imported almost 46% of their goods from Britain. As suggested by the theory, the empire became the only site where British manufacturers prospered; everywhere else, they were overwhelmed by competition from more efficient producers in the United States and Germany. Its ostensible policy of free trade clearly did not prevent a strong imperial bias from emerging in trade flows.[44]

The Europeans did try to limit or at least regulate the competition for empire. As noted earlier, the Berlin Conference was called to divide up the unclaimed areas of Africa and elsewhere and to fix borders where they were unstated or ambiguous (in these cases, borders were typically drawn as straight lines on the map). This would, it was hoped, avoid conflict and misunderstandings as the Europeans moved further into the interior of the continent.[45] Bilateral deals were also made. Britain and France nearly came to blows at Fashoda at the headwaters of the Nile in 1898 but eventually pulled back. In the rapprochement that followed, Britain ceded Morocco to France in exchange for dominance in Sudan. This series of bilateral concessions began the reconciliation that eventually led to them to fight together against Germany in 1914.

Despite high economic interdependence and efforts to regulate competition between the European imperialists, tensions steadily grew, especially with the imperial 'latecomers' of Germany and Italy. Driven by their own rent-seeking groups, famously the coalition of Iron and Rye in the former, both had to squeeze their territorial ambitions into the few remaining vacancies between established claims by Britain and France.[46] It is likely too strong to conclude that this imperial competition caused World War I, although there is a long tradition of this type

43 Bairoch, 'European Trade Policy, 1815–1914', p. 113.

44 *Ibid.*, p. 127.

45 See Matthew Craven, 'Between Law and History: The Berlin Conference of 1884–1885 and the Logic of Free Trade', *London Review of International Law*, Vol. 3, No. 1 (2015), pp. 31–59.

46 Peter Gourevitch, 'International Trade, Domestic Coalitions, and Liberty: Comparative Responses to the Crisis of 1873–1896', *Journal of Interdisciplinary History*, Vol. 8, No. 2 (1977), pp. 281–313; Snyder, *Myths of Empire*.

of argument.[47] At the very least, however, the competition for exclusive zones that were increasingly closed to other countries was a contributing factor to the growing great power tensions that erupted at Sarajevo in 1914. As a worrisome preview of our possible future, high interdependence did not prevent economic competition from pulling the world apart and driving the great powers to global war.

Interwar Imperialism

The efforts to build privileged economic zones by Germany and Japan, precipitating World War II, are well known. Germany, in particular, posed the greatest threat to stability in the core of the international system since Napoleon. Japan threatened to overturn the East Asian order, already fragile given China's imperial decay. Less prominent in the traditional narratives—but highlighted by Dale Copeland's recent work—is that these efforts stimulated great power competitions and, even more so, were the product of fears on all sides that such spheres of influence would be closed to foreign economic competition.[48]

Although defeated in World War I, Germany never entirely gave up its imperial ambitions and, especially, its concerns over access to essential raw materials. World War II is clearly overdetermined, with too many sufficient causes to sort out the effect of any one factor. The draconian peace settlement at Versailles and the onerous reparations demanded by the victors, the Great Depression of the 1930s that helped bring Hitler to power, Hitler's own prejudices and megalomania, and more, are all possibly sufficient causes of the war. Equally, however, the war was also the product of great power competition for economic privilege, and especially fears of economic exclusion.

Early in the Nazi regime, Hitler not only called for *lebensraum* in the East but also began systematically redirecting trade and investment in Central Europe to its own interests and advantage.[49] Stimulated further by the collapse of the world economy after 1930, the spread of beggar-thy-neighbor policies and the growth of imperial preference systems, Germany sought a self-sufficient *grosswirtschaftsraum* (large economic area)—or an exclusive zone—as used here.[50]

Without an ability to export to depressed and closed markets, the free traders lost whatever political influence they might have had in Berlin. In the Four-Year Plan of 1936, imports were restricted to only those essential items that could not be produced within Germany, an important first step toward greater autarky.

47 J. A. Hobson, *Imperialism: A Study* (Ann Arbor: University of Michigan Press, 1965); Lenin, *Imperialism*; Nazli Choucri and Robert C. North, *Nations in Conflict: National Growth and International Violence* (San Francisco: W. H. Freeman, 1975).

48 Copeland, *Economic Interdependence and War*.

49 Albert O. Hirschman, *National Power and the Structure of Foreign Trade* (Berkeley: University of California Press, 1980).

50 On Interwar trade blocs more generally, see Joanne Gowa and Raymond Hicks, 'Politics, Institutions, and Trade: Lessons of the Interwar Period', *International Organizaiton*, Vol. 67, No. 3 (2013), 439–67.

The goal for Hitler was '100 per cent self-sufficiency … in every sphere where it is feasible'.[51] Without access to markets in Britain, France, and elsewhere, Hitler was convinced that the only safe option for Germany was an European empire. Once the war broke out, Germany's vision of an exclusive and closed continental empire fully played out, with the trade and investment of subordinate economies being redirected to and exploited by Berlin.[52] Although, again, the reaction of Britain, France, and eventually the United States to Germany's aggression in Europe is overdetermined, clearly, the attempt to create an exclusive economic zone that would fracture the world economy and exclude the eventual Allies from important markets was a major contributing factor to the conflict.

Japan's quest for empire in Asia is, of course, a complicated story with many nuances that are still debated today. In broad strokes, however, Japan was also a late entrant into the race for empire, seizing control of Taiwan in the first Sino-Japanese War (1894–1895) and Korea in the aftermath of the Russo-Japanese War (1904–1905)—formally annexing the peninsula in 1910.

Japan initially kept markets within its sphere relatively open. Indeed, in the struggle between Russia and Japan for dominance in Manchuria in the early years of the 20th century, Moscow more eagerly sought monopoly control of the region than did Tokyo. In its alliance with Britain in January 1902, Japan agreed to maintain the territorial integrity of China and Korea and, importantly, to secure 'equal opportunities in those countries for the commerce and industry of all nations'. The United States also supported this open door policy, lodging a protest in February 1902 against Russia's supposed plan to create an economic monopoly over Manchuria.[53] Japan continued to adhere to the open door after the Russo-Japanese War, including in areas of China where it was increasingly dominant. Seeking to avoid tensions, the United States signed (i) a secret agreement in July 1905 acknowledging Japan's 'suzerainty' or hierarchy over Korea, (ii) the Root–Takahira Agreement in May 1908 in which it and Japan agreed to respect the status quo in Asia, uphold the independence and integrity of China, and uphold the open door to trade and investment in the region, and (iii) a secret protocol in November 1917 that recognized Japan's special interests in China, in return for an affirmation by Tokyo of the open door principle.[54] So complementary were their interests, Steven Lobell argues that Britain treated Japan as its heir or proxy in Asia as it began to retrench in Europe following the Boer War and the rise of Germany.[55]

Improving economic conditions in the 1920s kept the peace in Asia, but the fragile equilibrium quickly broke down in the Great Depression with the passage

51 Quoted in Copeland, *Economic Interdependence and War*, p. 138.

52 On the German empire and how it worked, see Mark Mazower, *Hitler's Empire: How the Nazis Ruled Europe* (New York: Penguin Press, 2008).

53 Copeland, *Economic Interdependence and War*, p. 111.

54 *Ibid.*, pp. 150–2.

55 Steven E. Lobell, *The Challenge of Hegemony: Grand Strategy, Trade, and Domestic Politics* (Ann Arbor: University of Michigan Press, 2003).

of the highly protectionist Smoot–Hawley Act of 1930 in the United States and the retaliation that ensued. Japan's exports to the United States alone fell by more than 55% between 1929 and 1931. With its loss of US markets, Japan retreated into mercantilism, closing the previously open door in its areas of control and seeking out new exclusive markets in its Greater East Asian Coprosperity Sphere—a propaganda tool announced only in June 1940 but which reflected a policy in place from at least 1938. As Japan sought to expand further into China and Southeast Asia, President Franklin Delano Roosevelt (FDR) called for a 'moral embargo' on military equipment sales to Japan in 1938. A downward spiral of mutual hostility accelerated, with Japan blocking free navigation up the Yangtze River, establishing a new currency in northern China that favored Japanese imports, and creating new monopolies in China. After an American protest, Foreign Minister Arita Hachiro responded that the open door should apply everywhere or nowhere and that, since the United States and Britain already had zones that allowed for economic self-sufficiency, Japan was entitled to territory 'from which she could not be cut off by belligerent action of third powers'.[56] The United States, in return, adopted an export licensing regime to restrict sales of iron ore, scrap iron, and oil to Japan, which then expanded into a complete embargo on oil exports in July 1941.[57]

Who moved first and 'caused' the rise of exclusive economic zones in both Europe and East Asia is somewhat beside the point. Fear of closure was as important as closure itself. The actions and reactions by all sides served to close each country's sphere to the other and escalate the underlying conflict. These vicious spirals playing out on both ends of Eurasia ultimately ended in a catastrophic global war. Given the multiple causes, war may have been inevitable. Economic closure contributed to the war, but we cannot say for sure that war would have been avoided in its absence. The important lesson, however, is how economic closure both contributes to and accelerates great power competition. Once started, vicious cycles are extremely hard to stop.

Cold War Competition

After World War II, the United States and Soviet Union both developed exclusive spheres of influence in Europe and Northeast Asia. Each bloc was tightly closed to trade with the other. Together, exclusivity and closure contributed to a Cold War that raged for decades. The superpower competition also extended deep into the developing world but usually not with the clear lines of demarcation established in the Northern spheres. Disputes over the boundaries of their exclusive spheres and attempts to extend those spheres in new areas of the developing world catalyzed the most acute crises of the Cold War, leading the two superpowers to the brink of nuclear war over Cuba. This case illustrates the dangers of great power competition combined with economic closure and the risks such conflict can pose to the world as a whole.

56 Copeland, *Economic Interdependence and War*, pp. 176–7.

57 *Ibid.*, pp. 180, 86.

Although we often think of the Cold War as rooted in bipolarity, ideological rivalry, or Stalin's expansionist ambitions, the historiography on this case is complex and disputed. At least on the US side, early writers blamed the expansionism on communist Russia, while later 'revisionists' attributed primary responsibility to a series of US decisions—intentional or not—that threatened the Soviet Union and froze it out of an integrated or possibly neutral Europe. Postrevisionsists took a more balanced approach, pointing to the supposedly inexorable constraints of bipolarity and mutual misunderstandings. The more recent wave of post-postrevisionists, drawing on newly opened Russian archives, incline toward where the debate started, placing primary responsibility on Soviet Premier Joseph Stalin and his supposed quest for world domination.[58] This disputed history persists because there is an element of truth in each version, with really only a difference in emphasis separating perspectives.

Regardless of ultimate 'responsibility', upon defeating the Nazi regime, the Soviet Union and its massive military forces found themselves in control of Eastern Europe and the Eastern half of Germany itself, while the United States and its allies found themselves having liberated Western Europe and in control of the Western half of Germany. The passive voice here is intentional. Having fought a war against fascism, the victors, nonetheless, inherited control and responsibility for the continent and Northeast Asia; unlike the past and future cases reviewed here, these great powers incurred the costs of establishing control over subordinates for other reasons. These sunk costs then appropriately dropped out of the equation each calculated in deciding on its postwar strategy. Although exactly what was decided at the Yalta summit among President Roosevelt, Prime Minister Winston Churchill, and Stalin remains disputed, there is little doubt that each side generally understood that it would have primary responsibility for its own sphere of influence, at least in an initial postwar phase.

Likely going beyond the agreement, however, both East and West quickly sought to install proxy governments through which they could govern their respective spheres. The Soviet Union supported and, in some cases, installed communist regimes throughout Eastern Europe and its sector in Germany. Lacking significant popular support, the communists adopted autocratic, Leninist regimes and severely repressed opponents. Adopting the Soviet model of centralized economic planning, a degree of regional economic integration later emerged. The closure of the system was exemplified by the construction of the Berlin Wall in

58 One early view is George F. Kennan, *American Diplomacy, 1900–1950* (Chicago: University of Chicago, 1951). Principal revisions are William Appleman Williams, *The Tragedy of American Diplomacy* (New York: Dell Publishing, 1972); Walter LaFeber, *The American Age: U.S. Foreign Policy at Home and Abroad, 1750 to the Present* (New York: W. W. Norton, 1994). For a postrevisionist account, see Melvyn P. Leffler, *A Preponderance of Power: National Security, the Truman Administration, and the Cold War* (Stanford: Stanford University Press, 1992). A post-postrevisionist is John Lewis Gaddis, *We Now Know: Rethinking Cold War History* (New York: Oxford University Press, 1997); John Lewis Gaddis, *The Cold War: A New History* (New York: Penguin Press, 2005).

1961.[59] For its part, the United States promoted a liberal, capitalist, and democratic regime in West Germany under the leadership of Konrad Adenauer, assisted conservative parties throughout the West, and actively undermined communist parties in Italy, France, and elsewhere. When covert support threatened to be insufficient, communist strength in Greece was attributed to the meddling of the Soviet Union, prompting President Truman to articulate his famous doctrine. Through massive economic aid in the Marshall Plan, large troop deployments in Europe (first under the occupation and later under the North Atlantic Treaty Organization) and access to the US market through unilateral reductions in trade barriers institutionalized in the GATT, the United States built a regional order that was open for its members but excluded the Soviet Union and its subordinates.[60] The same split arose in Northeast Asia, with the Soviet Union establishing a local proxy in North Korea and the United States doing the same where its troops occupied territory, most prominently in Japan and South Korea.

The upshot of this series of decisions and moves by both sides, large and small, was the division of Eurasia into two economic zones that were open to members of each sphere but closed to each other. As in the other cases reviewed here, economic exclusion or fears of possible exclusion drove political hostility, and political hostility spurred economic closure, creating a spiral of economic and political competition that threatened to spill over into actual conflict. From the start, the United States fear of closure in the Soviet sphere contributed to suspicions of Stalin's motives and antagonism to communist rule. This is the kernel of the revisionist history that saw the United States demand for foreign markets driving the hostility toward the Soviet Union, to which Moscow then responded by consolidating control over its sphere. Unable to compete economically with the West and to consolidate control over states that lacked a natural political affinity toward Russia, the Soviet Union attempted to grab as much territory as possible and then actively excluded countries in the United States sphere; this is the core of the realist and post-postrevisionist interpretation of the Cold War. While the competition between the United States and Soviet Union was ultimately rooted in bipolarity, alternative ideologies, and unfortunate misperceptions, the closure of the two spheres toward one another was a central feature of the Cold War era that greatly exacerbated tensions between the two superpowers. Until Cold War tensions moderated in the 1970s under détente, little trade or investment crossed the East–West divide.

Although the boundaries of these spheres 'solidified' over time, the competition between the United States and Soviet Union remained intense. Indeed, virtually all of the Cold War crises identified in the international relations literature

59 A classic description of bloc politics is Zbigniew Brzezinski, *The Soviet Bloc: Unity and Conflict* (Cambridge: Harvard University Press, 1967).

60 Good overviews are Leffler, *A Preponderance of Power*, John Lewis Gaddis, *Strategies of Containment: A Critical Appraisal of Postwar American National Security Policy* (New York: Oxford University Press, 1982).

revolved around disputes over boundaries between the economic zones of the two superpowers. Of the 11 international crises directly involving the United States and Soviet Union during the Cold War, 7 were clearly stimulated by the struggle over where to draw the lines between their respective economic zones, with only the Suez crisis of 1956 being somewhat ambiguous and the two Arab–Israel wars being, at most, proxy wars (see Table 1).[61]

Most important, perhaps, was the Cuban missile crisis in which the Soviet Union not only sought to catchup in the nuclear arms race but, critically, also encroached on the traditional informal empire of the United States in the Caribbean. Cuba had long been an economic vassal of the United States, dominated by its landed elite in alliance with American investors. To overthrow the regime of President Fulgencio Batista, Fidel Castro also had to break free from the US economic zone. It was this defiance of US economic domination that led to the political hostility between Washington and Havana. In the bipolar world, however, the new regime appealed to the Soviet Union for support, which was readily given if for no other reason than to poke a sharp stick at the United States. When the Soviet Union introduced new missiles into Cuba in a radical attempt to solve its own strategic missile gap with the United States, relations between the superpowers reached a breaking point. Even after the removal of the missiles, the United States maintained a punishing sanctions regime on Castro's Cuba that ostracized its former colony—relaxing the sanctions 55 years later and restoring relations only in 2016, although this repeal remains contentious and subject to revision under President Trump.

Only when the lines between the two economic zones were drawn more clearly through such crises could the two superpowers reach a fragile détente. Even then, tensions remained as the two countries competed for influence and potential subordinates in Africa, switching sides in the conflict between Ethiopia and Somalia, supporting a proxy war between Western-back UNITA and Cuban-backed government forces in Angola, and, in general, supporting opposing sides in nearly every minor rebellion.[62] Détente itself was broken over the expansion of the Soviet Union in Afghanistan, previously in its sphere but then governed more directly after the invasion by a Soviet-backed proxy.[63] Relations worsened when US President Ronald Reagan appeared to endorse the old idea of 'rollback' and invested in placing intermediate range nuclear missiles in Europe. Although not every conflict of interest between the United States and Soviet Union revolved around the creation and defense of their respective economic zones, the question of where to draw the lines between their respective spheres of influence is a

61 Ray Takeyh and Steven Simon, *The Pragmatic Superpower: Winning the Cold War in the Middle East* (New York: W. W. Norton, 2016).

62 Odd Arne Westad, *The Global Cold War: Third World Interventions and the Making of Our Times* (New York: Cambridge University Press, 2007); Robert J. McMahon, ed., *The Cold War in the Third World* (New York: Oxford University Press, 2013).

63 Odd Arne Westad, ed., *The Fall of Detente: Soviet-American Relations During the Carter Years* (Oslo: Aschehoug AS, 1997).

Table 1. US–Soviet Crises during the Cold War (1945–1991)

Crisis	Inter-Hierarchy Boundary Issue
Azerbaijan (1946; ICB #108)	Withdrawal of Soviet troops from Iran
Korean War II (1950; ICB #133)	Entry of Chinese troops into Korean War with Soviet support
Suez-Nationalization War (1956; ICB #152)	Israeli, British, and French invasion of Egypt; then, an emerging client state of Soviet Union.
Berlin Deadline (1958; ICB #168)	Soviet demand that Berlin become a free or neutral city, under threat of turning East Berlin to the control of East German government.
Berlin Wall (1961; ICB # 196)	Erection of wall in Berlin
Cuban Missiles (1962; ICB #196)	Placement of intermediate range missiles in Cuba, former client state of the United States and, then, a client state of Soviet Union
Congo II (1964; ICB #211)	Soviet Union protested US–Belgian rescue of hostages held by Soviet-backed rebels
Six Day War (1967; ICB #222)	None
October-Yom Kippur War (1973; ICB #255)	None
War in Angola (1975; ICB #260)	United States backed the FLNA and Soviet Union backed the MPLA in Angolan civil war
Afghanistan Invasion (1979; ICB #303)	United States backed insurgents fighting against the Soviet-backed regime and Soviet military forces

Source: International Crisis Behavior Project, http://sites.duke.edu/icbdata/

surprisingly common thread running through what are sometimes interpreted as, otherwise, disparate events or crises driven by the mere fact of bipolarity. Indeed, it might not be an exaggeration to argue that the Cold War, from its origins to its very end, was a competition for exclusive economic zones driven not only by mutual fears of closure but also actual closure. Even if we do not attribute primacy to economic competition, there is no doubt that economic exclusion and fears of exclusion were important contributing factors to the bipolar conflict of the Cold War.

The Imperialism of Free Trade

The most successful and peaceful transition between great power-dominated economic zones occurred in Latin America in the late 19th and early 20th centuries between Great Britain and the United States.[64] This peaceful transition was made possible by the economic openness of both the fading British and the rising American spheres of influence. Britain ceded responsibility for maintaining regional order to the United States without fear of losing its market access. The United States, in turn, took on new responsibilities, assuming that political dominance

64 Stephen R. Rock, *Why Peace Breaks Out: Great Power Rapprochement in Historical Perspective* (Chapel Hill: University of North Carolina Press, 1989); Lobell, *The Challenge of Hegemony*.

would eventually create economic dominance and become self-sustaining. This case is crucial in showing how economic liberalism and the absence of competition for exclusive economic zones allowed for a peaceful transition of geopolitical leadership between the declining and rising hegemons. Although identifying the ultimate cause of great power conflict is difficult in the other cases examined here, this leadership transition at least suggests that competition for exclusive economic zones may be a necessary condition for geopolitical rivalry.

After the fall of the Spanish and Portuguese empires in Latin America in the wake of the Napoleonic wars in Europe, Britain came to dominate the region in what John Gallagher and Ronald Robinson famously called the 'imperialism of free trade', which remains the most apt description available.[65] The British navy dominated the seas, especially in the Atlantic, preventing any other European power from reinserting itself into the region. The United States boldly issued the Monroe Doctrine in 1823, which claimed the region for itself, but as widely acknowledged even at the time it wholly lacked the ability to defend this unilateral assertion and relied on Britain to humor the Americans and limit 'outside' influence.[66] The absence of other great powers in the region allowed Britain to exercise authority over the continent without any significant competition and, in turn, without the need to preemptively assert formal control over territories. This was the opposite of what occurred in the race for empire later in the 19th century.

In turn, Britain supported local Spanish elites who, in highly unequal political and economic systems, were vested in large cattle ranches in the Southern cone, plantation agriculture in more tropical zones, and raw materials extraction wherever it was attractive.[67] Britain's industrialization and voracious appetite for food and raw materials reoriented trade to London, increased the dependence of large landowners on the British market, and drew these elites into closer relations with Britain. In return, Britain found a willing outlet for its manufactures and investments. The net result was an open but informal empire that, nonetheless, systematically biased trade and investment flows toward British interests.

By the late 19th century, two trends converged to prompt the transition from Britain to the United States. On one hand, increased imperial competition elsewhere, especially in Africa, and great power competition within Europe itself after German unification led Britain to shed some of its regional responsibilities where partners existed who would be willing and able to maintain an open system. It tried to transfer responsibility to Japan in Asia, which eventually defected and started its own quest for formal empire as described earlier, but found just such a partner in the United States in the Western Hemisphere.[68]

65 Gallagher and Robinson, 'The Imperialism of Free Trade'.

66 Brian Loveman, *No Higher Law: American Foreign Policy and the Western Hemisphere since 1776* (Chapel Hill: University of North Carolina Press, 2010), chapter 2.

67 Kenneth L. Sokoloff and Stanley L. Engerman, 'History Lessons: Institutions, Factor Endowments, and Paths of Development in the New World', *Journal of Economic Perspectives*, Vol. 14, No. 3 (2000), pp. 217–32.

68 Lobell, *The Challenge of Hegemony*.

On the other hand, as the United States rose to global power status, Washington was looking to spread its wings and convert its growing influence into economic privileges. Expanding its navy, sending the Great White Fleet around the world in 1907, it finally acquired the ability to enforce the Monroe Doctrine, even against Britain, which it then used to squeeze out the remaining European powers that still had footholds in the Caribbean. Problems of regional stability arose mostly in the Caribbean and Central America.[69] Under the British system, the Southern cone prospered. By 1914, Argentina was the sixth richest country on earth *per capita* and politically stable. Only after World War I and the collapse of agricultural prices over the 1920s did the country fail economically, with real per capital income falling in absolute terms, and begin the cycle of political instability that has lasted through this day. Rather, it was in the Caribbean—much closer to 'home'—that political and economic instability threatened and to which the United States responded. The many islands and states on the Caribbean littoral were heavily indebted to European banks and frequently bordered on default. In the Spanish American War of 1898, the United States pushed Spain out of Cuba, its largest remaining imperial possession in the region (and from the Philippines, its largest possession in the Pacific). It then set about consolidating its dominion over other states. With its eyes on a transisthmian canal, President Theodore Roosevelt issued his famous corollary to the Monroe Doctrine in 1904, claiming an international police power over states that did not meet their international financial and other obligations.

The United States intervened militarily 20 times in states on the Caribbean littoral between 1898 and 1932.[70] These interventions were envisioned as limited and temporary military operations intended to restore the foundations for effective political order within the subordinate countries. As part of the larger strategy of building regional order, the United States also promoted—or at least tolerated—local proxies who governed in a dictatorial or authoritarian fashion—'our SOBs' as President Roosevelt famously described them. Typically drawn from the Spanish elite, these local strongmen governed to reinforce the status quo. Although generating substantial anti-Americanism as a backlash to US-supported authoritarian rule, by the 1930s, the region was sufficiently stabilized that FDR could announce the 'Good Neighbor' policy.[71]

As integration into the US market deepened in time, the economies of several Caribbean states, at least, evolved along the lines of comparative advantage to become either tourist destinations for Americans or light manufacturing export

69 On the early US informal empire, see Loveman, *No Higher Law*.

70 *Ibid*. On the response of Latin American states to these interventions, see Max Paul Friedman and Tom Long, 'Soft Balancing in the Americas: Latin American Opposition to US Intervention, 1898–1936', *International Security*, Vol. 40, No. 1 (2015), pp. 120–56.

71 Butt argues that the Great Depression led to less United States involvement in the region and more conflict. See Ahsan I. Butt, 'Anarchy and Hierarchy in International Relations: Examining South America's War-Prone Decade, 1932–41', *International Organizaiton*, Vol. 67, No. 3 (2013), pp. 575–607.

platforms. In either case, the benefits of economic openness and integration were gradually extended to the broader population. Today, with a greater convergence of interests between the average citizens of the subordinate states and average Americans, integration into the informal empire and democracy are no longer incompatible. Indeed, the Dominican Republic now has deep economic relations with the United States, solidified by the Central American Free Trade Agreement (CAFTA-Dominican Republic), and a popular pro-US and democratically elected government.[72]

As the United States assumed responsibility for political and economic stability in the region and extended its influence over the individual states, it maintained the openness of the regional order constructed under Britain. After the Spanish American War, it did not attempt to push out the remaining European colonies, several of which remain to this day. In consolidating debts and extending economic control over its subordinates, the United States did not seek special economic privileges for its exporters. After toying with preferential duties to be granted reciprocally in the 1890's, it abandoned the idea in favor of broad free trade.[73] As with Britain earlier, there was a systematic bias to trade and investment flows, but this appears to have followed from the effective enforcement of a regional order that made trade and investment secure than from any policies designed to intentionally direct flows to the advantage of the United States. The process of reorienting the economies of the region from Britain to the United States was gradual and incremental, rather than sharp and sudden.

It was this openness that likely made the peaceful transition from British to American hierarchy possible. Britain may have lost some its formal colonies in the region, but it did not lose access to established markets—although trade and investment patterns did evolve toward the United States over time. Moreover, its substantial investments and loans were guaranteed or, indeed, paid by the United States, which in turn assumed a major part of the risk. Openness allowed Britain to turn its attention to those regions where competition was more intense or in which it lacked partners to whom it could devolve similar responsibility. In return for keeping markets open, the United States was able to establish control over the region, especially on the Caribbean littoral, without competing with or, worse, fighting Britain. When compared with the other cases examined here, this successful transition appears anomalous—but it is an anomaly that presents us with an important lesson. If great powers are confident their rivals will keep a region sufficiently open to trade and investment, and especially if the declining power is

72 See Clare Ribando Seelke, 'Dominican Republic: Background and U.S. Relations', Congressional Research Service, Washington, DC, 2012. On CAFTA-DR, see Raymond Hicks, Helen V. Milner and Dustin Tingley, 'Trade Policy, Economic Interests, and Party Politics in a Developing Country: The Political Economy of Cafta-Dr', *International Studies Quarterly*, Vol. 58, No. 1 (2014), pp. 106–17.

73 David A. Lake, *Power, Protection, and Free Trade: The International Sources of American Commercial Strategy, 1887–1939* (Ithaca: Cornell University Press, 1988), chapter 3.

confident in the liberal intentions of the rising power, economic competition and, in turn, geopolitical rivalry can be avoided.

Great Power Competition in the 21st Century

If economic closure has been an important impetus to great power competition and, occasionally, conflict, what might we expect from the two great powers of the early 21st century: China and the United States? There are reasons for concern on both sides stemming not only from their great power status but also, especially, from their domestic economic interests.[74] The international economy today, of course, is not identical to that of the late 19th and 20th centuries. The United States and China are more deeply interdependent than past great powers. Not only are trade and financial flows larger overall than, say, between Britain and Germany prior to World War I, the last great period of interdependence, but the supply chains of the United States and China are also more intertwined than ever before. The disaggregation of production into discrete steps, and the global outsourcing of components and production, means that severing economic ties between the United States and China would be more costly than in past great power rivalries. Yet, as the high levels of interdependence before 1914 remind us, economic ties alone cannot prevent an unraveling of great power cooperation. In 2018, the two great powers of the 21st century are moving ever closer to a trade war that threatens to pull apart the world economy. The key question is whether both sides can resist demands from politically important and well-connected domestic groups for economic closure at home and exclusivity in their spheres of influence.

China

China only began to open to the international economy in 1978 under Deng Xiaoping. It joined the WTO in December 2001. Although its official trade restrictions are low and generally in compliance with WTO rules (but see further),

74 On the US–China rivalry, see note 1 and Aaron L. Friedberg, *A Contest for Supremacy: China, America, and the Struggle for Mastery in Asia* (New York: W. W. Norton, 2011); Mark Beeson, 'Hegemonic Transition in East Asia? The Dynamics of Chinese and American Power', *Review of International Studies*, Vol. 35, No. 1 (2009), pp. 95–112; C. Fred Bergsten et al., *China's Rise: Challenges and Opportunities* (Washington, DC: Peterson Institute for International Economics, 2009); William A. Callahan, 'How to Understand China: The Dangers and Opportunities of Being a Rising Power', *Review of International Studies*, Vol. 31, No. 4 (2005), pp. 701–14; Thomas J. Christensen, *The China Challenge: Shaping the Choices of a Rising Power* (New York: W.W. Norton, 2015); Martin Jacques, *When China Rules and World: The End of the Western World and the Birth of a New Global Order* (New York: Penguin Press, 2009); David C. Kang, *China Rising: Peace, Power, and Order in East Asia* (New York: Columbia University Press, 2007); Evan Braden Montgomery, 'Contested Primacy in the Western Pacific: China's Rise and the Future of U.S. Power Projection', *International Security*, Vol. 38, No. 4 (2014), pp. 115–49.

China's domestic economy remains relatively closed to outside traders and investors. Although it is just now reaching out and beginning to develop its own economic zones and it has not explicitly asked for nor received preferential treatment in any foreign market, China's intentions in these regions are not yet clear.[75] President Xi Jinping's Belt and Road initiative (BRI) is the most prominent attempt to build an economic zone, but the more diffuse role of China in Africa has some of the same qualities. The fear is that, extrapolating from its protection of Chinese industries and treatment of foreign firms in its domestic market, it will extend similar restrictions on access to these and future economic zones it may create. In understanding the future risks of great power competition, it is important to remember that it is not necessarily the reality but the perceptions of current and fears of future policy that can lead to devastating cycles of economic closure.[76]

Today, China's overall trade to Gross Domestic Product (GDP) ratio is relatively low at 37% (peaking at 65% in 2006, before the recession), with exports comprising about 20% of GDP and imports about 17%.[77] This is roughly in line with other export-led developing countries at similar stages of industrialization, such as Japan in the 1960s and South Korea in the 1990s.[78] In terms of bilateral trade, likely the most relevant signal to which US firms and political leaders pay attention, China is the third largest export market for the United States and, from 2006 to 2016, its most rapidly growing (expanding by 115%). China has also become a critical link in the global supply chain that feeds the United States with a host of products, not all manufactured in China itself. Nonetheless, imports from China have consistently exceeded US exports, creating a ballooning bilateral trade deficit that attracts much popular attention.

China's state-capitalist economy creates strong incentives for the Communist Party of China (CCP) and its supporters to pursue economic rents by restricting its domestic market to outsiders.[79] Government intervention in the economy

75 On China's regional free trade agreements, see Ka Zeng, 'China's Free Trade Agreement Diplomacy', *Chinese Journal of International Politics*, Vol. 9, No. 3 (2016), pp. 277–305.

76 For an insight into US fears, see Max Fisher and Audrey Carlsen, 'How the Rise of China is Challenging Longtime American Dominance in Asia', *The New York Times*, 16 March, 2018.

77 https://data.worldbank.org/indicator/NE.TRD.GNFS.ZS?locations=CN.

78 In their early stages of export-led growth, Japan's trade/GDP hovered around 20% in the 1960s and South Korea about 55% in the 1990s, placing China well within the range.

79 On China's authoritarian political economy, see Susan Shirk, *The Political Logic of Economic Reform in China* (Berkeley: University of California Press, 1993); Susan Shirk, *China: Fragile Superpower: How China's Internal Politics Could Derail Its Peaceful Rise* (New York: Oxford University Press, 2007); Jie Chen and Bruce J. Dickson, *Allies of the State: China's Private Entrepreneurs and Democratic Change* (Cambridge: Harvard University Press, 2010); Xiaoqin Guo, *State and Society in China's Democratic Transition: Confusianism, Leninism, and Economic Development* (New York: Routledge, 2003); Stefan Halper, *The Beijing Consensus: How China's Authoritarian Model Will Dominate the Twenty-First Century* (New York: Basic Books, 2010).

always lies on a continuum from pure market-based principles where governments act only to protect property rights, enhance competition, and solve clear market failures to politically based principles where governments set prices, property rights, and terms of competition to fit their own needs. Western democracies are far from pure market systems but lean in that direction. While China is far from a pure politically based system, it leans that way, allowing politics a greater role in allocating resources than found in Europe and North America.

Opening to the global economy has had the predicted effect in China of raising national income and benefiting the abundant factor of production, namely low-skilled labor. As underemployed labor has moved from agriculture to light manufacturing and other labor-intensive production, wages and standards of living for workers have increased dramatically. Yet, rents for scarce factors of production, mostly capital and human capital, and industries that use these scarce factors intensively abound within the Chinese economy. By running current account surpluses year-after-year through various explicit and implicit barriers to trade and investment, China eases pressure on otherwise comparatively disadvantaged industries; China's 'high tech' sectors, for instance, simply do not face the same import-competition they would otherwise without government restrictions, subsidies, and infringements on intellectual property. By suppressing consumer spending, in turn, China redirects at least some of the gains from trade to capital and capital-intensive industries. This has produced both more billionaires in China than in any other country in the world and bloated SOEs that survive on loans that may never be recovered. As China directs resources to industries of the future in its China 2025 scheme, new rents will be created in industries and firms that continue to be uncompetitive at home and abroad.

Although they are hard to estimate because so many barriers to trade and investment are implicit, behind-the-border restrictions, state-generated and directed rents appear to be high and pervasive. According to a recent report by the nonpartisan Congressional Research Service, although United States–China trade is recognized by most analysts as being mutually beneficial, there are significant tensions over a number of Chinese policies and practices that are 'protectionist, economically distortive, and damaging to US economic interests'.[80] In particular, US exports suffer from (i) an extensive set of industrial policies that aim to promote Chinese firms and sectors designated as important to future economic growth, especially SOEs, (ii) the targeting of US firms with anticompetitive investigations to limit market share, (iii) the failure to provide adequate intellectual property protections, (iv) a mixed record of implementing WTO obligations and, especially, the WTO's Government Procurement Agreement, and (v) currency manipulations to make imports of foreign goods less attractive, although this practice appears to have lessened in recent years. In addition to these nationally directed restrictions, provincial governments have imposed a host of trade

80 Wayne M. Morrison, 'China–U.S. Trade Issues', Congressional Research Service, Washington, D.C., 2015, p. 30.

restrictions to boost local industries and firms.[81] In recent talks, President Xi has promised to address some of these concerns, principally government procurement, but little progress is evident.

In similar ways, China is open to foreign investment in principle and by official policy but severely restricts actual inflows of direct investment. Although China is one of the world's top sites for foreign investment, it still imposes numerous restrictions on capital inflows, especially in sectors and industries deemed important to economic development and growth.[82] The United States–China Business Council has identified ownership barriers in nearly 100 industries, while the Organization for Economic Coperation Development ranks China as the most restrictive on foreign investment of the 57 countries it tracks 'based on foreign equity limitations, screening or approval mechanisms, restrictions on the employment of foreigners as key personnel, and operational restrictions (such as restrictions on branching, capital repatriation, and land ownership)'.[83]

State-capitalism is reflected in all aspects of the economy, but nowhere more clearly than in the still large SOEs, their tremendous debt-overhang, and the implicit guarantee of support by the government that enables them to engage in risky investments abroad.[84] In managing the economy for political purposes, rents are created for some firms and economic actors, especially SOEs that are 'too big to fail' and kept afloat because of this fact. On the other hand, many SOEs are less profitable than they might be and have accumulated mountains of debt because they invest not only according to market dictates but also for political reasons, building factories in less attractive areas that are politically important and hiring more workers than efficiency alone might dictate so as to absorb migrants from rural areas or curry favor with political leaders. In these cases, the 'rents' do not appear on the accounting books of firms but in the investments they make and maintain even in the face of more profitable alternatives.

The fear is that this same state-capitalist model will be extended to areas where China is wielding ever increasing influence, such as in BRI. Accustomed to state direction at home and often having close ties between major economic actors and the party, it will be hard for China not to privilege its own firms and investors in states within its sphere of interest. The same economic sectors that benefit from rents at home will seek economic privileges abroad through various preferential trade or investment arrangements. Comparatively disadvantaged, such sectors and industries cannot compete effectively on international markets against

81 Timothy P. Stratford, 'Measures and Practices Restraining Foreign Investment in China: Prepared for the European Commission Directorate-Generat for Trade', Covington & Burling LLP, Beijing, 2014, pp. 6–7.

82 On patterns and rates of China's inward and outward FDI, see Thilo Hanemann, Daniel J. Rosen and Cassie Gao, 'Two-Way Street: 25 Years of US–China Direct Investment', National Committee on US–China Relations and the Rhodium Group, New York, 2016.

83 Morrison, 'China–US Trade Issues', p. 25.

84 Weiyi Shi, 'The Political Economy of China's Outward Direct Investments', University of California, San Diego, 2015.

cheaper or higher quality goods from the United States or Europe and, thus, will seek special arrangements negotiated by the Chinese state that then shares in the rents. Even if future economic zones are not fully closed to international competition, the incentives of the CCP and its economic allies will be to manipulate market principles to their own political ends of bolstering trade and investment with China to sustain the high rates of growth necessary for domestic legitimacy. The bias in third-country markets will likely be significantly larger than that in, say, the US sphere today.

The current practices of SOEs may be particularly informative about how China may choose to manage its economic zones in the future. Here, we can see that the seeds of potentially more exclusive economic zones are already being sown through China's investments in politically unstable regions. In its quest for raw materials, China has encouraged SOEs to invest in site-specific assets in Africa, Central Asia, and elsewhere that are often too unstable and politically risky for private Western firms.[85] These investments, in turn, are implicitly guaranteed by the central government, shifting the risk from the SOEs to the state.[86] Coupled with the government's hands-off policy toward autocratic rulers and potential human rights abuses, China is now the major investor in many politically unstable countries. China need not consciously aim to exclude other foreign investors to gain a potentially privileged status over time. Similar arrangements are arising in big infrastructure projects in the BRI. As Chinese technology firms seek international markets, at least in the near term, state-led privileges will also have to be negotiated to offset current comparative disadvantages.

The greater the bias toward China in its nascent economic zones, the more the United States and other major traders will be excluded from subordinate state markets and the more likely they will be to oppose the creation of new Chinese economic zones. The greater the rents earned by China, in turn, the less the subordinate states themselves will gain from the economic relationship with China relative to more open competition, and the more they will resist being drawn into the Chinese sphere—perhaps by appealing to the other states now excluded from the zone. Excluding and restricting competition in possible subordinates is likely to lead other great powers and those subordinates to forge alliances or, more importantly, their own economic zones against China.

The road to great power competition is not foreordained, but it is the one more likely to be chosen as China spreads its wings. As noted earlier, reality is less important than the perception or fear of economic closure. China need not actually close its domestic market or economic zones for the West to respond as if

85 Fantu Cheru and Cyril Obi, 'De-Coding China-Africa Relations: Partnership for Development or (Neo) Colonialism by Invitation?', *World Financial Review*, No. 5 (2011); Tukumbi Lumumba-Kasongo, 'China-Africa Relations: A Neo-Imperialism or a Neo-Colonialism? A Reflection', *African and Asian Studies*, No. 10 (2011); Peter Ferdinand, 'Westward Ho-the China Dream and "One Belt, One Road": Chinese Foreign Policy under Xi Jinping', *International Affairs*, Vol. 92, No. 4 (2016), pp. 941–57.

86 Shi, 'The Political Economy of China's Outward Direct Investments'.

it has closed its markets. The simple perception that it might do so may be enough to spark a modern-day 'race for Africa' and beyond.

The United States

Until recently, it appeared that the United States itself and the US sphere more generally were likely to remain open to Chinese traders and investors. Although a source of concern for the United States about China's future sphere, countries always project their domestic political economies onto the international system, if possible.[87] Adapted to a liberal, market-oriented economy at home, the United States, its firms, and its investors created and thrived in a liberal market economy within the US sphere abroad. With large and politically influential interests around the globe and increasingly in China, US-based international business might be expected to lobby hard to maintain the liberal market-oriented economy if it were threatened by those who might otherwise seek to contain China. The United States could easily break its relationship with the Soviet Union and pursue containment because there were few economic ties between the two superpowers, even after World War II.[88] As noted, the United States and China today exist in a very different and far more interdependent world. Although its domestic political polarization and gridlock are often regretted, the large number of veto players in the US political system also make it hard to change policy and more likely to preserve the status quo.[89] This suggests continuity in US policy and continued liberalism, which should alleviate Chinese fears that the United States might close its market and economic zone in the future.[90]

Despite the deeply embedded liberalism of the Pax Americana, however, something changed in the United States (and across Europe) in 2016. A new backlash to globalization has spread across the West, exemplified in the strength of nationalist parties in Eastern Europe, the surprise vote in favor of Brexit, and, perhaps, most importantly the election of Donald J. Trump as President of the United States. The core of the Trump constituency is lower-skilled workers who have been especially hard hit by technological change and import competition, especially from the 'China shock' that followed from Beijing's accession to the WTO.[91] China's opening to the international economy is the single largest and fastest reallocation of

87 On 'waves' associated with different rising powers, see Seva Gunitsky, 'From Shocks to Waves: Hegemonic Transitions and Democratization in the Twentieth Century', *International Organizaiton*, Vol. 68, No. 3 (2014), pp. 561–97.

88 This was, of course, the critique Waltz offered of the interdependence school. See Waltz, *Theory of International Politics*.

89 Peter F. Cowhey, 'Domestic Institutions and the Credibility of International Commitments: Japan and the United States', *International Organization*, Vol. 47, No. 2 (1993), pp. 299–326.

90 For a balanced review of the issues and advice to the new administration, see Schell and Shirk, 'U.S. Policy toward China'.

91 David H. Autor, 'Skills, Education, and the Rise of Earnings Inequality among the "Other 99 Percent"', *Science*, Vol. 344, No. 6186 (2014), pp. 843–51; Autor, Dorn, and Hanson, 'The China Shock'.

comparative advantage in world history. Where past liberalizations occurred relatively gradually, as tariffs were negotiated downward by small increments, China's accession to the WTO liberalized one of the world's largest economies almost overnight, sending shock waves through other states. On the campaign trail, Trump mobilized workers displaced by technology and trade—and those fearful of further dislocations—by promising to build a wall in Mexico to prevent illegal immigration, to declare China a 'current manipulator' and impose a 45% tariff on Chinese goods, and to pull out of or renegotiate existing trade agreements, including the Transpacific Partnership (TPP) and NAFTA. With the Democrats also inclined toward protectionism—even Hillary Clinton eventually came out against the TPP which she had supported as Secretary of State—a protectionist coalition in Congress that seeks to revise US policy is certainly possible, despite possible opposition by the traditional Republican establishment.[92] The Trump administration has clearly moved in a significantly more protectionist direction by imposing tariffs on washing machines and solar panels and, claiming a threat to national security, on steel and aluminum. Significantly, selected allies were initially exempted from these tariffs, giving the unmistakable impression that there is a double-standard for favored friends and 'economic enemies'. The Trump administration has also imposed punitive tariffs on a range of imports from China and threatened even more if China retaliates.

Banning the sale of computer chips to Chinese manufacturer ZTE also suggests the extent of economic competition between the two countries. The case is, of course, complicated. ZTE was originally punished for selling regulated technologies to Iran and other prohibited markets. The ban was imposed for the firm's failure to abide by the terms of the earlier settlement. Under pressure from China, the ban was then removed and ZTE agreed to a further fine, stoking the ire of both Democrats and Republicans in Congress who—combining both protectionism and security concerns—may still insist upon a complete ban on sales to the company. The upshot of this imbroglio, whatever its eventual outcome, is strong evidence of rising economic tensions between the two great powers.

Similar trends are apparent with Chinese foreign direct investment in the United States.[93] Chinese FDI in the United States reached an all time high in the first six months of 2016, nearly triple the amount from the equivalent period one year earlier. In turn, a large number of investments, especially mergers and

92 On the wreck of the TPP, see Gardiner Harris and Keith Bradsher, 'China's Influence Grows in Ashes of the Trans-Pacific Trade Pact: A Rival Deal Gains Traction', *The New York Times*, 20 November, 2016. Yet, even here, the Republican establishment may be cracking. See Mark Landler, 'As Xi Tightens Grip on China, Washington Sees Conflict Ahead', *The New York Times*, 28 February, 2018.

93 See Dustin Tingley, et al., 'The Political Economy of Inward FDI: Opposition to Chinese Mergers and Acquisitions', *Chinese Journal of International Politics*, Vol. 8, No. 1 (2015), pp. 27–57.

acquisitions of existing US firms, have come under more intense scrutiny from the Committee on Foreign Investments in the United States (CIFUS). In February 2016, CIFUS officials reported that 68 of 358 deals reviewed involved China, making it the single largest target of its scrutiny. Several significant deals were scuttled after CIFUS raised objections.[94] Under President Trump, we can expect more rigorous reviews and more rejections, although this has not yet been a focus of his activity. Noteworthy, however, was the administration's blocking of Broadcom's bid for Qualcomm, the leading maker of telecommunications chips in the United States and an innovator of the 5G network. Although Broadcom was based in Singapore, this was a telling sign of the administration's willingness to use national security as a ruse for its economic nationalist agenda.

Although President Trump has softened some of his anti-globalist rhetoric from the campaign and offered China a 'better deal' on trade if it helps with North Korea, there is no doubt that the United States is turning in a more protectionist direction. There are real concerns about Chinese trade and investment practices that underlie some of these moves, and even some free trade stalwarts within the Republican Party have applauded the effort to 'get tough' with Beijing. If the punitive tariffs and the singling out China as an 'economic enemy' is just a negotiating ploy, this will be a risky but, perhaps, not entirely unwarranted move. Better, in the views of many administration critics, would be to rally other countries facing similar restrictions on trade and investment in China, especially the Europeans, and to negotiate as a united front. Moreover, preferred would be to operate through the WTO and its dispute resolution mechanism. If the Trump administration truly wanted to negotiate a better deal with China, these would have been reasonable first steps—with unilateral tariffs held in reserve if agreements could not be reached. That it has not pursued these options suggests that simple protectionist motives may be at play. Chinese fears about a closing US market in the future would not be unreasonable.

At the same time, each may fear that the other is seeking to develop an exclusive or, at least, privileged economic zone. The United States worries that it may be shut out of markets developed under the BRI. China may now worry that US allies and friends will be treated more favorably. With both the United States and China possessing legitimate fears about the future economic openness of the other and their economic zones, the risk is that each might begin to close its zone in anticipation of closure by the other. Despite unprecedented levels of interdependence, the open international economy could rapidly unravel, sparking a new, 21st century great power competition over exclusive economic zones.

Conclusion

Unlike the extreme views of conservative or liberal commentators within China or the United States, neither conflict nor cooperation is inevitable. How relations

94 Ellen Sheng, 'As Chinese Investment in US Increases, So Too Does Scrutiny', *Forbes*, 2 November, 2016.

fare in the future is still very much contingent on the choices of both states. If China demonstrates through practice a commitment to economic openness, the US reaction to China's rising influence in world politics is likely to be more favorable and accommodating. If the United States under the more nationalist Trump administration eschews protectionism, China will be less fearful of losing its principal market as well. Given the mutual suspicions of the United States about a China that cannot commit to openness within any future economic zone and China about a United States that may itself turn protectionist, however, the risk of great power competition is always present—and growing.

Given the risk of economic closure, what can each great power do to reassure the other and avoid the potential for great power competition? On the China side, Beijing should, first, liberalize its domestic market not only in name but also in practice. It should take seriously complaints by US firms about nontariff barriers to trade, especially its discriminatory practices that privilege national over foreign firms. Doing so would not only signal its benign intent to the United States and its commitment to the free movement of goods and capital across borders but also possibly reduce the ties between Chinese firms and the government that encourage the political manipulation of market incentives.

Second, China should build investment consortia in areas where it is increasing its political and, by implication, economic influence. Instead of carving out special niches for Chinese firms and investors, China should encourage joint undertakings with Western firms. Given its prominence in recent political disputes, a very important signal of its commitment to openness, for instance, would be to open the South China Sea to bids on mineral rights from Western firms or joint Western/Chinese investment consortia. China should also encourage joint investments in Central Asia and other regions of the BRI. Such joint undertakings would be a powerful signal that, despite its rising influence, China will remain committed to economic liberalism.

On the US side, the Trump administration should refrain from protectionism at home and preferential exemptions from protectionism when it is necessary. Although the president needs to deliver for the rust-belt constituency that supported him, getting 'better deals' on trade and investment risks setting off retaliatory trade wars. That any existing agreement might not be 'perfect' from the perspective of the United States will not prevent China from drawing negative inferences about future economic policy if such pacts are abandoned. To repeat, the fear of closure may be just as dangerous as actual closure. A degree of caution by the administration is essential, as history suggests that the slope toward conflict is slippery indeed—and well-greased by current political sentiments. This is not to suggest that the United States should not use the economic levers available to it to create a fair and equitable market, but antidumping and currency rules should be used only when valid and appropriate and not just to satisfy protectionist interests.[95] Finally, the United States should continue to encourage China to become a 'responsible partner'. This includes participating in Chinese initiatives.

95 Schell and Shirk, 'U.S. Policy toward China'.

President Obama made a potentially catastrophic mistake in opposing the Asia Infrastructure Investment Bank. When China reaches out to the United States and others to join it in developing international markets, the United States should participate fully.

Finally, each of this century's great powers must recognize that they are, in fact, interdependent, not only economically but also politically. As in physics, every action has an opposite reaction. The great powers must coordinate their industrial policies in such an interdependent system. To date, China still appears to act as if it is a 'small' economy whose policies do not affect the international economy as a whole. The China 2025 program, aiming to upgrade China's technological capabilities, is a noble and essential policy, but it will carve away another layer of comparative advantage in the United States, setting off another round of job displacement. The program will do little good if China's technological progress creates a protectionist backlash that closes the US market to its exports. China needs to think ahead not only economically but also politically. The United States, in turn, needs to reform its domestic political economy to embrace international change. It must expand worker-retraining programs, facilitate relocation of workers from geographic areas dominated by import-impacted industries to regions with expanding opportunities, and it needs to invest further in human capital and technology, its newest forms of comparative advantage. Protectionism looks backward to preserving the status quo. Rather than seeking to hold onto the past, the United States, like China, must look to the future.

Nothing is inevitable in world politics. But, if China does choose openness over closure and the United States eschews protectionism, we may be able to forge a new global order that avoids great power conflict and competition. The British–United States transition is a hopeful analogy and not entirely implausible. Economic openness makes passing the baton of leadership considerably easier. But, there are more ways for the rise of Chinese power in the shadow of declining US power to go badly than well. Both sides to the relationship face important domestic constituencies who will advocate for special economic privileges that put the overall relationship at risk. But as suggested by the British–United States case, there is at least a path to separate but open spheres that can accommodate two great powers in the future. This truly is a future worth striving for.

Acknowledgements

I am grateful for financial support from the 21st Century China Program at the University of California, San Diego, and comments by Jeff Frieden, Steven Lobell, Susan Shirk, and two anonymous reviewers.