

THE

G-ZERO

Investors face "a period of dramatic geopolitical disorder," says political risk expert Ian Bremmer

By Nathan Jaye, CFA

WORLD

Geopolitical awareness may be more crucial than ever for the savvy investor. A leadership vacuum in international affairs has not only increased instability and uncertainty but will continue to do so for the next 10 years, according to Ian Bremmer, president and founder of Eurasia Group, a global political risk research and consulting firm. The author of *Superpower: Three Choices for America's Role in the World* and *Every Nation for Itself: What Happens When No One Leads the World*, Bremmer describes the current situation as a G-Zero world (where no country is willing or able to set the international agenda). In this interview with *CFA Institute Magazine*, Bremmer discusses the implications of geopolitical disorder, his outlook for key regions and countries, how to prepare for fat-tail events, and the importance of "pivot states."

Are we seeing an unraveling of the current world order?

This is an historic time for the G-Zero. The United States does not want to be the world's policeman, and nobody else wants the job. Globalization continues; Americanization does not. We're seeing this play out most obviously in the Middle East and North Africa. We're also seeing it in the undermining of Ukrainian sovereignty by the Russians.

The Syrian refugee crisis, the rise of ISIS, and the lack of any effective individual or collective response—all of this is an outcome of a geopolitical order that is no longer American led.

It's not multipolar either. Multipolar implies that there are a bunch of global powers that are

competing for influence. There aren't a bunch of global powers. There's the Americans, who are doing less. There's the Chinese, who are challenging the US economically but not militarily or diplomatically, not even close. Everyone else is paying attention only to their backyard. That's where we are.

What lies ahead?

I think the G-Zero is really an interregnum between the old US-led order and something else. We're not sure what that something else is yet. It could eventually be a G-2 between the US and China if the Americans and Chinese can harmonize their relations and learn to work together. Or it could become a new Cold War if the Americans and Chinese end up in a much more conflictual, zero-sum relationship.

We could see something that looks more like international governance (more like a true G-7, G-10, G-whatever) if the importance of countries like India and Germany grows in relation to the US and China and if the response to global problems like refugees, terrorism, and climate change ends up being more collective.

Or it could become a world of regions, where you see different local hegemonies and very different standards, very different sets of norms and values that don't necessarily translate into anything global. To be very clear, the G-Zero is going to persist. I don't see it going away for at least another 10 years.

What does this mean for investors?

It means a greater flight to stability and safety in a period of dramatic geopolitical disorder. Again, that period is just starting. It's not something we've really experienced in the past few years. It means gold does well, but more importantly, the Americas, the United States, the Western Hemisphere as a whole look geopolitically stable and insulated from many of the other problematic trends we see in the world.

Japan, which doesn't grow, nonetheless looks a lot more resilient as a society and as an economy than many other countries. They've got a higher debt-to-GDP ratio than Greece. But you'd never know it in terms of their stability.

The quality of global growth is going to be lower, which means if you're seeking growth return, you have to recognize that the risk you're taking on is going to get much larger. That's clearly going to be true when China becomes the largest economy in the world in the next 10 years.

Is Russia getting stronger or weaker?

I think that Russia is in decline as a power. Economically, it's not growing. This year, it's shrinking by 4%. It's largely a petro-state, and oil prices are going to stay low. Russia has not been able to diversify its economy. It has not been able to attract significant investment. There have been demographic challenges and a huge brain drain.

When you look at the BRICs, Russia really doesn't belong in that category. It's not really an emerging market at this point. Yet Russia occupies enormously important strategic territory, and it also has one of the world's largest militaries, which it is willing to use. I believe Putin is the single most powerful individual in the world. Even though Russia is getting weaker, the ability of Putin as an individual actor to disrupt the international order is significantly greater today than it was 10 or 15 years ago.

What are possible fat-tail outcomes in the Middle East?

Medium term in the Middle East, one would be a major terrorist incident in Saudi Arabia that could destabilize that regime. The Saudis remain a crucial energy producer, and their government is deeply dependent on energy revenue. That is a serious problem, especially as they start to feel the economic pinch of lower energy prices, greater security demands, and an expanding population that isn't very [economically] productive.

Another is the metastasis of the Syria conflict, with more refugees leading to additional failed states—potentially Jordan and Lebanon—given the refugee burdens. The potential of a Turkey–Russia war breaking out over Syria, that would be another fat tail.

How can investors prepare for fat-tail events?

Fat tails are not black swans. Fat tails are things that you actually recognize as having a significant chance of happening. There's a much more significant chance of Grexit [Greece exiting the European Union] now than there was six months ago. If you're a financial institution, you now need a plan for that. A fat tail is something you actually need to plan for.

So, number one, you have to understand: "Were *this* to happen, what steps will I take?" You have to actively think it

through. You need contingencies in place. Two, you actually need a set of checkpoints. Fat tails are things you can assess. For example, what are the events that would suddenly make these fat tails my baseline expectation? You should be actively monitoring for those things. Three, if they occur, you should start taking some of the steps in your contingency [plan].

In your book *Superpower*, you write about Independent America. What's that?

In the book, I wrote about three leadership choices for America: Moneyball America, Indispensable America, and Independent America. Moneyball admits we can't meet every international challenge and we need to prioritize. Indispensable argues that it's in America's interest to be the global policeman. Independent says we're not going to do that; instead, we focus on our own problems and lead by example. When I wrote the book, I didn't know which one I would support. I ended up picking Independent America.

Independent America focuses more on itself and building its own economy and therefore being much more of a beacon for other countries. Hopefully, that includes an immigration beacon, because immigration makes America stronger.

You've said America is asking what it stands for. Can you elaborate?

When you ask our allies around the world, they'll tell you they don't know what America stands for. They don't know what we're committed to. We ourselves know what we *don't* want. We don't want to fight in Iraq and Afghanistan. We don't want to put boots on the ground all over the place. We don't want to pay for NATO if our allies don't want to do it.

So what *do* we want? What do we stand for? Do we want to promote democracy? Do we want to promote human rights? Do we want to promote a global free market, or do we not? Does the Statue of Liberty matter? Do we believe that it's important to continue to offer a haven for immigrants all over the world to come to the United States to integrate no matter what their accents, no matter what their backgrounds? We don't know. Americans have no idea.



What's more problematic for Europe: a eurozone crisis or a refugee crisis?

They're connected, but the refugee crisis is more important because it's structural. The refugee crisis undermines the ability of countries in Europe to react, to have any form of leadership. It's undermining [German chancellor Angela] Merkel. It's undermining the Schengen Agreement and, as a consequence, the common market. There's an agreement on 160,000 refugees to be resettled. It sounds great. But once you resettle them, if they have free passage within countries, how are you going to get them to stay in a country they

don't want to be in? The refugee crisis, especially because it's only going to get worse, is a fundamental challenge to governance in Europe. It makes Grexit more likely. It undermines German leadership. It creates populism and xenophobia across Europe. It undermines the social contract that the European Union is actually founded on.

Syriza ["the Coalition of the Radical Left"] won the Greek elections again. What does this mean?

It means that Greece is a democracy and it just experienced a depression. Therefore, they've decided to vote for something that's other than what they had. The establishment in Greece had enriched itself. So, even though Greeks support staying in the eurozone and staying in the EU, they came out very heavily for Syriza. The Germans were pushing a very tough deal down their throat, and Tsipras said, "Give me your mandate." They gave him the mandate. After they implemented that and they're taking more pain, Syriza had another vote and said, "Vote for me." And they all voted for [Tsipras] again. It's not a surprise.

Does it change anything in terms of Grexit?

Grexit was a possibility only by accident. There was never going to be a likely Grexit because all of the elites across Europe wanted the Greeks to stay in. I was saying that consistently. I hold to that.

What are pivot states, and why are they important?

Pivot states are good at building relationships with multiple major powers. We don't have the US creating global standards the way it used to. Pivot states are very important, particularly in Asia, where you have a strongly rising China, and also in parts of the world where the Chinese are playing a very, very big economic role.

Countries that are able to work with lots of different partners, with lots of different political and economic systems, are very important. Part of the reason the Middle East is falling apart is that it has no pivot states. You're on one side or you're on the other, and you're fighting. That's a serious problem. Whereas in Asia, India is a pretty effective pivot state. They can work with the Americans. They can work with the Japanese. They can work economically with China. That's pretty good.

Singapore is an amazing pivot state. It's doing very well. In the Middle East, only the United Arab Emirates acts as a pivot state. It works with the Saudis and the Iranians. As a consequence, it's doing comparatively well.

What does the future hold for China?

It's certainly going to become the world's largest economy. Over the next few years, I don't see huge instability in that country, despite the market perturbations. The real question is what are the longer-term issues? Because when China becomes the largest economy, it will be by far the most volatile in the world of major economies. China has huge challenges coming down the pike, whether it's environmental or demographic or demands for political reform and a greater voice that come with becoming a

consumer-led economy with an open financial marketplace.

Those are big issues, and the Chinese government can forestall all of them. They can kick them down the road because of the consolidation of power that [President] Xi Jinping has managed to pull together. But there are potential scenarios for China as we look 10–20 years down the line. Does it continue to reform? Does it become a more advanced industrial economy that's more aligned with the United States? Does it become much more xenophobic, much more nationalist, or does it fall apart?

Does the US-China cyber-agreement have any teeth?

No one I've spoken to in the Obama administration feels like it's going to prevent the Chinese from engaging in attacks against American firms for critical intellectual property. I think you could drive a truck through some of the legal interpretations of the deal that was actually signed, especially because we're talking about the private sector. Chinese companies are owned by the state. Therefore, they have a different definition of national security.

I do think it's reasonably likely that the Chinese government will use this cyber-agreement as part of an anti-corruption campaign. They'll probably make a show of a few people that they say they've caught engaging in this. It's basically PR [public relations]—PR that has a purpose domestically. I wouldn't put a lot of stock in the Americans and Chinese no longer engaging in a cyber-fight.

Who are winners and losers in a G-Zero world?

The United States is the winner in a G-Zero world. The fact is, in a G-Zero world, you're seeing the Middle East blow up. You're seeing Russia invade Ukraine. You're seeing refugees show up across the Middle East and now into Europe. They're not coming to the United States. The Western Hemisphere is surprisingly stable geopolitically. One of the biggest issues we've had in the Western Hemisphere has been the Colombian war between the FARC and the government. Now it looks like that's even been resolved. Cuba was a big problem. That's being resolved.

That all means that the US is a comparative winner near term, [though] probably not long term because instability eventually washes up to American shores. We don't govern long term. As a consequence, we're not going to do much about that.

The entire Middle East loses in the G-Zero. A whole bunch of relatively vulnerable non-consolidated democracies, like Turkey and Brazil, are going to be more vulnerable in the G-Zero world. Emerging markets that don't have a lot of resilience and aren't as well governed tend to be really problematic in a G-Zero world.

Rogue states tend to be winners. The Iranians have more ability to skirt American desires precisely because they can play ball with the Europeans, the Russians, and the Chinese. ISIS is a winner in a G-Zero world. I don't think that's a good thing. In short, stable states, rogue states, and pivot states (the ones that can hedge with everybody) are winners.

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