

## Geopolitical challenges and geo-economic shifts

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The year 2024 will probably go down in history as a time of rapid change in the global political and economic landscape.<sup>1</sup> This process obviously has been underway for a number of years, but so far it has rather tested major world powers for their readiness for fundamental shifts.<sup>2</sup> Since the early 2020s, it has become apparent that the world is moving away from a rules-based multilateral order and towards power politics, generating unprecedented risks and challenges that the world has not seen since WWII.

Instead, there are accelerating global transformations resulting in rather controversial and often undesirable changes; meanwhile, challenges are turning into risks that could seriously impede the civilised development of humanity.<sup>3</sup>

And this may be particularly true of European society, including the Ukrainian one, as it already has every right to be considered an integral part of this community.

During the 1990s and early 2000s, the European Union managed to significantly strengthen its institutional capacity, allowing it to expand to 27 countries and to exert its political, economic, and diplomatic influence not only among democracies but also in the region now called the Global South.

In the past few years, however, the deterioration of international relations, including declining transatlantic ties, fading European competitiveness and institutional weaknesses in consensus decision-making, have raised concerns about the EU's authority and its decisive role in international diplomacy. Furthermore, the rapid decline in the European economy's share in the global economy has made dynamic emerging economies less willing to listen to the EU's decisions.<sup>4</sup>

Despite not being recognised as closely associated with EU countries in the past, Ukraine surprisingly has played a key role in European processes in the past two years. First, the war in Ukraine and the country's courageous defence of its independence and freedom strengthened Euro-Atlantic solidarity and mutual understanding, united Europe, consolidated its efforts to counter the aggressor, and demonstrated the real weight of European values. By the way, one of Europe's responses to Russian invasion of Ukraine was the adoption of a strategy to reduce the risks<sup>5</sup> of the EU's economic relations, economic dependence and economic vulnerability, which is the essence of strategic autonomy.<sup>6</sup>

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<sup>1</sup> Rapprochement intentions or readiness for disengagement / Kyiv, Razumkov Centre, 2024. – <https://razumkov.org.ua/images/2024/05/14/2024-PAKT-8-ENGL-2.pdf>

<sup>2</sup> For example, the 2024 meeting of the OECD Ministerial Council was held under the slogan "Co-creating the Flow of Change" – The OECD, Southeast Asia and a new global economic order, <https://www.japantimes.co.jp/2024/05/02/special-supplements/oecd-southeast-asia-new-global-economic-order/>.

<sup>3</sup> Ideology behind restoration of economic liberties / Kyiv, Razumkov Centre, 2024. – <https://razumkov.org.ua/images/2024/02/29/2024-PAKT-ENGL-3N.pdf>

<sup>4</sup> Balázs P., et al. The changing world order and its implications for the "wider Europe". – <https://cens.ceu.edu/projects/changing-world-order-and-its-implications-wider-europe>

<sup>5</sup> Fasulo F., et al. Defying Gravity: Is De-Risking from China Possible? – <https://www.ispionline.it/en/publication/defying-gravity-is-de-risking-from-china-possible-150813>.

<sup>6</sup> The Seismic Changes of China-EU relations: An Overview. – <https://www.ispionline.it/en/publication/the-seismic-changes-of-china-eu-relations-an-overview-175805>.

Meanwhile, 2024 may lead to the EU's informal but principled division, just like 2022 has consolidated Europe (with Ukraine playing an almost decisive role in both cases) if, following the European elections, right-wing radical forces expand their influence (along with anti-Ukrainian sentiment) in individual countries and in the EU as a whole, and especially if supported by Hungary's position during its rotating presidency of the EU Council. Furthermore, the results of the US presidential election may even harm the entire Euro-Atlantic structures that have long served the global security mission.<sup>7</sup>

## Geopolitical challenges

The US-China trade wars that began in the late 2010s, coupled with transatlantic contradictions that are rising to a new level with the approaching US presidential election, have deepened political differences not only between the leading nations but also their partners and satellites, disrupted global production and logistics links, and called into question the benefits and achievements of free trade. And the invasion of Ukraine by Russia has further highlighted that the global order, which included economic, financial, energy and food security, could no longer exist in its "usual" form. This required significant "risk mitigation" to create new global structures, including supply chain resilience and enhanced security of global markets.<sup>8</sup>

**Rejection of the WTO in favour of security initiatives.** The creation of the World Trade Organisation (WTO) in the mid-1990s was initially welcomed as a positive development for global trade, as it was believed that the openness and liberalisation of trade flows under WTO control would boost investor confidence in the protection and profitability of investments, and thus encourage further investment expansion (which would accompany trade expansion).

However, the WTO quickly proved to be increasingly incapable to resolve disputes, especially among major players, leading to a decline in confidence in the WTO, which limited investor intentions to expand investments, especially new investment projects. Moreover, investors were increasingly willing to allocate their capital to less "regulated" economies, giving preference to individual projects or refocusing on mergers and acquisitions.<sup>9</sup>

The cruciality of the ongoing and accelerating trade transformations is not only related to the diminishing significance of global trade and investment, but also to the emerging reality where geopolitical risks, including the use of economic dependencies as a weapon by some countries, create a negative spiral that encourages protectionism and reduces openness and trust between countries, and thus accelerates the fragmentation of the global economic space.<sup>10</sup>

Furthermore, even a partial loss of economic interests would almost certainly lead to greater political tension and even confrontation, which undermines the reliability of businesses that would rather leave countries experiencing geopolitical divides. The global economy's liberal content had to be replaced by new "narratives" of economic development, and it quickly became apparent that regular declarations of free development veil an increasing concern for economic security. Moreover, it prioritised the national socio-economic and socio-political environment, and then the international one.

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<sup>7</sup> Colomina C. The World in 2024: ten issues that will shape the international agenda. – [https://www.cidob.org/en/publications/publication\\_series/notes\\_internacionales/299/the\\_world\\_in\\_2024\\_ten\\_issues\\_that\\_will\\_shape\\_the\\_international\\_agenda](https://www.cidob.org/en/publications/publication_series/notes_internacionales/299/the_world_in_2024_ten_issues_that_will_shape_the_international_agenda)

<sup>8</sup> A Strategy to Securitise the Economy? The EU's Partnerships in the Indo-Pacific. – <https://www.isdp.eu/event/a-strategy-to-securitize-the-economy-the-eus-partnerships-in-the-indo-pacific/>

<sup>9</sup> The world's economic order is breaking down. – <https://www.economist.com/briefing/2024/05/09/the-worlds-economic-order-is-breaking-down>

<sup>10</sup> The OECD, Southeast Asia and a new global economic order. – <https://www.japantimes.co.jp/2024/05/02/special-supplements/oecd-southeast-asia-new-global-economic-order/>.

**The race of global initiatives.** The beginning of the 2020s was highlighted by the launch of global initiatives by the United States, European Union and China. First, let's mention the Chinese Global Development Initiative (GDI, 2021), the Global Security Initiative (DSI, 2022), and the Global Civilisation Initiative (GCI, 2023). Each of them is aimed at transforming the international economic (and political) system and bolstering China's central position in such a global system.<sup>11</sup>

One should acknowledge that China's economic presence, especially in trade and investment, in the emerging economies is expanding at a rather high rate. And these countries seem to be more "willing" to embrace China rather than the developed economies. China successfully exploits the opposition between the developed nations and the Global South countries, many of which are already under China's influence, while downplaying the importance of developed countries' assistance to the developing world, because in reality large, developed nations – the United States (\$55 billion in 2022), Germany (\$35 billion), Japan (\$17 billion), and others – have always been and still are the main donors of foreign aid.<sup>12</sup>

A peculiar feature of these initiatives, which supposedly emphasised their economic orientation, is a very specific interpretation of provisions on which civilisational security is based. In particular, the DSI, while declaring the unconditional sovereignty, insists on recognising the principle of the indivisibility of security, which holds that the security of one country shall not be fulfilled at the expense of the security of other countries; and that this principle must become the basis of a new international security architecture.<sup>13</sup> In fact, this serves as the basis for justifying Russian aggression against Ukraine, as (according to Russian propaganda) the attack was allegedly necessary to stop NATO expansion allegedly threatening Russia.

And the GCI asserts the ability of states to manage democratic processes. In particular, states are to determine their own systems of citizen rights and obligations, and that no country or alliance of countries can interfere in determining the acceptable level of human rights in another country.<sup>14</sup> This essentially means that democratic and human values become secondary to the state ideology and practice of each individual country.

Two strategic programmes (also of an economic nature) focused on the infrastructure expansion of the EU's partner countries and regions were expected to respond to China's initiative challenge. These are the G7 Partnership for Global Infrastructure and Investment<sup>15</sup> and the European Union's Global Gateway Strategy.<sup>16</sup>

Additionally, interregional security documents were also presented. As a response to Russian aggression, NATO and the EU have published updated security strategies.<sup>17</sup> The EU's Strategic Compass emphasises partnerships with powerful international organisations and alliances, such as ASEAN, which is already part of the global security system. This essentially complements the United States' Indo-Pacific Strategy,<sup>18</sup> which focuses on building regional partnerships and actually presents

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<sup>11</sup> Economy E. China's Alternative Order. – <https://www.foreignaffairs.com/china/chinas-alternative-order-xi-jinping-elizabeth-economy>

<sup>12</sup> Amighini A., et al. China's Grip on the Global South Here to Stay? – <https://www.ispionline.it/wp-content/uploads/2024/05/policy-paper-AMIGHINI-chinaandglobal-south-2024compr-1.pdf>

<sup>13</sup> China's Strategic Calculations in the Russia-Ukraine War. – <https://www.wilsoncenter.org/blog-post/chinas-strategic-calculations-russia-ukraine-war>.

<sup>14</sup> Economy E. China's Alternative Order. – <https://www.foreignaffairs.com/china/chinas-alternative-order-xi-jinping-elizabeth-economy>

<sup>15</sup> FACT SHEET: Partnership for Global Infrastructure and Investment at the G7 Summit. – <https://www.whitehouse.gov/briefing-room/statements-releases/2023/05/20/fact-sheet-partnership-for-global-infrastructure-and-investment-at-the-g7-summit/>.

<sup>16</sup> Global Gateway. – [https://commission.europa.eu/strategy-and-policy/priorities-2019-2024/stronger-europe-world/global-gateway\\_en](https://commission.europa.eu/strategy-and-policy/priorities-2019-2024/stronger-europe-world/global-gateway_en).

<sup>17</sup> Rodríguez A. EU Strategic Compass: The Right Direction for Europe? – <https://www.ispionline.it/en/publicazione/eu-strategic-compass-right-direction-europe-35453>

<sup>18</sup> FACT SHEET: Indo-Pacific Strategy of the United States. – <https://www.whitehouse.gov/briefing-room/speeches-remarks/2022/02/11>.

a doctrine of countering China, protecting and improving the region for international cooperation. The focus of these initiatives is to integrate economies and societies within a global security environment.<sup>19</sup>

Whereas democratic countries' global initiatives and programmes are aimed – at least declaratively – at creating positive examples and best practices for humanity development, there is also an open and blatant demonstration of aggressive intentions, in particular with regard to Ukraine, especially when the unity between democratic countries is vague.

**The clash of initiatives.** Delays in decisions on providing assistance to Ukraine may be seen by aggressive countries as a sign of uncertainty of developed nations about their own position, and thus as political weakness, which inevitably provokes further aggressive intentions. In particular, Russia is already openly threatening neighbouring European countries that are NATO members. Experts believe that Russia's next step will likely be aggression against neighbours as a way to demonstratively "punish" them for supporting Ukraine. These actions can frighten European society, which is accustomed to living in peace and security.

Furthermore, if Russia is successful in its actions, it could encourage territorial claims by China in the Indo-Pacific, where confidence in the readiness of Western countries to defend their eastern partners and allies will weaken. Such negative perceptions could spread globally, undermining faith in democratic countries and the values they profess and are willing to defend.<sup>20</sup>

Meanwhile, China's ability to use disagreements between other countries to expand its own influence is noteworthy. Thus, Russian aggression has clearly marked China's place in transatlantic relations. As positions of some EU countries in terms of supporting and helping Ukraine have become questionable over time, this has led to a Euroscepticism-like disassociation of such countries from the EU's alliance and partnership commitments, also increasing US dissatisfaction with Europe's inability to come up with swift political measures to support Euro-Atlantic unity.<sup>21</sup>

For its part, in order to establish itself as a global independent actor, the EU needs to develop and strengthen its own "independent voice", which would not only confirm the relevance of the EU's leadership in resolving global conflicts, but also prevent further confrontation between the United States and China, which, in turn, would fortify Euro-Atlantic (political and economic) values and their practical protection.<sup>22</sup>

However, the effectiveness of such measures may be hindered by significant economic shifts in the global economic landscape.

### **Is the global economy saturated?**

The global economy is now showing numerous signs of changes in globalisation processes, with increasing fragmentation and "fragmentegration". And while recently there was talk of renewed

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<sup>19</sup> Wu J.J. Defending Taiwan by Defending Ukraine. – [https://www.foreignaffairs.com/china/defending-taiwan-ukraine-jaushieh-joseph-wu?utm\\_medium=newsletters&utm\\_source=twofa&utm\\_campaign=East%20Asia's%20Coming%20Population%20Collapse&utm\\_content=20240510&utm\\_term=FA%20This%20Week%20-%20112017](https://www.foreignaffairs.com/china/defending-taiwan-ukraine-jaushieh-joseph-wu?utm_medium=newsletters&utm_source=twofa&utm_campaign=East%20Asia's%20Coming%20Population%20Collapse&utm_content=20240510&utm_term=FA%20This%20Week%20-%20112017)

<sup>20</sup> Zagorodnyuk A., et al. A Theory of Victory for Ukraine. – [https://www.foreignaffairs.com/ukraine/theory-victory-ukraine?utm\\_medium=newsletters&utm\\_source=twofa&utm\\_campaign=How%20China%20Will%20Squeeze%2C%20Not%20Seize%2C%20Taiwan&utm\\_content=20240524&utm\\_term=FA%20This%20Week%20-%20112017](https://www.foreignaffairs.com/ukraine/theory-victory-ukraine?utm_medium=newsletters&utm_source=twofa&utm_campaign=How%20China%20Will%20Squeeze%2C%20Not%20Seize%2C%20Taiwan&utm_content=20240524&utm_term=FA%20This%20Week%20-%20112017)

<sup>21</sup> Alcaro R. More Integration, Less Autonomy: The EU in Europe's New Order. – <https://www.jointproject.eu/2022/09/01/more-integration-less-autonomy-the-eu-in-europes-new-order/>

<sup>22</sup> Morillas P. The US, China, and the EU in a New Global Order: A World of Two or Three? – [https://www.cidob.org/es/publicaciones/serie\\_de\\_publicacion/opinion\\_cidob/seguridad\\_y\\_politica\\_mundial/he\\_us\\_china\\_and\\_the\\_eu\\_in\\_a\\_new\\_global\\_order\\_a\\_world\\_of\\_two\\_or\\_three](https://www.cidob.org/es/publicaciones/serie_de_publicacion/opinion_cidob/seguridad_y_politica_mundial/he_us_china_and_the_eu_in_a_new_global_order_a_world_of_two_or_three)

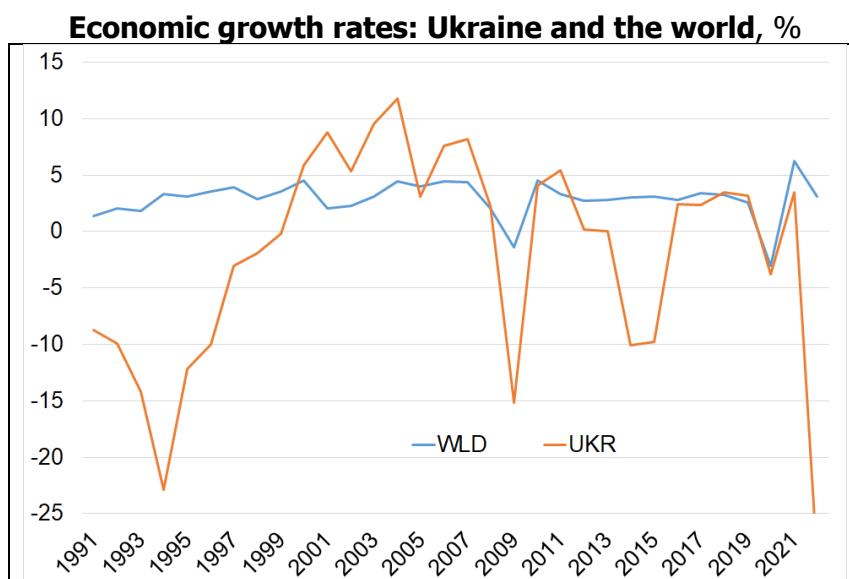
drivers accelerating globalisation, today there is more concern about developed countries losing their leadership positions in the global economy, while large emerging economies, while demonstrating significant potential for development (growth, trade, investment), become cluttered with negative manifestations (fiscal deficits, debts, industrial pollution) that may soon call into question their leadership ambitions.

In order to demonstrate these important shifts in the global economy and the redistribution of sources of growth, the authors will use indicators and characteristics from both the global level and some world leaders, such as the US and the EU as the most developed economies, and China as the leading representative of the Global South, to provide a more comprehensive understanding of global changes.

**Economic dynamics.** First of all, let's look at the "positive" shifts that indicate the growing significance of emerging countries in the global economy.

While the world economy grew steadily in the 1990s and the first half of the 2000s at an average annual rate of 4-5%, a downward trend clearly surfaced after the Global Financial Crisis (GFC). This was largely due to the developed countries' rather symbolic growth of 2-3%, while emerging economies, China included, struggled to navigate the crisis.

In contrast, Ukraine had never effectively implemented first a stabilisation policy, and then a growth and development policy, so the country was increasingly losing its potential and falling further behind global welfare standards (Figure "Economic growth rates...").<sup>23</sup>



It should be noted that the unevenness of economic growth and development has not gone anywhere, and countries, especially emerging ones, have had different successes in transformations and reforms (Box "Paradoxes of growth").

#### PARADOXES OF GROWTH

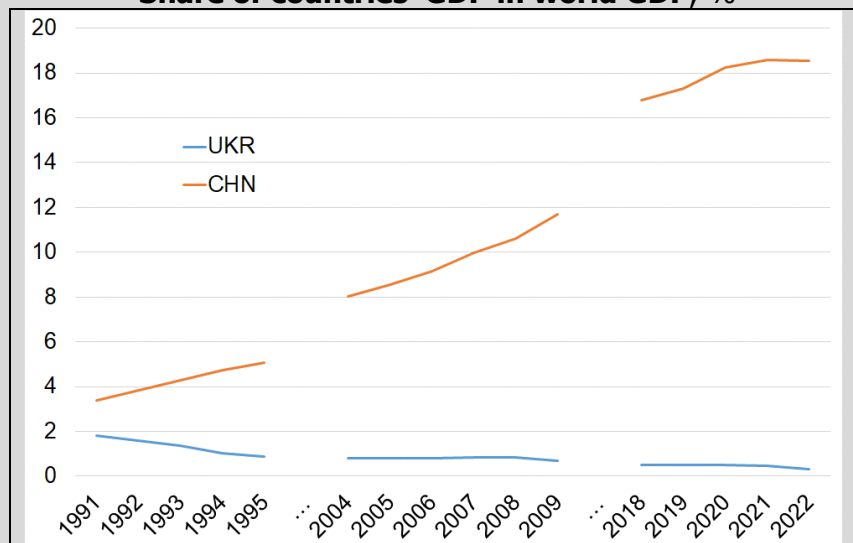
Sadly, but Ukraine is one of the countries that has not achieved successful transformation shifts.

It may seem surprising, but immediately after the Soviet Union's collapse in the early 1990s, Ukraine's GDP was only half the size of China's. The country's starting opportunities looked very promising.

<sup>23</sup> Unless indicated otherwise, data from *World Bank Indicators* (<https://data.worldbank.org/indicator/>) are used for international comparisons. Recognised three-letter international abbreviations are also used to refer to economies: USA – United States, CHN - China, GBR – United Kingdom, etc.

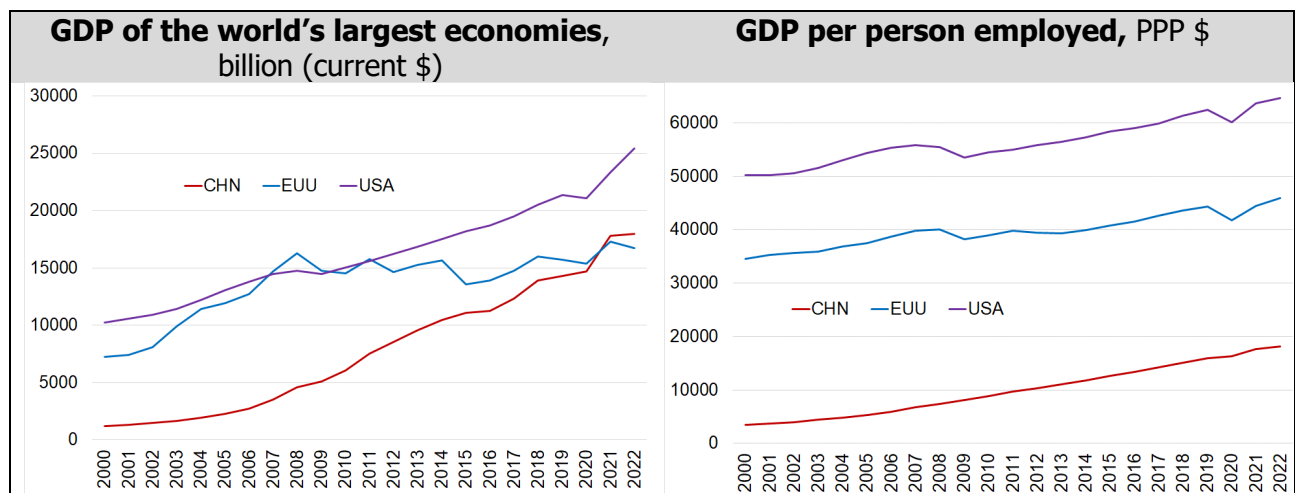
But then the situation changed dramatically. The Chinese economy grew rapidly for the next 25 years, while Ukraine's became increasingly less visible on a global scale (Figure "Share of countries' GDP in world GDP").

Share of countries' GDP in world GDP, %



In recent years, one could observe two increasingly evident trends in the global distribution of value added. First, the share of developed economies in global GDP production has been declining steadily, while the share of emerging economies has been growing consistently.

Second, the G3 (the United States, the European Union and China)<sup>24</sup> continues to consolidate its leadership in the global economy despite periodic negative influences (Figure "GDP of the world's largest economies"). At the same time, China's labour productivity is still significantly lower than that of the US and the EU (Figure "GDP per person employed"). And in the EU, although the total value added shows no notable changes,<sup>25</sup> labour productivity is still significantly higher than in China.<sup>26</sup>



<sup>24</sup> Ing L.Y., Lin J.Y. Economic Transformation and a New Economic Order. – <https://www.eria.org/uploads/Economic-Transformation-a-New-Economic-Order.pdf>

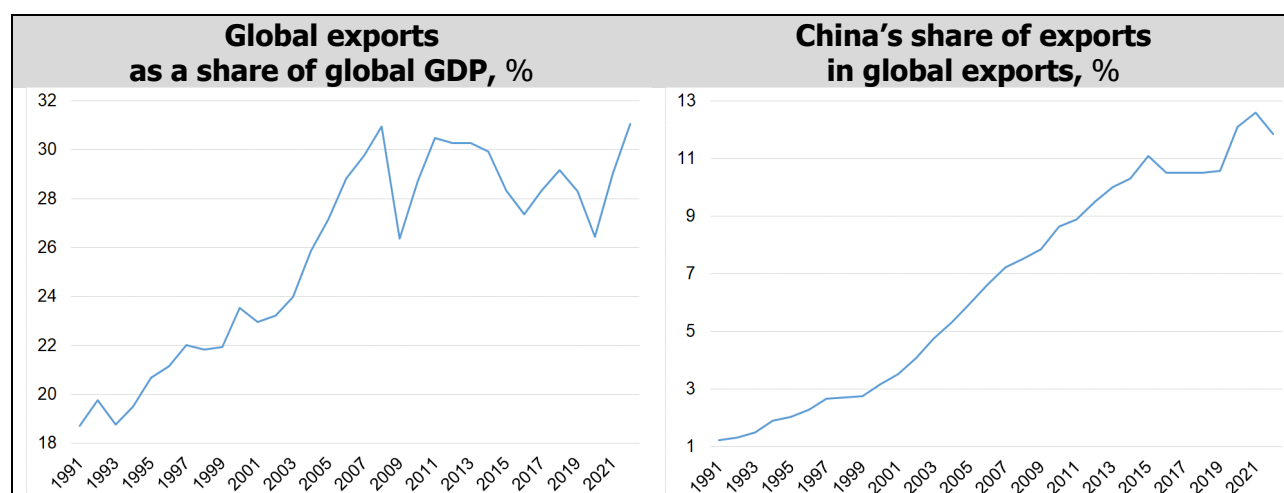
<sup>25</sup> There are reasons to believe that over time, the EU will increasingly lag behind China in the global GDP formation, and the productivity of European and Chinese economies will align. In this case, systemic questions are about the consequences of a gradual decline in the EU's share of the global economy and the extent to which the preservation of the EU's cultural and institutional traditions can compensate for the decline in economic benefits.

<sup>26</sup> This is the source of further growth in China's economy. Given the size of the workforce, even a slight increase in productivity will mean a significant boost in the country's GDP.

**World trade.** International trade flows are another area demonstrating the weakening of global economic dynamics, which in recent years has been making a U-turn from free trade to fragmentation with elements of trade wars, as well as the abandonment of institutions that played a crucial role in development.

In particular, the rapid growth of exports in GDP before the GFC of 2008-2009, including due to support for the export-oriented development model of China and other emerging, mainly Asian, economies, gave way to a mostly downward trend (Figure "Global exports..."), reflecting the abandonment of regulatory institutions such as the WTO, the introduction of new trade duties and restrictions, increasingly justified by national (economic) security needs.

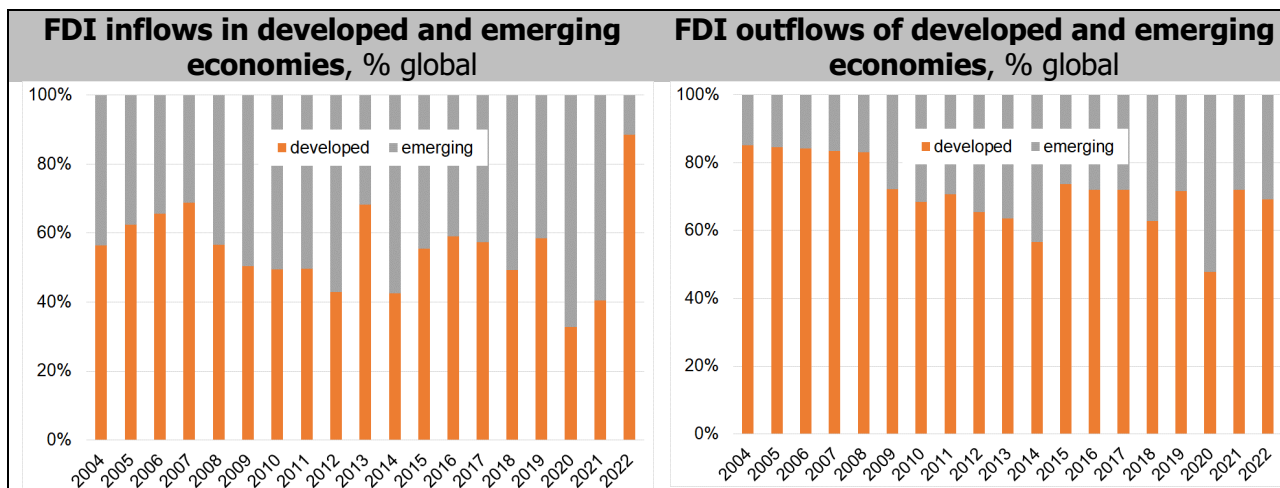
Even China has partially abandoned its export expansion, reducing exports (primarily to developed markets) and expanding domestic consumption (Figure "China's share of exports..."). Meanwhile, this reduction in export capacity in many countries has been driven by a misconception about the benefits of import substitution and one of its most common mechanisms – the requirement of so-called localisation of production (using more components and intermediate products from domestic producers). However, import substitution in many cases has only led to a loss of relative advantages, decreased competitiveness and hindered structural and technological changes.<sup>27</sup>



**Investments.** Over the past two decades, there has been a notable shift in investment flows. For example, until the mid-2000s, foreign direct investment (FDI) inflows to emerging economies accounted for 30-40% of total FDI, which was associated with high risks and relatively few big profitable projects. However, after the GFC, which affected virtually all developed countries, emerging economies, especially in the Indo-Pacific, began to attract more investors due to their increased industrial technological capacity. As a result, the share of global FDI inflows to developed and emerging economies have almost equalised in recent years (Figure "FDI inflows in developed and emerging economies").

Meanwhile, post-GFC economic acceleration of emerging economies allowed some of these countries to start exporting FDI to other emerging economies, particularly in the Indo-Pacific. As a result, China, South Korea, and ASEAN countries, which until recently were only FDI recipients, could establish investment and production networks of technological goods mainly exported to the United States, Canada, the EU, and other developed countries, and thus increasingly entered global capital market flows. Consequently, the share of emerging countries in FDI outflows now exceeds one-third of global FDI exports (Figure "FDI outflows of developed and emerging economies").

<sup>27</sup> Ing L.Y., Lin J.Y. Economic Transformation and a New Economic Order. – <https://eria.org/uploads/Economic-Transformation-a-New-Economic-Order.pdf>



Speaking of inbound and outbound investment, the European Union, being one of the largest foreign investors in the world, has been giving significant attention to their “correctness” and security recently. While the EU recognises the importance of open global markets, it also acknowledges the growing concerns regarding outbound investments in a narrow set of advanced technologies, the vast majority of which are dual-use, and that could enhance military and intelligence capabilities of actors who may use these capabilities against the EU or to undermine international peace and security.<sup>28</sup> Although the European Commission has published the so-called White Paper on outbound investment, the level of understanding of the possibilities of preventing potential risks remains insufficient (more on that below).

**Industrial displacement.** The expanding globalisation since the beginning of the century and transnational corporations’ super-profits enabled by cheap labour force in emerging economies, have led to the relocation of production capacities from industrialised to emerging countries, resulting in industrial and technological growth of the latter. In these settings – with wider access to relatively cheap technological and consumer imports – industrial production was displaced from national economies, especially in Europe.

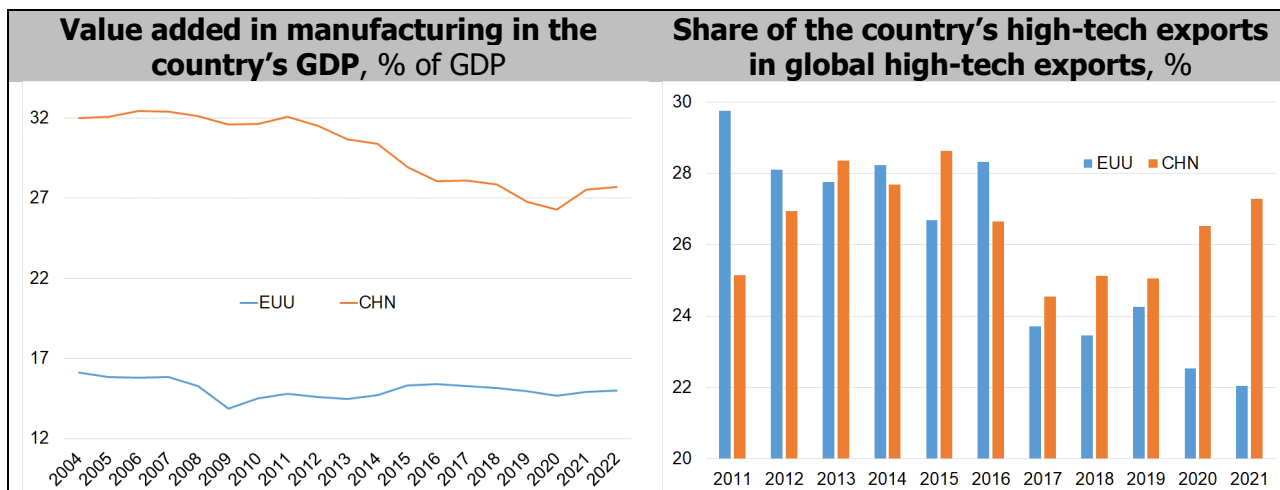
Even today, the EU’s task of achieving strategic autonomy is quite challenging due to the lack of necessary production resources (including adequate labour force) and slower introduction of technological innovations compared to the US and China.

Although China’s share of value added in manufacturing is decreasing, it is still significant and is almost twice that of the EU (Figure “*Value added in manufacturing...*”). This serves as a foundation for the ongoing strengthening of China’s industrial sector, which is accompanied by rapid technological change.

This is further confirmed by the fact that the share of high-tech exports from the EU in global exports has clearly declined over the past decade by 6-8 percentage points, from 28-30% to 22-23%. In the meantime, after a sharp decline in 2017-2019 as a result of the US-China trade war and EU-supported restrictions on Chinese technology imports, China’s share of high-tech exports has resumed growth in recent years and already exceeds the EU’s by 4-5 percentage points (Figure “*Share of the country’s high-tech exports...*”). Additionally, other countries in the Indo-Pacific, such as South Korea, India, Indonesia, have also increased their share of technological exports, strengthening the region’s competitive position in general and indicating the relocation and formation of a new global centre for technological production.

<sup>28</sup> Commission proposes new initiatives to strengthen economic security. – [https://ec.europa.eu/commission/presscorner/detail/en/IP\\_24\\_363](https://ec.europa.eu/commission/presscorner/detail/en/IP_24_363)





The production of semiconductors and chips, which are the basis of modern technological shifts, deserves special attention. There are 387 production facilities globally, with 80% concentrated in 4 countries – Japan (102), Taiwan (77), the United States (76), and China (70).<sup>29</sup> While developed countries currently dominate production, China is rapidly expanding its capacity and aims to capture a quarter of the global market in the next decade.

It should be borne in mind that China has an edge that could be decisive if international tensions escalate, potentially leading to developed countries losing their advantage in semiconductor production. Multiple critical minerals, critical metals, and rare earth elements (REEs) are required for the various components of semiconductors, and many of the supplies for these minerals are dominated by China. China controls 80% of the world's REE supply for which the US is 100% import-dependent. Currently, the US imports 80% of REE directly from China, while remaining portions are indirectly sourced from China through other countries., posing high development risks.<sup>30</sup>

**Debt aggravation.** Stimulating economic acceleration usually comes at a cost, which, in the case of irrational government policy, can nullify the benefits of economic expansion and create negative pressure on the country's welfare. So, let's consider some "negative" shifts.

The "debt trap" is one of the most common pitfalls in the government's attempts to support economic acceleration. With limited public resources, domestic and foreign borrowing seems like a reasonable solution for the country's socio-economic development. However, it is often forgotten that these funds need to be repaid.

Although in the second half of the 20<sup>th</sup> century many developed countries accumulated significant debts, they also developed effective debt repayment or restructuring mechanisms. Since the early 2000s, most of these countries have implemented strategies to reduce debt pressure. Instead, emerging economies, which have long been unable to access affordable loans from developed countries or tried to maintain high economic dynamics (often for political reasons), were actively "catching up" on the foregone funds. As a result, debt positions of many emerging economies were rapidly deteriorating (Figure "General government gross debt").<sup>31</sup>

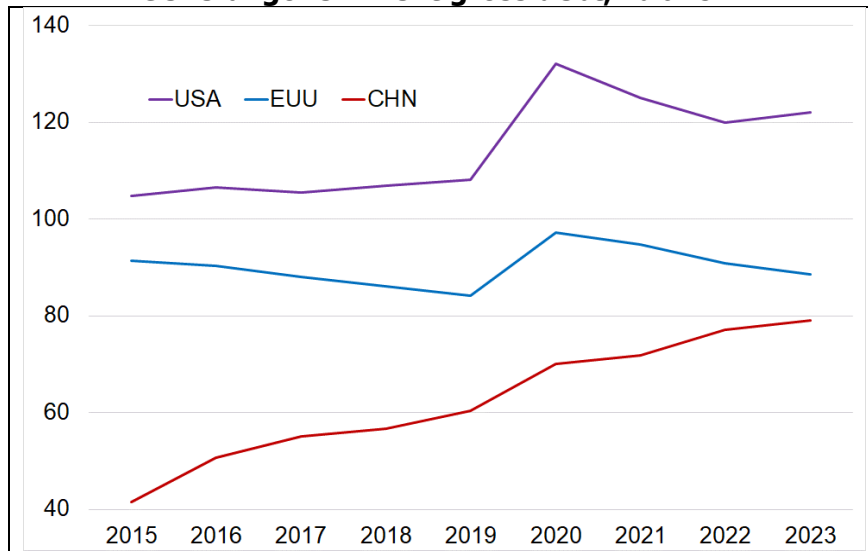
It is noteworthy that many developed countries, even those with traditionally low debts, have experienced a significant increase in public debt during the COVID-19 pandemic due to the introduction of unprecedented measures to combat the coronavirus crisis. This is in marked contrast to limited measures that even large emerging economies could afford, including those that, following China, have tried to implement a (near) "zero-COVID" policy.

<sup>29</sup> Semiconductor Market. – <https://www.precedenceresearch.com/semiconductor-market>

<sup>30</sup> The Global Semiconductor Supply Chain: Key Inputs. – <https://bbnc.bens.org/semiconductors---page-3-key-inputs>.

<sup>31</sup> IMF Fiscal Monitor. – <https://www.imf.org/external/datamapper/datasets/FM>.

**General government gross debt, % of GDP**



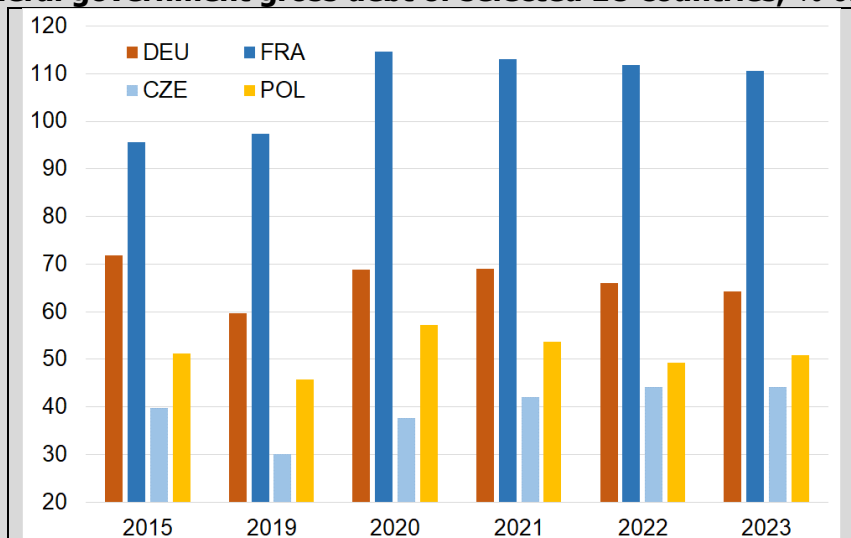
At the same time, developed countries or alliances of countries also face specific challenges that hinder the implementation of desired changes. This is clearly evident in the European Union, where the absence of a fiscal union means the lack of centralised control and rapid response to global threats (such as slow approval of the level of aid to Ukraine in the first weeks of the invasion) or unfair economic practices (such as Chinese government support for its state-owned and private companies in their expansion into European markets), which is detrimental to the EU's open economic space.

Another challenging area for the EU is its extremely diverse fiscal and debt positions. Historically, Europe's leading economies have been donors to European budgets and funds. However, with their debt positions disturbed, these countries' sentiment towards financing common expenditures has changed significantly (Box "Debt positions of EU countries").

**DEBT POSITIONS OF EU COUNTRIES**

The readiness of Central and Eastern European countries for the EU was assessed based on the so-called Maastricht (Copenhagen) criteria, which determined the levels (fluctuations) of key macroeconomic indicators, including the level of public finance debt. It was considered safe for public debt to be below 60% of GDP (*ceteris paribus*), as this could be financed through domestic and external borrowing.

**General government gross debt of selected EU countries, % of GDP**



The countries that joined the EU in 2004, known as the first wave candidates, mostly complied with the Maastricht criteria and had relatively balanced budgets with deficits below 3% of GDP and moderate debt pressures. Meanwhile the “old” EU members, despite trying to pursue a balanced fiscal policy, still occasionally deviated from restrictive commitments. In such settings, the “new” EU members, such as the Baltic States, Czechia, and Poland, are now in a much better (balanced) position in terms of public finances (Figure “General government gross debt of selected EU countries”).

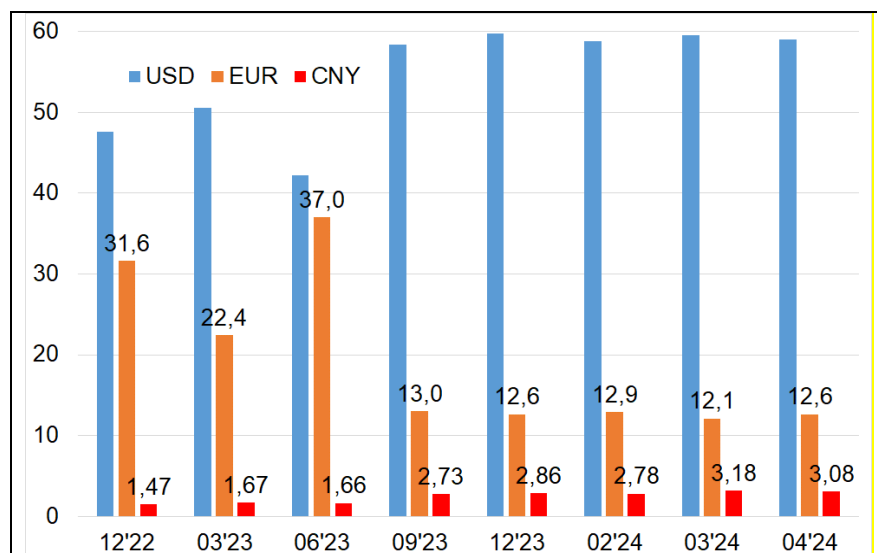
Redistribution of funding for the EU’s common spending could obviously help align the fiscal positions of its member states. However, better-balanced budgets are mostly found in smaller countries, which is not enough to significantly change the structure of the EU’s financial flows in general.

There is one more fundamental difference between the debt positions of developed and emerging economies, and it concerns external debts. Since the world’s leading currencies are in universal demand, debts denominated in such currencies have different “weights” for debtors.

No matter how large their debts are, developed countries will have no problem covering debts in their own or another hard currency, as the conversion will hardly cause any complications. Emerging economies usually have very limited hard currency reserves, and their national currencies are not universally accepted. Therefore, the level of risk of international currency debt differs significantly between developed and emerging economies.

**Fostering dollarisation?** The sanctions policy against Russia has had a controversial impact on the global economic environment. While the European Union has indeed reduced trade with Russia to the maximum extent possible, China has not only opened its market to Russian energy exports but has also become an important source of imports. In the process, China has emerged as the largest supplier of not only commercial goods, but increasingly of dual-use components covered by Western export controls.<sup>32</sup>

**Share of USD, EUR and CNY in international SWIFT payments, % of total**



That is, China has not at all refused to expand trade on favourable terms. Yet, it seems that Beijing was pursuing a much more important goal – to increase the yuan’s importance in international payments. So, it used Russia’s invasion of Ukraine and related Western sanctions to push for the de-dollarisation of the global economy. China is now settling its trade with Russia mainly in yuan and is taking steps to replace petro-dollars with petro-yuan by expanding payments for oil imports (from the

<sup>32</sup> Sher N. Behind the Scenes: China’s Increasing Role in Russia’s Defense Industry. – <https://carnegieendowment.org/russia- Eurasia/politika/2024/05/behind-the-scenes-chinas-increasing-role-in-russias-defense-industry?lang=en>

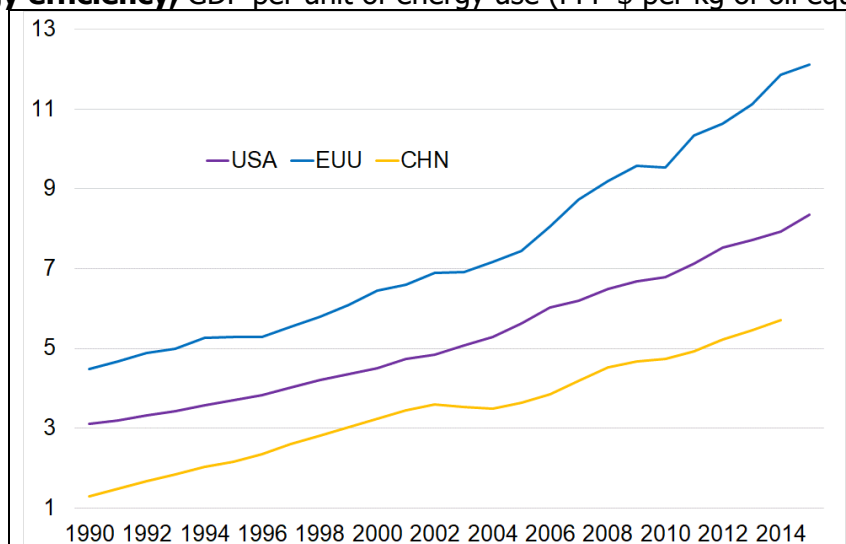
Persian Gulf countries) in yuan. China is also actively trying to introduce the yuan into international payments, including between third countries, to promote de-dollarisation.

Despite these efforts, the dollar has not yet been significantly affected, although the share of the euro in international payments has clearly decreased. While the yuan's share has slightly increased, it has been at the expense of the dollar, which continues to extend its dominance over other currencies (Figure "Share of USD, EUR and CNY in international SWIFT payments").<sup>33</sup>

**Environmental protection.** Economic acceleration also requires higher national expenditures on energy and raw materials, access to which (including extraction) often harms the environment. Similarly, the utilisation of raw materials in low-tech facilities is much more harmful than in modern "green" factories, mainly owned by leading developed countries.

By the mid-2010s, the problem of environmental protection was already present, but it had not yet become critical, so the ever-increasing use of energy resources by industrialised countries helped them maintain competitive advantages and boost their GDP, while better technologies ensured higher energy efficiency (Figure "Energy efficiency").

**Energy efficiency, GDP per unit of energy use (PPP \$ per kg of oil equivalent)**



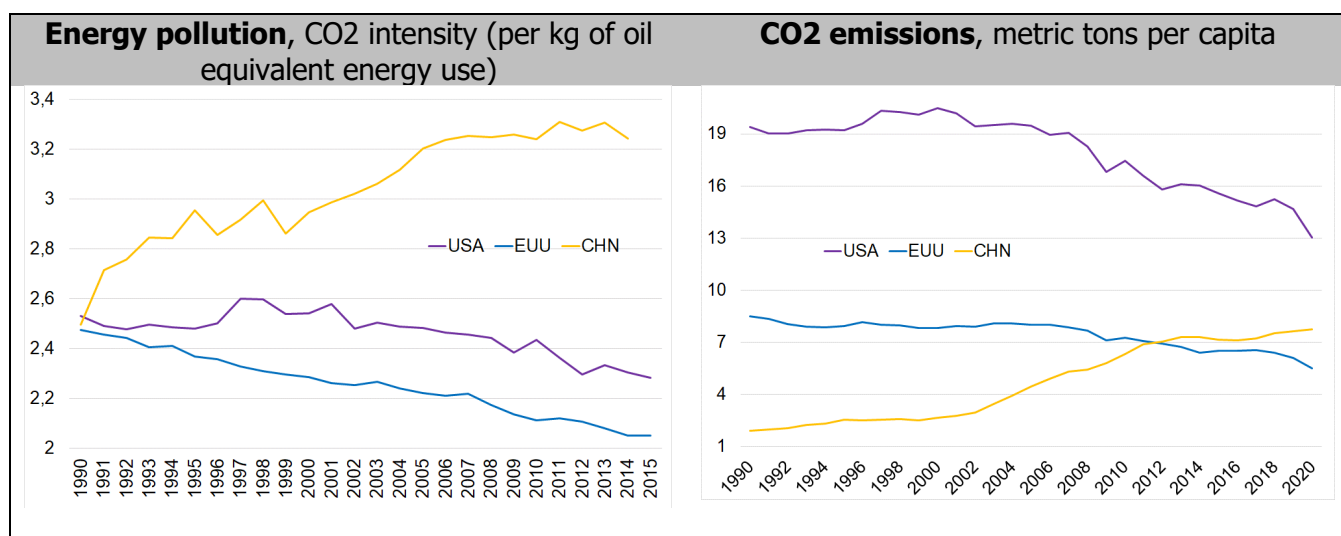
This resulted not only in the excessive use of energy resources, but also in significant carbon emissions – a source of environmental pollution and a factor in climate imbalances. Since the early 2000s, developed economies have adopted policy measures aimed at reducing environmental damage. Emerging economies, on the other hand, largely disregarded pollution, thinking that economic benefits would outweigh the damage caused to the country's and the region's ecosystems. Consequently, pollution caused by dynamic emerging economies continued to grow (Figure "Energy pollution").

Subsequently, pollutant emissions, while decreasing in developed countries, continued to increase in emerging economies (Figure "CO2 emissions"). One could think of it as of a domestic problem, but harmful substances are easily spread beyond national borders by air or water, causing global damage.

Recognising the urgency of the green transition for all countries, China is taking the initiative to become a leader in implementing such changes in emerging economies, especially those facing financial constraints in trying to achieve the target criteria. It has already become customary for China to offer partial coverage of these costs, establishing its global leadership among emerging

<sup>33</sup> Most used currency in the world for international payments in SWIFT. – <https://www.statista.com/statistics/1189498/share-of-global-payments-by-currency/>

countries as a “compensation”.<sup>34</sup> It is assumed that this financing will be in yuan, so this perfectly aligns with the goal of raising the yuan’s international status (and de-dollarisation in the best-case scenario).



### Areas of economic security strengthening

The growing significance of emerging countries in shaping the modern world order is indisputable. Therefore, no matter how contradictory and unstable they may seem, we should accept them and seek their support for policies of civilised growth and development. Moreover, we cannot allow the birth of a new world order dominated by authoritarian regimes that can destroy justice and freedom.

**Institutional de-risking mechanisms.** In the current geopolitical context, dominated by growing technological competition and increasing economic interdependence between countries produced by globalisation and openness, the boundaries between economy and security are increasingly blurred. Global shocks such as the COVID-19 pandemic, Russian aggression, the weaponisation of dependence, or even the growing rivalry between the US and the EU,<sup>35</sup> have underscored the risks inherent in excessive dependence, such as energy or supply chain vulnerabilities. Such risks can challenge the functioning of democratic societies and developed economies,<sup>36</sup> including the European Union, which will be critical for Ukraine’s future. Therefore, this section focuses on the possibilities of protecting the European security system, while some of the tasks were discussed in earlier publications.<sup>37</sup>

Developed countries have been actively seeking institutional mechanisms to address systemic risks even before the COVID-19 pandemic. The establishment of the EU-US Trade and Technology Council (TTC) is a notable example, as it focuses on economic, trade, and technology policy issues in addition to economic security. And TTC’s practical value was immediately felt when Russia re-invaded Ukraine and the partners needed to rapidly coordinate on export controls<sup>38</sup> and other sanctions measures.

<sup>34</sup> A Chinese Marshall Plan in the Green Economy Era, Huang Yiping suggests. – [https://www.eastisread.com/p/a-chinese-marshall-plan-in-the-green?utm\\_source](https://www.eastisread.com/p/a-chinese-marshall-plan-in-the-green?utm_source)

<sup>35</sup> Open strategic autonomy: illusion or reality? – <https://www.ispionline.it/en/publication/open-strategic-autonomy-illusion-or-reality-175757>

<sup>36</sup> Borrell J. Economic security: a new horizon for EU foreign and security policy [https://www.eeas.europa.eu/eeas/economic-security-new-horizon-eu-foreign-and-security-policy\\_en](https://www.eeas.europa.eu/eeas/economic-security-new-horizon-eu-foreign-and-security-policy_en)

<sup>37</sup> Rapprochement intentions or readiness for disengagement / Kyiv, Razumkov Centre, 2024. – <https://razumkov.org.ua/images/2024/05/14/2024-PAKT-8-ENGL-2.pdf>

<sup>38</sup> Trade and Technology Council: is it really enhancing dialogue? – <https://www.ispionline.it/en/publication/trade-and-technology-council-is-it-really-enhancing-dialogue-175778>

Moreover, the TTC was instrumental in developing a transatlantic counterweight to China, which was mutually consistent with the strategic objectives of the leading Indo-Pacific countries (through the AUKUS and Quad alliances).

The presentation of the EU Economic Security Strategy on 20 June 2023 was another decisive step towards economic security. The strategy aims to assess current challenges and risks while providing detailed plans to regulate investment and trade rules for European companies operating in other countries. Notably, the strategy prohibits European businesses from producing key modern technologies such as supercomputers, AI and advanced chips in countries like China "...with differences in values, models and interests".<sup>39</sup>

Meanwhile, institutional mechanisms have been introduced to protect against unfair competition, in particular:

- *Anti-Coercion Instrument (ACI)* to protect the interests of European companies when they are threatened abroad,
- *Foreign Subsidy Regulation (FSR)* to ensure a level playing field in the European single market, and
- *International Procurement Instrument (IPI)*.

As part of the European Green Deal, the European Commission has introduced the so-called Carbon Border Adjustment Mechanism (CBAM) to protect European manufacturers from unfair competition and promote higher environmental standards worldwide. The so-called G7's voluntary AI Code of Conduct has been developed in relation to artificial intelligence. Furthermore, the European Commission has adopted five initiatives to enhance the EU's economic security in the context of Russian war against Ukraine and amidst growing geopolitical tensions and technological changes.<sup>40</sup>

However, compared to the United States, the European economic security system is more cautious when it comes to China in general and the risks posed by Chinese expansion in particular. Partly this is due to European diplomatic traditions, and partly – due to existing intensive economic exchanges with China in countries like Germany and Italy.<sup>41</sup> Despite becoming commonplace, this cautious tactic does not hinder the EU's aim of accelerating the "double transition" to a green and digital economy within its strategic autonomy approach and restoring its competitive position in various strategic areas, including semiconductors, electric vehicles, artificial intelligence, quantum computing, biotechnology, and other strategic goods and services.

In the current European context and in view of the ongoing Russian aggression, the EU should focus on improving coordination of export controls<sup>42</sup> to prevent objects with both civilian and defence applications (such as advanced electronics, chemicals, missile technology) from being used to undermine security and human rights.<sup>43</sup> Outbound investment<sup>44</sup> also needs to be monitored, as it can export to third countries technological advances that, if misused, could cause significant harm and losses to humanity.

**The South is adjusting the South.** Unfortunately, the easing of opposition and confrontation between developed and emerging economies, largely mirrored in the US/EU confrontation with

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<sup>39</sup> The EU wants to ban European companies from producing critical technologies in China. –

<https://www.euointegration.com.ua/news/2023/06/20/7164027/> (in Ukrainian)

<sup>40</sup> Rapprochement intentions or readiness for disengagement / Kyiv, Razumkov Centre, 2024. –

<https://razumkov.org.ua/images/2024/05/14/2024-PAKT-8-ENGL-2.pdf>

<sup>41</sup> Trade and Technology Council: is it really enhancing dialogue? –

<https://www.ispionline.it/en/publication/trade-and-technology-council-is-it-really-enhancing-dialogue-175778>

<sup>42</sup> White Paper on export controls. – <https://circabc.europa.eu/ui/group/aac710a0-4eb3-493e-a12a-e988b442a72a/library/a44df99c-18d2-49df-950d-4d48f08ea76f/details?download=true>

<sup>43</sup> Commission proposes new initiatives to strengthen economic security. –

[https://ec.europa.eu/commission/presscorner/detail/en/IP\\_24\\_363](https://ec.europa.eu/commission/presscorner/detail/en/IP_24_363)

<sup>44</sup> White Paper on outbound investment. – <https://circabc.europa.eu/ui/group/aac710a0-4eb3-493e-a12a-e988b442a72a/library/51124c0d-58d8-4cd9-8a22-4779f6647899/details?download=true>

China, will be neither easy nor quick. One effective approach is to find a “mediator” who is not perceived as an “outsider” by both sides, and who understands both global concerns (climate change, pandemics, nuclear threat) and specific concerns of emerging countries (welfare, employment, state failure).

While China is seen by many emerging countries as the ideological and economic leader of the Global South, not everyone agrees to back Beijing’s ambitions. It is also becoming increasingly evident<sup>45</sup> that geographically distant countries are “gravitating” towards China, while geographically close ones are increasingly less enthusiastic about China’s growing influence in the region. The level of conflict and confrontation between China and its neighbours bordering the South China Sea is increasing from year to year, indicating regional risks rather than benefits.

Artificial islands, military bases, and provocative military exercises are meant to demonstrate who is the “boss” in the region. A map of the territories that Beijing considers its own has emerged recently, showing that China claims most of the South China Sea, including territories that are recognised by international law as part of the economic zones of Indonesia, Vietnam, the Philippines and Malaysia. So far, such actions are not critical but resemble the initial processes leading to Russia’s full-scale aggression against Ukraine.

Emerging economies are still lacking the experience of coordinated decisions to counter “old” or “new” aggressive neighbours, but they need a leader who is committed to peaceful coexistence and has experience of implementing such policies. In this regard, India, as a true representative of the Global South, can become a worthy ally for democracies and play a crucial role in mediating between developed and emerging nations.

With the weakening of Russia and the strengthening of China, India is increasingly focused on political and economic cooperation with partners that do not accept China’s encroachment on leadership but openly align with developed countries. These efforts of India are supported by the EU.<sup>46</sup>

The 2021 Strategy for cooperation in the Indo-Pacific<sup>47</sup> marked the first recognition by EU policy makers of the region’s relevance at the strategic level and set out core tenets for stronger multilateral cooperation and a level economic playing field in the Indo-Pacific, including security.<sup>48</sup>

The EU has already involved India in the Trade and Technology Council (TTC). Another important example of India’s engagement is the intensification of free trade negotiations with the EU and UK. Their successful outcome seems very likely after the signing of agreement with EFTA – the European Free Trade Association consisting of Iceland, Liechtenstein, Norway and Switzerland. India’s participation in the Resilient Supply Chain Initiative<sup>49</sup> is also important, because Japan and Australia, while playing a significant role in its implementation, are centres of gravity for many Indo-Pacific countries.<sup>50</sup> These policy actions recognise India’s economic and technological importance for the future and as the main regional opponent of China.<sup>51</sup>

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<sup>45</sup> Taiwan's choice: possible consequences. / Kyiv, Razumkov Centre – <https://razumkov.org.ua/komentari/vybir-taivaniu-mozhlyvi-naslidy> (in Ukrainian)

<sup>46</sup> Leadership transformations in the Indo-Pacific / Kyiv, Razumkov centre – <https://razumkov.org.ua/images/2024/02/26/2024-PAKT-ENGL-4-1.pdf>

<sup>47</sup> EU Strategy for cooperation in the Indo-Pacific. – <https://data.consilium.europa.eu/doc/document/ST-7914-2021-INIT/en/pdf>

<sup>48</sup> Future-proofing EU security and defence policies in the Indo-Pacific: doubling down with friends. – <https://www.realinstitutoelcano.org/en/analyses/future-proofing-eu-security-and-defence-policies-in-the-indo-pacific-doubling-down-with-friends/>.

<sup>49</sup> Resilient Supply Chain Initiative. – <https://initiatives.weforum.org/global-supply-resilience-initiative/home>

<sup>50</sup> The BRICS Summit: a time for consolidation or confrontation? / Kyiv, Razumkov Centre – <https://razumkov.org.ua/images/2023/07/12/2023-MATRA-I-KVARTAL-11.pdf> (in Ukrainian)

<sup>51</sup> A Strategy to Securitise the Economy? The EU’s Partnerships in the Indo-Pacific. – <https://www.isdp.eu/event/a-strategy-to-securitize-the-economy-the-eus-partnerships-in-the-indo-pacific/>

In such settings, the strengthening of India's position in South Asia and the Indo-Pacific may be boosted by Europe's own interests in promoting free trade, ensuring resilient supply chains and limiting the Chinese factor in the supply of strategic resources – risks that increase Europe's economic dependence on China.<sup>52</sup> At the same time, the current "simmering" conflict means that further polarisation of India-China relations in the Indian Ocean will generate more concerns about the region's militarisation, and therefore will pose a problem not only for India, but also for the United States and Europe.<sup>53</sup>

In the meantime, India is driving its efforts eastward. Its East Policy Act has led to institutional and political changes aimed at solidifying economic and political ties with Southeast Asia, East Asia, Oceania and Pacific Island states<sup>54</sup> and is in line with the country's growing intention to become a leading power in the Indo-Pacific, which largely falls within the needs of global democratisation.

**Ukraine as a role model.** Ukrainian experience has already generated lessons for the world, particularly in relation to the Taiwan situation. If China had gained control of the island, the economic losses and supply chain disruptions could have been mitigated over time, but a geostrategic shift in favour of China's authoritarian expansionism would damage the modern world order for decades.<sup>55</sup>

An important signal from Ukraine is that if a country is attacked, it can only count on strong support from partners when showing its resolve and heroism in defending itself and its statehood. As soon as Ukrainians demonstrated their willingness to fight for their democracy, the rest of the world was there to help. And in the coming years, the fate of Taiwan, like that of Ukraine, will be a crucial test of whether the world's democracies will not fail but stand.

At the same time, although Ukraine's struggle for independence and freedom has contributed to the strengthening of the European Union, some European countries are now showing intentions of redistribution, which is typical of aggressive autocratic states and should not happen in a civilised environment. As Ukraine continues to fight for its freedom and independence, the European Union, having such an example before its eyes, could be inspired to follow its own democratic traditions.

## **EU elections: moderate challenges and risks**

The results of the European Parliament elections held in early June 2024 were not too unexpected. Moreover, the process of forming pan-European institutions and putting them into operation is not quick, let alone the practical results of their activities. Yet, the outlines of the EU's renewal will become increasingly clear.

**Political component.** Despite certain success of right-wing radical (far-right) parties in European elections, it was not as significant as anticipated, with centrist forces still maintaining the majority. And this presents a somewhat unexpected opportunity for European renewal, which will depend on the willingness and ability of centrist and far-right parties to cooperate not only within individual political decisions, but also in the five-year perspective. The most important thing for Ukrainians in this regard is the European parliamentarians' attitude to Ukraine's fight against the aggressor.

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<sup>52</sup> Political, economic and structural consequences of Russian aggression for Ukraine and the international community. Challenges of Ukraine's economic recovery in the post-war period in view of European integration priorities / Kyiv, Razumkov Centre, 2023. – <https://razumkov.org.ua/images/2023/04/21/2023-ECONOM-VIDNOVL-ENGL.pdf> (extended summary)

<sup>53</sup> Leadership transformations in the Indo-Pacific / Kyiv, Razumkov centre – <https://razumkov.org.ua/images/2024/02/26/2024-PAKT-ENGL-4-1.pdf>

<sup>54</sup> ... first and foremost, Japan, Australia, Singapore, Vietnam, the Philippines and Indonesia.

<sup>55</sup> Wu J.J. Defending Taiwan by Defending Ukraine. – [https://www.foreignaffairs.com/china/defending-taiwan-ukraine-jaushieh-joseph-wu?utm\\_medium=newsletters&utm\\_source=twofa&utm\\_campaign=East%20Asia's%20Coming%20Population%20Collapse&utm\\_content=20240510&utm\\_term=FA%20This%20Week%20-%20112017](https://www.foreignaffairs.com/china/defending-taiwan-ukraine-jaushieh-joseph-wu?utm_medium=newsletters&utm_source=twofa&utm_campaign=East%20Asia's%20Coming%20Population%20Collapse&utm_content=20240510&utm_term=FA%20This%20Week%20-%20112017)

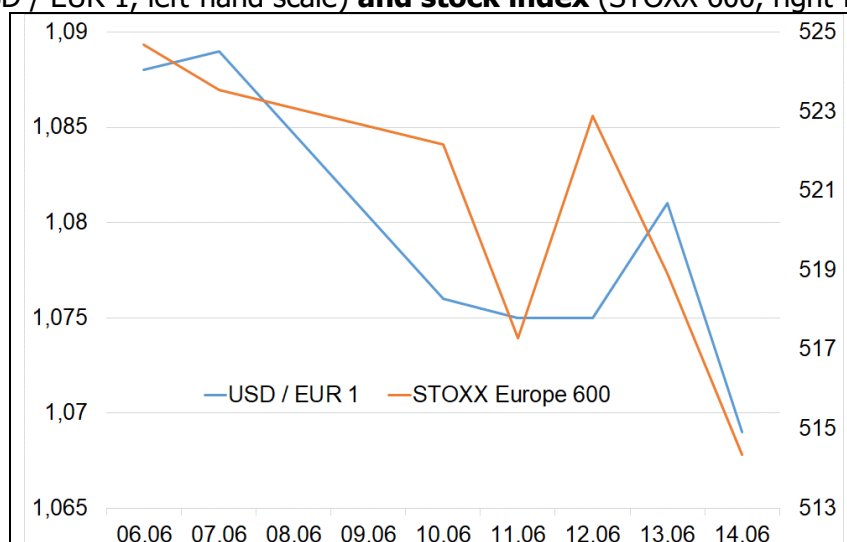


Long before the elections, the European People’s Party (EPP) did not rule out cooperation with the “conservatives and reformists”, informally led by Italian PM Giorgia Meloni. As a reminder, Ms Meloni is the leader of the far-right Brothers of Italy. Early in her political career she had a history of advocating good relations with Russia and even opposed the imposition of tougher anti-Russian sanctions in 2014. However, the large-scale invasion of Ukraine in 2022 has changed not only the rhetoric but also the practical approaches of the Italian right.<sup>56</sup> Meloni now considers support for Ukraine is a key pillar of her foreign policy, and this support is not only through statements but also through tangible actions. Italy is actively providing significant military to Ukraine, also aiming to increase its role in the European security system.

Meanwhile, the Italian far-right may well deepen cooperation with the French counterparts, led by Marine Le Pen, at least in terms of the Ukraine war. It is worth recalling that in early March, Marine Le Pen, the main opponent of President Macron and the far-right leader who was widely considered an unconditional supporter of Russia, made a statement in support of Ukraine and condemned the aggressor.<sup>57</sup> It is quite possible that Le Pen’s statement was an opportunistic pre-election message,<sup>58</sup> but this may also suggest that Europeans are increasingly rejecting the Russian aggressor and its barbaric actions.

**Economic prospects.** The strengthening of cooperation and interaction between the “historical” political rivals within new European institutions is crucial for the EU’s further development. Otherwise, Europe will become less understandable and predictable, and therefore less attractive to international investors.<sup>59</sup> As the EPP retains leadership in the renewed European Parliament, Ursula von der Leyen will probably be nominated as the next President of the European Commission. Her main economic policy priorities will likely include addressing security issues, updating industrial policy, and extending or easing the rules of the green transition as a “concession” to the far right.<sup>60</sup>

**Euro (USD / EUR 1, left-hand scale) and stock index (STOXX 600, right-hand scale)**



<sup>56</sup> Italy's withdrawal from the Belt and Road Initiative. / Kyiv, Razumkov Centre – <https://razumkov.org.ua/statti/vykhid-italii-z-initsiatyvy-odyn-poias-odyn-shliakh> (in Ukrainian)

<sup>57</sup> “Putin's friend” Le Pen criticises Russia's war against Ukraine. – <https://www.pravda.com.ua/eng/news/2024/03/14/7446404/>

<sup>58</sup> How realistic are France’s ambitions for leadership? / Kyiv, Razumkov Centre – [https://razumkov.org.ua/images/2024/05/14/2024-PAKT-7-RC\\_eng.pdf](https://razumkov.org.ua/images/2024/05/14/2024-PAKT-7-RC_eng.pdf)

<sup>59</sup> European elections: What a shift to the right could mean for the economy and markets. – <https://www.hellenicshippingnews.com/european-elections-what-a-shift-to-the-right-could-mean-for-the-economy-and-markets/>.

<sup>60</sup> The strict rules and deadlines for implementing the green transition in Europe are heavily criticised by right-wing radical parties due to the high cost of such a policy.

The EU's economic prospects will depend on how quickly it can form governing bodies and define its main tasks, as well as how well European businesses accept the new economic policy. Although it is too early to draw analytical conclusions about the business attitude towards the election results, there have been signals in the EU currency and stock markets during the first post-elections week.

The euro has weakened significantly, with a 2-cent drop in the exchange rate against the US dollar. Similarly, the leading European equity index STOXX 600 has also experienced a decline (Figure "*Euro and stock index*"), although it reached its all-time high of 525.59 in mid-May. So, the current decline may be seen as a correction rather than a fundamental loss of value caused by political events and processes, such as the increased representation of right-wing radicals in European institutions.

It is obvious that these parties' real influence in the European Parliament will strongly depend on their ability to unite and achieve common or agreed goals. For Ukrainians, the key concern is their willingness to continue supporting Ukraine, which seems unquestionable<sup>61</sup> at the moment. And today there are reasons to hope that this support will continue and grow even stronger.

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<sup>61</sup> Voting in the European Parliament shows consistently high support for Ukraine - in the vast majority of cases, the number of positive votes exceeds the number of negative or abstentions by an order of magnitude – How will gains by the far right affect the European Parliament and EU?, <https://www.chathamhouse.org/2024/06/how-will-gains-far-right-affect-european-parliament-and-eu>