The Besa Times

Monday 6 February 2023

3rd Edition

Foreword by our president, Tess Coullon

The US dollar is stronger than ever: How is this problematic for the global economy?

Labour markets in the post-pandemic world: from surplus to shortage?

The FTX Fallout and What It Made Us Rethink of Trust

Are Central Banks truly responsible for inflation?

If there has ever been a time in history where mainstream medias have communicated about inflation, it is our current period. Indeed, one solely needs to set his television on or open the social medias to see thoughts and takes from all sides of the political spectrum about the topic. However, there seems to be a common understanding among the general public that Central Banks directly caused our current inflation that is now close to 10% in the Eurozone. Nonetheless, there are other factors to consider such as supply chain disruption, and the geopolitical state of the World, all in a post-pandemic context.

The setting of prices is linked to the relation between supply and demand. And when it comes to inflation, this indicates two possibilities.

Either the demand is too high, or the supply is too low, and this is when Central Banks come into play. Indeed as we know, Central Banks are the suppliers of money in the economy and thus we can think intuitively that by increasing the money supply with the economic measures taken during the pandemic, the demand for goods has risen past the supply, causing inflation

The weaponization of Finance and its effects on the US dollar

We witnessed Russia's particular vulnerability to the USD after its invasion of Ukraine. Two days after the attack the G7 countries announced they'll impose painful sanctions on Russia and freeze nearly half of its $600 billion in foreign reserves. The western alliance also limited Russia's access to the SWIFT payment system - though they made exceptions to sustain trade in key commodities such as oil, gas and wheat. Such sanctions and measures have been taken before on countries such as Afghanistan, Iran and Venezuela. However, this round is different, not only in the force and scope of the sanctions package, but also because it targets a major world power, Russia.

Why is China holding an ambiguous position in the Ukraine war?

As both Russia and Ukraine seem far away from ceasing the hostilities, thus exacerbating the already terrible consequences of the war, both from a humanitarian and economic point of view, a major issue remains the role of China in this conflict.

Indeed, the country led by President Xi Jinping has not yet taken any clear official stance on which side to support:although it has often stated that the sovereignty, the integrity and independence of any country should be respected and has indicated dialogue as the right means through which a solution is to be found, China has referred to the Russian attack as an invasion and still considers Vladimir Putin as a fundamental partner and ally. Conversely, the Russian President has recently publicly acknowledged the concerns Beijing has on the war, highlighting a difference between the positions of the two countries for the first time since the beginning of the conflict.

However, the Chinese government keeps avoiding tackling the issue directly in front of the public, whilst stressing its commitment to "work with Russia and fulfill their responsibilities as major countries".

Now someone might ask: why is China behaving in such an ambiguous way?

The answer, as it usually happens in politics, is anything but definite, although it is reasonable to assume that the aforementioned strategy is the most convenient for the Chinese government.

But then the question remains: why is this the case?

On the one hand, the alliance between China and Russia, recently defined as "limitless" by both parties, concerns a wide range of fields, such as national defense, foreign policy, energy and trades. It is undeniable that the most important common denominator between the two countries is the opposition against NATO and, more specifically, the US supremacy, to which both want to become a valid alternative in international relationships.

Furthermore, the situation between Russia and Ukraine is very similar to the one between China and Taiwan, an independent, democratic and economically flourishing island off the coast of the former and on which China has never concealed its expansionist ambitions.

Foreword

I am more than happy to present to you the BESA Times' third edition. BESA is a place where you can share, discuss, and create. One of our core activities is the creation of this magazine in which each one of us has the possibility to express himself or herself. The members of our Research team provided insightful articles about the world's economy and its link to geopolitics.

We aim at delivering different perspectives and opinions regarding past, current, and upcoming situations. The BESA Times is our way to share our thoughts and analysis on the topics we care about.

I am thrilled to be presiding BESA and I am very proud of what our team has accomplished last semester. It is a continuous pleasure to meet up with our members during roundtables to discuss interesting topics. I want to thank both the Research team members for their qualitative and relevant output and the Marketing team members for making this possible.

Looking forward to getting the next semester start and to welcoming new passionate members.

Enjoy your reading!

Tess Coullon,
President of BESA

BESA
Bocconi Economics Student Association

The Summary:

The FTX Fallout and What It Made Us Rethink of Trust

By An-Binh Bui

FTX, the crypto empire built by Sam Bankman Freid, who was once compared to titans of finance like John Pierpont Morgan and Warren Buffett, collapsed last month
after a deposit run that left it with an $8 billion shortfall.

On one hand, the damage has rippled across the crypto industry, destabilized other companies, and sowed widespread distrust of the technology. On the other hand, it made us reflect over how common tech fallout recently came down to one point of failure: the blind faith investors put in the founders/CEOs' abilities.

Crypto, a runway off the problem of trust?

Finance and mostly everything in our modern life can be transmitted into databases that are controlled by banks, governments, and corporations. As we depend heavily on databases, we have to trust the institutions that control them. However, after the 2008 financial crisis, trust in those institutions, especially baking, has faded. That was when Satoshi Nakamoto came along with the Bitcoin white paper, which created the first cryptocurrency. Crypto allowed direct transactions between two willing parties without a trusted third party, and this founded the way for shared databases using "cryptographic proof instead of trust" to our world.

Worth zero dollars when just invented, Bitcoin at its peak last November was valued more than $67,000 dollars. The total value of crypto in circulation peaked at $3 trillion. People who got into crypto early turned rich, and that convinced more to trust that trustless system, where FTX was once one of largest, and fastest-growing crypto exchanges. Along with Binance, FTX accounted for most global cryptocurrency trades and was valued at $32 billion in its latest funding round in January 2022.

In November 2022 however, as political arguments blared between Mr. Bankman-Fried and Mr. Zhao (Binance's billionaire founder), Binance has yanked more than $500,000 worth of FTX tokens. This initiated a series of sharp declines for FTX, as investors fretted about the stability of the sector and the financial health of FTX.

In one week, the token's value cratered from $22 to $0 and drove FTX to bankruptcy. This in turn triggered price shocks across crypto-firms and investors, which revealed further loose practices and rampant risk-taking.

The Cult of Founders

In the spectacular downfall of FTX, millions of fingers were pointing at its founder Sam Bankman-Fried.

Before the fall, Bankman-Fried was himself globally eminent. To the outside world, he was the outspoken "mayor of cryptoland" on a mission to convince regulators, investors, and enthusiasts of the new finance. FTX, his cryptocurrency trading exchange, used algorithms that cross-check positions and risk within milliseconds and protect customers from bad trades, he said. FTX did look like a safe bet in an otherwise volatile industry and has attracted billion dollar funding from major financial players such as Sequoia and Temasek to fund its growth.

FTX turned out to have lent huge sums of money to another trading firm owned by Bankman-Fried. This, surprisingly, has remained an oversight for Sequoia, who handed FTX money without carefully examining the exchange's numbers.

This phenomenon is sometimes called the "cult of the founder", a belief in the maximum leeway for founder/CEOs to run their companies as they see fit. The idea has been floating around since at least the 1970s, but it only took off in the late 2000s as Steve Jobs led the stunning turnaround of Apple and Mark Zuckerberg founded Facebook's success. In 2005, Peter Thiel translated this belief into a business model.

He started the Founders Fund venture capital and wrote his book Zero to One arguing for entrepreneurs' godliness. He made it a fully fledged religion, where founders are exceptional, especially those who behaved weirdly, by breaking norms or ignoring laws — they were extra exceptional.

Crazy might it sound, the idea then became conventional wisdom within the wide swaths of venture finance. Later we saw Adam Neumann of WeWork Inc., who profligately vaporized $15+ billion in the firm's investor capital and this summer still got $350 million from the top venture capitalist Marc Andreessen, predicated on "little more than a hazily sketched-out business model, [apartment buildings] and [questionable track record]", quoted Max Chafkin on Bloomberg. We also saw Andy Rubin, the Android creator who Andreessen keenly backed despite his extramarital affair and accusation of sexual misconducts ("s" capitalized, literally). Then in 2014, we had that echoed on Elizabeth Holmes and her $9 billion blood-testing startup – frauds all covered up beneath the Stanford drop-out, Silicon Valley material labels, until they were exposed.

Likewise to Sequoia, many of Bankman-Fried's red flags were seen as proof of his ingenuity. He was seen playing League of Legends in one FTX's major pitch. On the "Odd Lots" podcast in April, he also didn't bother to refute the question about his business as a Ponzi scheme essentially, saying that it was "completely reasonable" to assume many crypto assets are "worth zero." Axios even wondered "if FTX even has a board of directors, audit committee, CFO or chief compliance officer." Sequoia yet thought this was cool and marketed this as an extraordinary kind of financial foresight.

In the end, we saw that VCs love bucking convention — or at least being seen as doing so. The trust they gave to founders, the trust investors gave VCs, and the burgeoning trust we gave to the newfound cryptoland – now it caused customers to lose money and workers to lose jobs. Who is going to bear the responsibility?

Labor markets in the post-pandemic world: from surplus to shortage?

By Francesco DeLuca

Everyone agrees that a prosperous country needs a constant supply of human capital to keep stimulating economic growth. More importantly, and this is particularly true for developed economies, we want workers to be as skilled as possible.

The logic behind this principle is very simple: when there is an adequate supply of labor (which means, a supply of labor that exactly meets the demand for workers), then the economy will be able to run at full capacity. Ideally, in a developed economy, the demand will be mostly for skilled workers, which on average produce a higher benefit for the rest of the society, as Enrico Moretti shows in his book "The new geography of jobs".

However, in the real world, we rarely see a perfect balance of demand and supply; we usually hear about the latter being higher than the former, which often leads to unemployment, but also creates stronger competition among workers, thus encouraging them to get more skilled.

Nonetheless, in recent times, we have witnessed a rather peculiar phenomenon in some developed countries, namely an unprecedented labor shortage; numbers speak clearly: in the US the latest data show 11.3 million job openings, but only 6 million unemployed workers, in Australia up to 85% of businesses say they are facing staff shortages, while Canada hit an all-time high of almost 1 million job vacancies in the third quarter of 2021.

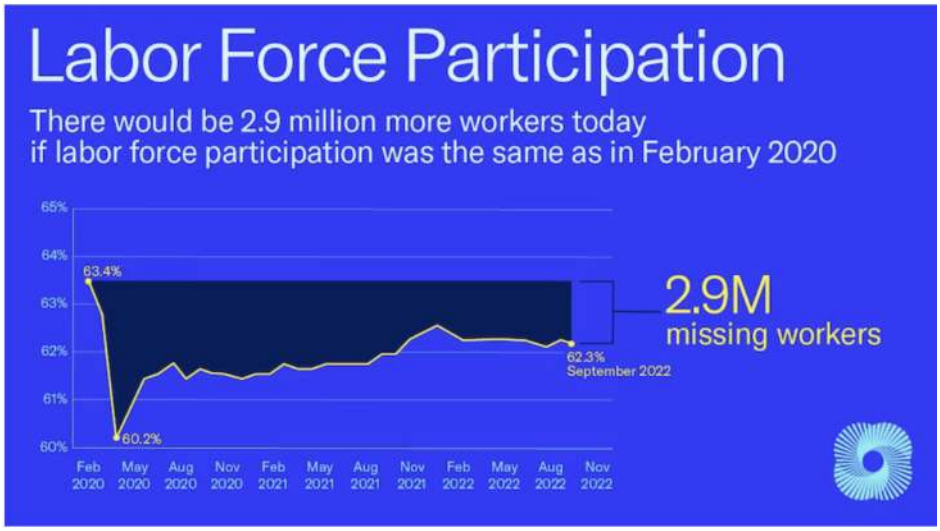
Already in 2014, some researchers from the Boston Consulting Group stated that, following the trend at the time, many countries were going to face labor shortages by 2020 (Germany, Brazil), and many more by 2030 (China, Italy, Canada); unfortunately, the trend worsened instead of improving, mainly due to the pandemic and the resulting economic meltdown.

The key drivers

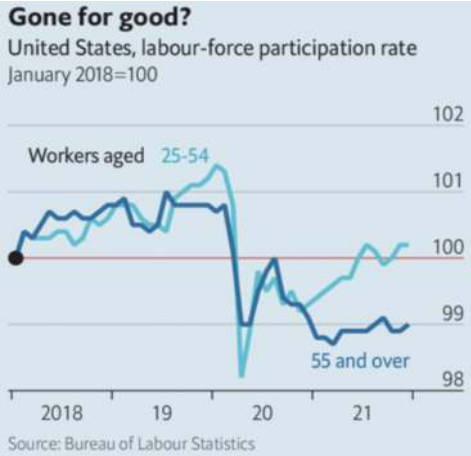
In general, to understand what determines labor supply, we need to look at a series of key drivers that can strongly influence workforce imbalances. One of them is demographics: even before COVID hit, several rich countries were already struggling with a shrinking workforce, due to extremely low natality. Some countries like Japan and Italy started experiencing this decades ago, whereas countries like South Korea and Germany only in recent times, but the witnessed effects are the same: as the workforce ages, more people retire, and the ones who keep working become less productive as time passes.

However, natality is not the only driver, since there are many more factors that can push the labor supply up or down. For example, an almost perfect substitute for high natality is a high immigration rate: importing talent from abroad is always extremely convenient since it allows one to reap the benefits of the investment that another country has made in the education of that worker.

Another possible way to tackle the issue is by increasing the labor force participation rate, i.e., convincing the ones that belong to the working population, but that have decided, for one reason or another, to stop looking for a job, to enter the labor market again.



When a country cannot achieve that either, the only way to keep the production of goods and services at such a level that meets the demand for those goods and services is to make workers work harder and for longer, which, in economic terms, can be translated to increasing the retirement age, increasing the weekly working time or increasing labor productivity (through technological change or in some other way).



Labor shortages: real problem or scaremongering?

Contrary to what is mostly emphasized in mainstream media, labor shortage can impact on the economy at least as bad as unemployment – a result of labor surplus. A lack of workers can trigger a harsh cascade effect: when an economy nears full employment it exhausts the space for further economic growth. Moreover, the demand for goods is high, while there are not enough workers to fulfill it, which consequently increases wages and prices. According to recent research from the Boston Consulting Group, the phenomenon may also reduce a country's competitiveness by disincentivizing workers to increase productivity and by making it harder for new businesses to hire workers and grow.

The COVID-19 pandemic made the situation worse by amplifying some negative trends tied to 3 key drivers of labor supply previously described: demographics, labor participation and immigration.
Firstly, due to concern about job security and money, birth rates have fallen. Many big countries such as Italy, Japan and Germany have had falling natality rates for decades (in 2020 they registered 1.30, 1.36 and 1.61 children per woman, respectively). However now, as most economies find themselves in a bad place because of the pandemic, the situation looks even grimmer and with little hope for improvements.

Secondly, while employers expected workers to eagerly get back to work once restrictions were lifted, these expectations have been defeated due to workers realizing the benefits of a more balanced work-life environment. Workers demand more flexibility from their employers, in an attempt to reclaim more time for themselves and their family. Moreover, many women, who often are still the ones who take care of the house, had to leave their job to look after their kids, thus being driven out of the labor market. The consequence is a lower labor participation rate compared to the pre-pandemic situation: at the moment, the US has 3 million less workers than it had in 2020, which represents a 2% contraction of the labor force.

Finally, due to the pandemic, most countries closed their borders to migrants, who make up an important part of developed countries' workforce: according to Mr Zaiour and Mr Peri, two researchers at the University of California, in the US "an industry with a 10% higher dependence on foreign workers than another industry in 2019 typically had a 3% higher rate of unfilled jobs in 2021".

As in most complex situations, there is no one-size-fits-all solution, so the best way to proceed is to look at each labor supply driver and try to improve them. The issues are numerous, but so are the possible solutions: better welfare interventions for childcare to incentivize young couples to have children, more investments in the development of new technologies to boost productivity, facilitate immigration, encourage people to get back to work by offering them more favorable conditions (work from home, less working hours) and so on.
It is unclear whether these trends are just temporary, however this situation gives us a glimpse of what the future labor market is going to look like if governments do not act now.

Income Inequality and Recessions

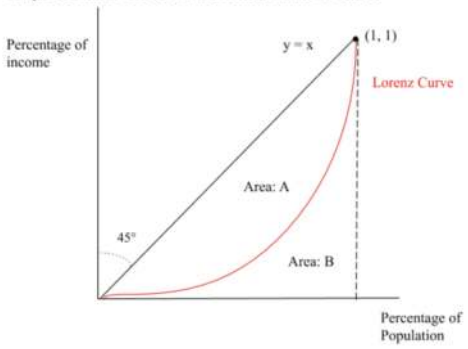
By Francesco Di Domenico

Do the poor get poorer in a Recession?

Economists nowadays face several problems on how to break a nation's poverty cycle. Income inequality is utilized to observe the uneven distribution of new earnings within a nation's wealth to assess the nation's well-being. Although economists believe in different schools of ideology, income inequality gives insight into the extent the government should intervene within the economy to prevent the masses from being affected by poverty. However, since poverty increases in economies under a recession, a period of six months or more where a nation's Gross Domestic Product (GDP) is negative, will income inequality also increase?

The Lorenz Curve will help us understand this process. The Lorenz Curve is a graphical representation of a country's income distribution utilized by economists as one of the methods to assess the well-being of a particular country. It is a plot of the cumulative income against the cumulative population. The 45° line, denoted on the graph below as y = x, is the representation of complete income equality, in which a person's income is equal to the mean income. The closer the Lorenz Curve is to the line of equality, the more equal the distribution of income across the population. The graph below is an example of a normal Lorenz curve of the United States in year K.

Graph 1: Lorenz Curve for the United States in Year K



Assessing income inequality of a year will require calculating the area of the triangle (represented with area A + B) and negating it by the area below the Lorenz Curve (area B) to get area A. Area B will be found by taking the integral of the Lorenz Curve function considering its domain restriction to be [0, 1]. The Lorenz Curve has this restriction because the population and total income cannot exceed 100%. Area A is then used to find the Gini Coefficient, a measurement of income inequality in which 0 represents perfect equality and 1 perfect inequality.

$$\text{Gini coefficient} = \frac{A}{A+B}$$

Although this analysis could be done with any country, the United States best represents a mixed economy. Analyzing a mixed economy is most appropriate when deriving a conclusion because most countries follow this economic system.

To avoid repetition this small investigation will assume that each year's Lorenz Curve will take the form of the graph above. Although the Lorenz Curve functions will not be the same, the graph serves as an overview.

The impacts of a recession on income inequality will be most evident when comparing two time periods: the year prior to the recession and the year the recession ended. This section assumes that an expansionary period is exactly one year before the recessionary period because the average recessionary period is about one year as shown in Table 1.

Table 1

Recession	Length of Recession (in months)	Average Length Period of a Recession (in months)
1980 Recession	7	12
Energy Crisis Recession	17	
Gulf War Recession	9	
Dot-com Recession	9	
The Great Recession	18	

The Bureau of the Census 1992 report claims a similar value of 0.403 for the Gini coefficient. Another source, still written by the Bureau of the Census but issued in 2000, claims the value to be 0.331. This inaccuracy made me eager to verify both sources. I further researched the methodology of the 2000 report, which revealed that the authors were using another formula to calculate the Gini coefficient. While the 2000 journal accounted for government taxation on income, the 1992 report did not. Henceforth the Gini coefficient ranged from 0.300 to 0.400. However, we will consider Gini coefficients not accounting for income tax because the Lorenz Curve is based on percentages of distributed untaxed income and not disposable income.

It is important to note that the impacts of a recession on an economy will not only be evident when the recession ends, but also in the years after the recession itself. The Dot-com Recession reflects this feature more than the other recessions.

The data below illustrates that the Gini Coefficient decreases after a recession arises. The Great Recession follows the same pattern as the 1980 recession, the Gulf War recession and Dot-Com recession. While the Energy Crisis might be an outlier, the data proves that recessions, although harmful to the economy, result in greater income equality in a country. Economists explain this phenomenon by analyzing the rate of wealth between the bottom and top 20% of the income population. As the country becomes poorer, the wealthier 20% of the population lose money at a faster rate than the other lower-income groups.

Recession	Gini Coefficient Reported by U.S. Census Bureau **for years of Expansion**	Gini Coefficient Reported by U.S. Census Bureau **for the year of Recession**
1980 Recession	0.404	0.401
Energy Crisis Recession	0.396	0.406
Gulf War Recession	0.424	0.421
Dot-com Recession	0.466	0.462
The Great Recession	0.461	0.457

In general the rich are not becoming wealthier compared to an expansionary period because the aggregate demand is lower as the whole economy is shrinking. Although the Lorenz Curve does not present enough information of the recession's scale, the bottom 20% of the income population will still be the ones to suffer most because they make less income than before the recession. Hence the government should still impose policies to help the lower-income households. Yet, over time the effects of the recession will lose significance and income inequality will continue to rise, assuming that the government policies stay the same and have little redistributional wealth plans.

Are Central Banks truly responsible for inflation ?

By Clément Fromageat

The main Central Bankers, Christine Lagarde president of the ECB and Jerome Powell chair of the FED.

If there has ever been a time in history where mainstream medias have communicated about inflation, it is our current period. Indeed, one solely needs to set his television on or open the social medias to see thoughts and takes from all sides of the political spectrum about the topic. However, there seems to be a common understanding among the general public that Central Banks directly caused our current inflation that is now close to 10% in the Eurozone. Nonetheless, there are other factors to consider such as supply chain disruption, and the geopolitical state of the World, all in a post-pandemic context.

Inflation is a phenomenon affecting the price of the goods and services produced by firms for consumers. For instance, a rise in the price of rents, food, and transports are drivers of inflation. However, a rise in the price of financial products or real estate does not count as inflation as they are not part of the basket of goods measured by the Consumer Price Index (CPI), the main measure of inflation used by the statistics institute.

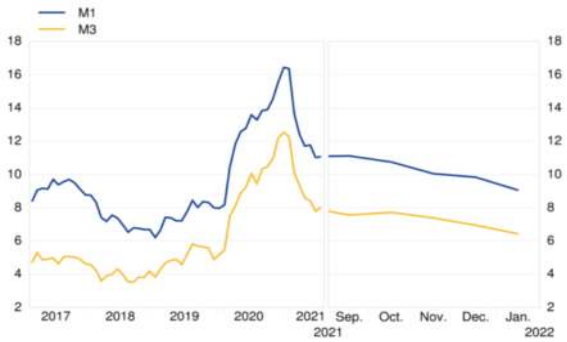
Furthermore, it is necessary to indicate that inflation is measured annually. Indeed, 10% of inflation in June does not mean that the prices gained 10% in one month but rather that since June of last year prices have increased by 10%. Another remark is that inflation is measured by the CPI: an average of the prices of more than 94,000 goods and services ranging from sectors such as food, energy, transport, apparel or even education. Thus, some prices can raise while others will diminish.

Now, why is inflation a concern? Firstly, obviously if prices increase faster than wages, the purchasing power of consumers allowed by their salaries or their savings decreases, causing a blow to the demand.

How does the Central Bank impact inflation?

The setting of prices is linked to the relation between supply and demand. And when it comes to inflation, this indicates two possibilities. Either the demand is too high, or the supply is too low, and this is when Central Banks come into play. Indeed as we know, Central Banks are the suppliers of money in the economy and thus we can think intuitively that by increasing the money supply with the economic measures taken during the pandemic, the demand for goods has risen past the supply, causing inflation. To represent these measures, this graph represents the money supplied by the ECB (M1 and M3 are just the names of monetary aggregates).

Nonetheless, the quantity of money circulating in an economy can only cause an increase in demand if it ends up in the hands of people willing to consume. Indeed, the main tool used these days by Central Banks to increase the money supply is quantitative easing which consists of purchasing securities in order to reduce interest rates and move the savings from the financial markets to the bank accounts of consumers.

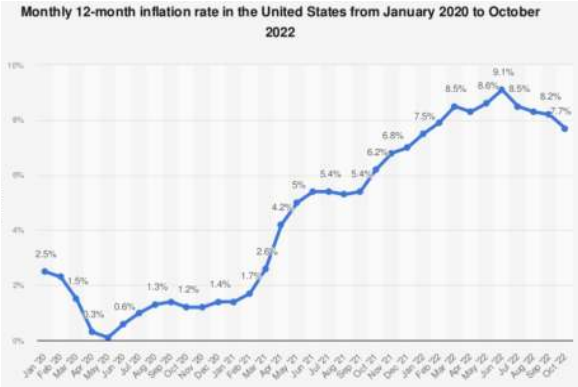


One could then ask how the purchase of securities by the ECB is going to lower interest rates? Well, by purchasing those products, the Central Banks are increasing their price, and by doing so the yields of securities decrease and as the yields serve as a basis to establish interest rates, it affects them at the end of the chain.

Coming back to our inflation issue, the lower interest rates combined with a transfer of savings to the real economy should trigger a higher demand. But this would be ignoring one major fact, the capacity to consume does not necessarily coincide with a willingness to consume.

However, if we look at the data, we notice that the Fed and the ECB started their QE programs 6 years apart (2008 for the US, 2014 for the EU) but inflation increased simultaneously. Looking at other economies, the Central Bank of Japan has been one of the first ones to implement QE in 2000 following their financial crisis in the 90s. They haven't had any inflation to this day.

Nonetheless, we still have surging inflation currently in our economies as shown on this graph representing the US inflation rate.



So, what are the drivers of inflation if not a surge in demand?

Demand is not responsible for inflation, so let's take a look at how supply side policies can affect inflation. Firstly, the biggest contributor to inflation is linked to an increase in the price of oil due to production levels decreasing during the pandemic to meet the much lower demand that still hasn't caught up with their pre-pandemic levels. Moreover, the war between Russia and Ukraine also has triggered this phenomenon as Russia was the 2nd biggest producer of oil in the world with an average of 10 million barrels per day in 2022.

Another of the main drivers of inflation these days is the increase in the price of food. But why is that? The main tool allowing us to produce food are ammonia-based fertilizers which we get by burning fossil fuels. A similar issue is faced with Russia which is currently the 2nd largest gas producer in the world, the war with Ukraine having caused a blow to the supply, which in the long-run increased food prices. Moreover, the conflict also increased food prices with Ukraine being the 3rd largest cereal exporter before the war started and now being unable to export (an agreement has been found between the two parties to let part of the Ukrainian cereal reserves leave the country through the Black Sea but it remains far inferior to the pre-war levels).

Therefore, we can conclude that even if the Central Banks increases in money supply might have accelerated the inflation phenomenon, they are far from being the sole cause for inflation as those measures have been in place for quite some time, without triggering a surge in inflation. Indeed, drivers of inflation can be identified as supply chain issues with meeting back the pre-pandemic level as well as direct consequences of the war in Ukraine, the latter targeting directly both the food and the energy sector. This topic is especially important for the general public to grasp as it is now affecting the life of every single person, causing a decrease in one's purchasing power and thus a relative impoverishment of society.

The US dollar is stronger than ever: How is this problematic for the global economy?

By Argyro Charizona

The euro dipped below parity with the dollar for the first time in two decades. In fact, in October, the US dollar was stronger than ever due to the policies of the Fed to tackle inflation. This situation continues to persist now as foreign currencies, such as the euro and the pound, are still depreciating against the dollar. Therefore, people are wondering about one thing: How will this impact them and the global economy?

Why has the US dollar appreciated so much?

During the war between Russia and Ukraine, energy exports from Russia have been limited. The energy shortage has led to a significant rise in energy prices since a lot of countries are dependent on Russia. However, energy is a requirement of all industrial and non-industrial activities; thus, the general price level has increased dramatically, causing inflation to skyrocket. The Fed has tried to tackle it by raising interest rates, which discourages borrowing and encourages consumers to spend less, eventually calming down inflation. However, while the Fed has been raising interest rates aggressively, US assets are becoming particularly attractive to foreign investors due to their high returns. Therefore, foreign investors are buying US currency and increasing capital inflows, resulting in the dollar's appreciation.

How does this affect Americans and the global economy?

A strong dollar reduces the prices of imported goods and the cost of international travel for Americans. Large multinational corporations that operate in multiple countries have recently expressed concern that the rising dollar will reduce their profits because foreign sales lose value when converted back into dollars, making them less competitive with local firms as their products become more expensive overseas. By one estimate from Morgan Stanley, each 1% rise in the dollar index has a negative 0.5% impact on S&P 500 earnings.

According to Marc Chandler, Chief Market Strategist at Bannockburn Global Forex, a stronger dollar helps to reduce inflation by making imports cheaper. When the dollar appreciates, foreign sellers are more likely to lower their prices, resulting in lower pricing for imported goods purchased by Americans. However, according to current data, wages are not keeping up with inflation.

Furthermore, a higher currency can make US real estate more expensive for international buyers, making those investments less appealing. This should help reduce some pricing pressures in the housing market, which is good news for Americans looking to buy a house.

What does this mean for developing economies?

A strong dollar raises import prices in other countries, which might lead to inflation in those countries. The consequences for emerging economies can be particularly severe. In fact, when interest rates in the United States are low, global investors tend to invest more in emerging markets, or economies that are transitioning into developed economies. However, when interest rates in the United States begin to increase and the dollar rises, money begins to flow out of those countries.

A strong dollar is also translated into a depreciation of foreign currencies as the value of the dollar is especially important for emerging economies since it increases their risk of debt default. Some developing countries are better prepared to deal with this because they have larger reserves or their exports are priced in dollars and have been rising in value, while others may suffer. Sri Lanka's economy, for example, is beginning to deteriorate as a result of a pile of debt and a lack of US dollars to pay for crucial imports of goods.

Countries that borrow significantly in dollars may suffer as repayments become more difficult when the dollar appreciates and their currencies decline, according to Mark Sobel, the United States' chair of the Official Monetary and Financial Institutions Forum and a former top Treasury Department official. "That implies the amount of money they need to get their hands on to make payments increases", according to Sobel.
The dollar has become extremely strong in comparison to other foreign currencies, negatively impacting the world economy. However, it needs to be highlighted that the euro has recently improved since it began to rise in value in November. The situation will remain unpredictable until inflation slows to the point that the Fed no longer raises interest rates.

The weaponization of Finance and its effects on the US dollar

By Mohamed Maiteeg

How did the US dollar become central to the global economy?

Following World War II, what came out of the Bretton Woods negotiations was one of the first steps towards the ambitious modernization plan of the capitalist system. The American economy was virtually unaffected by the war and thus emerged as the leader in the post-war era. The system that emerged from Bretton Woods revolved around the dollar and the US capital. The US pledged to peg the dollar to the price of gold in return for replacing the gold with the US dollar as the global currency.

This system was further strengthened by the collapse of the Soviet Union, the establishment of the WTO and the move by many countries towards currency convertibility.

The excessive dependence on the US dollar was recognized in the negotiations. Subsequent technical analysis highlighted how complex and critical it is to manage a currency for both domestic and international purposes. Valery D'Estaing (Former French Finance minister) called it an "exorbitant privilege" for the US to be able to run trade and fiscal deficits virtually without limit, but of course with consequences.

Even though the gold standard collapsed in 1971, the dollar continued to function as the world's reserve currency. The dollar is still used primarily in areas of trade and investment, and by multinational corporations in their global operations.

Today, the US dollar continues to dominate with more dollars in circulation outside the states than inside. Two thirds of all dollars are outside the United States. In addition, markets such as oil and minerals are almost entirely based on dollars leaving countries such as Russia and Saudi Arabia particularly vulnerable to the weaponization of the dollar.

How could the dollar be weaponized?

We witnessed Russia's particular vulnerability to the US dollar after its invasion of Ukraine. Two days after the attack the G7 countries announced they'll impose painful sanctions on Russia and freeze nearly half of its $600 billion in foreign reserves. The western alliance also limited Russia's access to the SWIFT payment system - though they made exceptions to sustain trade in key commodities such as oil, gas and wheat. Such sanctions and measures have been taken before on countries such as Afghanistan, Iran and Venezuela. However, this round is different, not only in the force and scope of the sanctions package, but also because it targets a major world power, Russia.

The actions taken by the western alliance signalled to the world that each country's access to its reserves could become unreachable based on its foreign policy. Of course, we are in exceptional times and moves such as the invasion of Ukraine are unprecedented actions that require unprecedented reactions, and a skillful move such as the sanctions package crippled Russia's ability to trade in international markets. However, Sergey Lavrov, the Russian foreign minister labelled the move as "theft" while Volodin, speaker of the Russian Duma lower house stated that "This is the beginning of the end of the dollar's monopoly in the world".

To what extent are these statements true? Is the weaponization of the US dollar going to lead to its downfall? After the pandemic and the war on Ukraine the global debt surged past the $300 trillion mark. The world today is highly financialized and most of this debt is denominated in US dollar. Any change to this ecosystem would have far reaching consequences in international finance. Ben Bernanke, the former chair of the Fed, highlighted that the centrality of the US dollar fosters safe, liquid and stable markets with a lender of last resort in the US government. Since the post war period, the US dollar has been central to the growth of international trade and this growth is at risk of loss in case this centrality fades away. With this being said, any changes to the current system will require changes in global trade and supply chains.

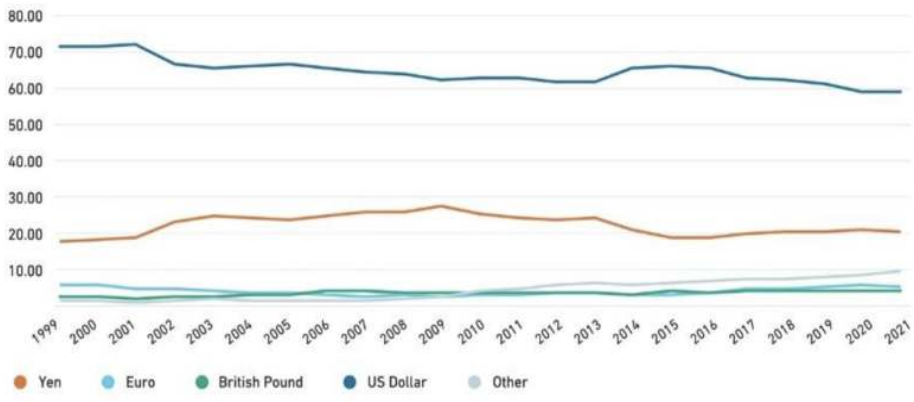
Nevertheless, the actions taken by the states against Russia have dramatically increased the readiness of the United States' adversaries to reduce their exposure to the dollar. The dollar has been declining as a foreign reserve currency for the past two decades, down from 70 to 60 percent over that period. There has been a shift towards non-traditional reserve currencies and to a lesser extent the Chinese renminbi. Figure 1 below shows the slow but steady decline in the use of the US dollar as a foreign exchange reserve.

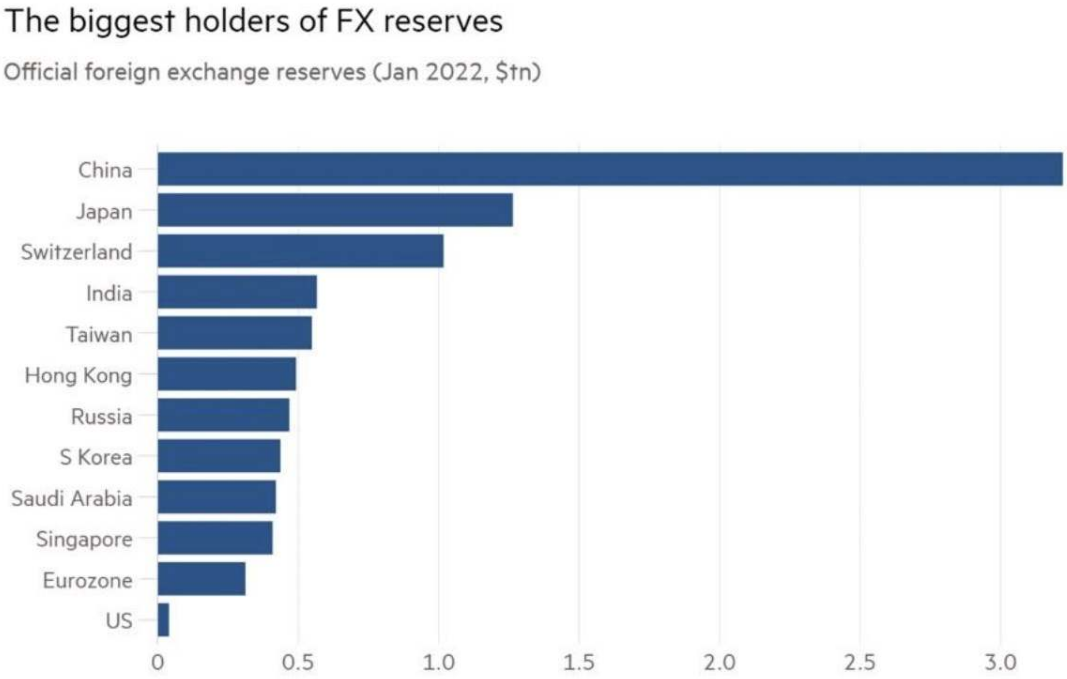
The slow erosion of the US dollar:

There are several factors at play leading to the decline of the US dollar. First, most of the fall in the use of the US dollar is diversion of assets towards currencies outside the big four (US dollar, British pound, Japanese Yen and Euro). These currencies historically weren't a viable option for foreign reserves as they did not have deep markets and came with high transaction costs. However, due to technological progress and the establishment of electronic trading platforms - automated market making (AMM) and automated liquidity management (ALM) - decreased the transaction costs substantially and deepened the markets, allowing currency reserve managers to safely adopt them in their portfolios.

The second factor causing the US dollar erosion as a reserve currency is the change in the investment strategies taken by reserve currency managers. A foreign exchange reserve is composed of an "investment tranche" and a "liquidity tranche", the latter being held to meet any contingent situations in case there is a balance of payment crisis. In recent decades, the investment tranche has grown to a sizable percentage of the reserves. The IMF conducted a survey at the end of 2017 on 55 emerging market economies and found 30 with excess reserves. In the 30 countries, the total reserves exceeded IMF's minimum reserve levels by 58% on average. This sizable excess in reserves is fuelling the diversification towards non-US dollar assets. The figure below shows the biggest holders of foreign reserves.

Figure 1: Currency Composition of Global Foreign Exchange Reserves 1999-2021 (as percent)





Various other factors are leading to the slow erosion of the US dollar. After the invasion of Ukraine, commodities that were primarily priced in US dollars are now priced in other currencies. Russia is now requiring "unfriendly nations" to pay for commodity exports in rubles. On the other hand, Saudi Arabia had talks with China on the possibility of pricing oil exports in Renminbi. Thus, we are seeing a gradual move away from the US dollar in the invoicing domain.

Ultimately, the unparalleled weaponization of the US dollar against Russia serves to accelerate financial fragmentation. Even though it's not possible to move away from the current centrality of the US dollar, the current structure can change gradually over time. However, the economic costs of such a change, especially if taken into consideration with the broader effects of the deglobalization that comes with it, may be very high.

The collateral damage of Russian Sanctions on Central Asian nations

By Alessandro Marti

The detrimental effect of the West's sanctions on Central Asia:

The sanctions imposed by the West on Russia are having a significant impact on Central Asian nations, which are heavily reliant on Russia's economy. The secondary effects of the economic penalties levied against Russia on Central Asia have been overlooked by Occidental policymakers and have destabilized vulnerable states that are dependent on Russia. The Central Asian Republics (CARs) – Kazakhstan, Uzbekistan, Turkmenistan, Kyrgyzstan, and Tajikistan – have deep socio-economic ties with Russia, which have been maintained since the collapse of the USSR.

Western policymakers have neglected the destabilizing power that such sanctions can have on dependent and vulnerable states, both from an economic standpoint as well as from a social and political standpoint. Occidental policymakers should look to mitigate the devastating impact that Russian sanctions are having on CARs which have unanimously taken a neutral stance in the Russo-Ukrainian war. Mitigating the devastating impact of the sanctions on Central Asian nations would not only be a charity, as it could also help strengthen Western influence in the region, prevent radicalization, increase political stability, and prevent China from increasing its influence in Central Asia.

The impact on Central Asian economies:

The extent to which Central Asian economies depend on Russia is not to be underestimated. In addition to Russia being one of, if not the primary trade partner for most of these countries, the economic ties that CARs have with Russia are embedded deeper within Central Asian economies. The extent of Central Asian dependence on Russia can be highlighted by the remittance-dependent economies of Tajikistan, Kyrgyzstan, and Uzbekistan, where remittances, respectively, make up 28%, 30% and 15% of their GDP.

These remittances are, to a great extent, coming from Russia. The sharp decrease in the value of the Ruble has made remittances lose much of their value for those who have been able to keep their job, but for the rest, Russia's economic turmoil has forced economic migrants out of their jobs. As a result, around 40% of Central Asia's economic migrants in Russia have indicated that they are ready to return home. This mass exodus has already begun, with Bishkek, Dushanbe, and Tashkent, announcing that hundreds of thousands of economic migrants have returned from Russia.

The effect of this severe downturn in Central Asian remittances on the population of these countries is catastrophic. Without Russian remittances, the poverty rate of these Central Asian countries that have hardly been recovering from the pandemic is estimated to rise by around 50%. These remittance-dependent countries have already had a sample of this impact during the COVID pandemic, which also slowed down remittances to a smaller extent. Kyrgyzstan, for example, experienced more than five-hundred thousand people sliding back into poverty, and a 20% increase in food insecurity. The Russian sanctions are expected to have a more profound impact on these countries than the pandemic, and this impact should be considered by the West when imposing sanctions on Russia.

The close link that Central Asian economies have with Russia can also be highlighted by how the war affected Central Asian currencies. As the Russian ruble plummeted, the Kazakh Tenge lost nearly 20% of its value despite the Kazakh National Bank pouring in nearly 100 million dollars to preserve the currency. All the other CARs experienced similar drops in their currencies as the Ruble plummeted. This devaluation

of CAR currencies as a result of Russian sanctions is extremely painful to all CAR economies but especially painful to Kyrgyzstan, Uzbekistan, and Tajikistan, which are running on a trade deficit. An increase in import costs, combined with extremely high inflation, will further strain their economies. This will also increase food prices and exacerbate the number of severely food-insecure people in Central Asia, a number that has already grown by seven million in 2020 due to the pandemic, and has continued to rise rapidly since the beginning of the war in Ukraine.

The political impact of the economic shortfalls caused by the sanctions on Russia will continue to destabilize Central Asian Republics (CARs) politically as well. Recent economic stagnation in Kyrgyzstan has allowed its democracy to fall prey to increasingly authoritarian rule, and Russian sanctions which will devastate the Kyrgyz economy are likely to be an opportunity for populist authoritarian leaders to strengthen control over the Kyrgyz democratic system. Moreover, a severe economic crisis is likely to exacerbate the brewing Islamist threat pouring in from Afghanistan into Turkmenistan, Uzbekistan, and Tajikistan, as poverty is a primary driver of radicalization.

The sharp decrease in the value of the Ruble and the imposition of sanctions on Russia have had a devastating effect on the economies of Central Asian countries, particularly those that are heavily dependent on remittances from Russia. The resulting economic shortfalls have led to an increase in poverty and food insecurity, and have destabilized the political landscape of these countries.

The West's imposition of sanctions on Russia has had a detrimental impact on the people of Central Asia, and it is important to consider the potential consequences of such actions. As previously mentioned, the proximity and eagerness of China to gain influence in the region may lead these countries to look to China for economic assistance, which could result in an increase in Chinese control in Central Asia.

An opportunity for China:

The proximity and eagerness of China to gain influence in the region need to be considered by the West as well. Through the Belt and Road Initiative, China has been building influence in the region and the West needs to consider its ramifications with more urgency. As Russian sanctions plunge CAR economies into budgeting shortfalls and political instability, these countries may be forced to look to China for a lifeline, which could result in a sharp increase in Chinese control in the region.

CARs, which have already been given unfavorable loans by the Chinese government, will be increasingly inclined to take extremely unfavorable loans from China. This will unquestionably increase Chinese control in Central Asia. It has been shown that countries that take on such Chinese loans often fall deeper into economic trouble, hindering potential future economic growth with crushing debt. This makes sovereignty from an authoritarian superpower - China or Russia - in the near future difficult to achieve. It is important to note that China's influence in the region could have long-term consequences on the political and economic stability of the region, and the West should be aware of this.

What can the West do?

The West can begin placing more importance in considering the collateral impacts of sanctions levied against enemy nations and taking a more holistic approach to foreign policy. Occidental states could mitigate the impacts that sanctions on enemy states have on allies, neutral nations, and innocent nations by integrating plans to reduce the economic devastation in Central Asia. By giving Central Asia a lifeline, NATO countries could strengthen democracy in the region and gain influence.
There are a variety of options available for the West to explore. Providing economic assistance and aid, promoting investment, and supporting local businesses and entrepreneurs, are all potential ways to mitigate the negative effects of sanctions. Additionally, supporting democratic development and civil society in the region could be a key step in ensuring stability and prosperity in Central Asia. It is important for the West to find ways to support the development of Central Asia while also achieving its foreign policy goals.

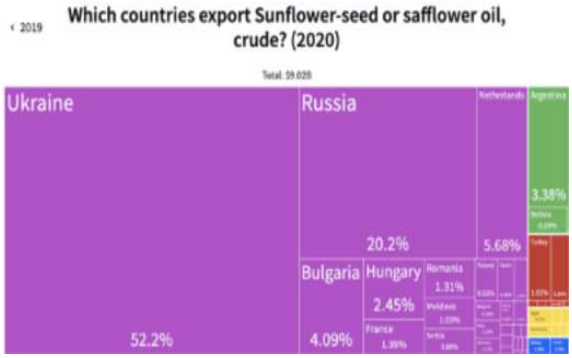
Implementing sanctions against governments, such as the Russian, Syrian, Iranian, and Eritrean governments, that carry out wars of aggression, human rights violations, and war crimes can arguably be justified, though evidence for their effectiveness is, at best, unclear and circumstantial. Nevertheless, the West could adopt a more holistic approach to implementing sanctions -not only for Central Asia but for all sanctions going forward-. The West could consider the crippling ripples that sanctions on enemy states have on countries with strong economic ties to the enemy state. Implementing harm mitigation plans for nations that are innocent, but impacted by sanctions, could make Western sanctions more justifiable from an ethical standpoint. It would also offer the West an opportunity to deepen ties with the vulnerable and innocent nations in question. By increasing their economic and political power within those nations, and helping them stabilize and democratize, the West would be able to reduce the risk of potential human rights violations and wars within those nations while benefiting from a foreign policy standpoint.

Why is the Black Sea Grain Initiative important?

By Duru Gülsaran

Increasing prices have been a regular trend but especially in the past couple of years, back-to-back crises in the World have been increasing the costs of living more significantly. The covid-19 pandemic, increasing effects of climate change, regional conflicts, and most recently the Russian-Ukrainian War have been acting as catalyzers to price increases. The war had, and still has, devastating effects on both countries' economies due to increased military expenditures as well as decreased production caused by the shifted human capital and emigration in Ukraine and wide sanctions imposed on Russia. However, the contracting economies of both countries have far reaching consequences. The rest of the World, especially the economically less developed countries, is at risk of never-before-seen high inflation.

Ukraine and Russia are both significant exporters of grains as well as other food staples. According to 2020 data, the two countries hold around 28.5% of the world's wheat, 19% of barley, 14% of corn, and 72.4% of sunflower-seed or safflower oil crude exports globally. In addition, Russia holds 14% of the fertilizer export which has -again- huge effects on the supply of agricultural products.



Previously, the route following the Black Sea through the Bosphorus Strait to the Mediterranean was commonly used by exporters but since the start of the war, some Ukrainian ports are occupied by the Russian army to stop any Ukrainian activity -civilian or military- and the ones remaining under Ukrainian control are closed for safety reasons. At the ports that can still work, ships of both countries were not able to leave the ports due to sea mines causing the shipments in the Black Sea to almost stop. With the blockage of its ports, exporters shifted to railways and road transport. The European Union tried to help by allowing the usage of the Port of Constanta in Romania and the Baltic ports. However, these initiatives were unable to meet the requirement with only 1.5 million tons of grain being able to exit the country -it was 7 million tons per month before the war.

The increased cost of transportation and goods being stuck at the ports affected the Middle Eastern and African countries that have sensitive markets and are largely dependent on Ukrainian grain. For example, in Syria bread prices have doubled, and in Yemen due to decreased supply of flour, bread prices rose by 42 and 25% respectively. In addition, the African Development Bank announced that 30 million tons of food deficit has appeared resulting in a 40% increase in the continent. Also, Ukraine has been the largest supplier of goods to the UN World Food Program, which provides commodities to underprivileged populations. According to the UN 2021 Global Report on Food Crises, published in 2022, 193 million people in 53 countries/territories have acute food insecurity trends and/or are at risk of famine, and it's at risk of increasing rapidly.

On July 22, 2022, the 120-day-long Black Sea Grain Initiative was signed by the UN, Ukraine, Turkey, and the Russian Federation in Istanbul. It was not a direct agreement between the Russian Federation and Ukraine but rather two different "mirror" agreements with the same name of "Initiative on the Safe Transportation of Grain and Foodstuffs from Ukrainian ports": the first between the Russian Federation, Turkey, and the UN and the second between Ukraine, Turkey and the UN. At the same time, another agreement was made for the UN to facilitate the transportation of Russian commodities and fertilizers to the global market. With this initiative, the UN aims for Russia to allow the transportation of the grain that is stuck in the Ukrainian ports through the Black Sea to help decrease world prices.

This initiative allows merchant vessels to pass through a safe maritime corridor from the Chornomorsk, Odesa, and Yuzhny ports of Ukraine with the guidance of Ukrainian pilot boats. As part of the agreement, a Joint Coordination Centre (JCC) was created in Istanbul, on July 27, headed by a Turkish admiral and a total of 20 delegates -five representatives from each party. The primary responsibility of the JCC is to monitor the vessels and to check the cargo and personnel (especially since Russia wants to make sure that the vessels are not carrying weapons or any kind of other support to the Ukrainian army).

On August 1st, the first ship left the port of Odesa and since then more than 360 ships have departed, carrying around 8.1 million metric tons of commodities. This way the global prices of food staples have declined by approximately 8.6% in July and 1.9% in August according to the Food Price Index published by the UN Food and Agriculture Organization. However, the decline rate fell as it was 1.1% in September and even started to increase again due to uncertainty about the future of this initiative.

The importance of this initiative was highlighted once again when Russia suspended its participation for an "indefinite period of time" on October 29th, claiming that Ukraine had used a cargo ship to conduct a drone attack on the port of Sevastopol and that the commodities were being transferred to Europe instead of the developing countries. World prices increased by around 6% but they did not rise more, as the markets were expecting such a move from Russia and prices were already rising again. After the phone talks between Turkey's President Erdoğan and Putin, Russia's Defense Ministry said they agreed to rejoin the deal after the U.N. and Turkey secured written assurances from Ukraine that the corridors would strictly be used for commercial purposes.

The deal was due to expire on November 19, but all four parties agreed to extend the deal for further 120 days without any changes to it. Ukraine's Minister of Infrastructure Oleksandr Kubrakov announced the extension from Twitter on November 17th followed by official announcements from the other parties.

Being one of the few things that the UN, Russia and Ukraine agree on, the Grain Deal allowed a milder communication between the parties. Given the success, a new question arises: Could this initiative be applied to other sectors to reduce world inflation even more?

The perseverance of the BRIC Alliance: The door to a multi-polar economy?

By Leonardo Bassino

The BRICS alliance: Brazil, Russia, India, China, and South Africa, are currently the main competitors challenging the economic and political supremacy of the current Atlantic powers. The US was already at the top of the world economies in the 1920s, GDP wise, but it was only after 1945 that it started leading the world towards the goals of what they refer to as freedom and democracy. The dissolution of the USSR in 1991 marked a moment in time where it was clear that two big fish cannot coexist in the small tank, one must go, and the remaining small ones better follow the survivor around to avoid being outcast. This was the reality of our world until recently somebody started to notice the US was tired of acting as the sheriff of our planet.

What makes China the primary competitor of the U.S.?

China is currently expanding its influence through countries across all continents. With a GDP of $18.32 trillion (nominal; 2022 est.). It is the second largest economy in the world, preceded only by the US which is, however, second to China when measured by Purchasing Power Parity (PPP). But PPP is not the only measure where the country leads: largest exporter, largest manufacturer, wider labor force and highest number of billionaires are just some characteristics attributable to the main Asian economy. Adjusted for inflation, China is already bigger than the USSR relative to the United States and without doubt a greater competitor in terms of economic power and influence. The Belt and Road initiative of the Chinese Government, a development strategy aimed at investing in more than 147 countries, is representative of the willingness of the country to develop its own expanded, interdependent market. The aggressive investment strategies aimed at African countries, based on the exploitation of the inability of African governments to repay their debts, has gained China control over countless infrastructures across the continent. The total loans from China to Africa are estimated at $153 billion between 2000 and 2019. Therefore, China can undoubtedly be labeled as the second big fish in the tank.

Who are the BRICS and how are they affecting the economy?

The rise of a new superpower is a game changer in terms of geopolitical equilibrium. The existence of a second economic pole opens opportunities to several countries that are waiting to be under the spotlight. The BRICS makes up the five countries currently leading as emerging economies. With a combined nominal GDP of US$26.6 trillion, 26,2% of the Gross World Product, through collaboration they share and build up a strong influence across the continents of Africa, South America, North-South Asia and Europe. The alliance's financial architecture is all towards investments, as we would expect given the presence of a superpower and 4 more or less developing ones. The New Development Bank is an international financial institution (IFI) headquartered in Shanghai and led by the five BRICS countries, whose primary aim is to provide liquidity to support public and private projects, mainly infrastructures, as well as establishing partnerships with other development institutions.

The NDB is the concretization of the ideology and strategy behind the foundation of the alliance: the creation of a multipolar world, with the support of all those countries that in the past did not get from the US and the EU the political and economic support they had hoped for. Maintaining the same fish metaphor, the BRICS are on the verge of creating their own shoal, eager to expand it and make it increasingly independent from the influence of the US. Paradoxically, the strongest bonds are being created between those countries that seek sovereignty and independence, and they are doing so joining the sphere of influence of a more advantageous superpower.

What was the response to the Russia-Ukraine conflict?

The BRICS alliance is currently experiencing a stress test. The 24th of February 2022 Putin declared war on Ukraine crossing its borders in what he calls a "special military operation." The response from the western world, in the form of sanctions, was almost instantaneous. Russian banks have been cut off SWIFT, the Central Bank of Russia is currently unable to access foreign-exchange reserves amounting more than $400 billion, and several sanctions have been imposed on individuals (oligarchs), politicians and companies. Many argue, however, that the underlying objective had always been the weakening of the Russian economy due to the ongoing economic warfare between the country and western powers, the attack on Ukraine being the geopolitical leverage allowing them to strike. Several analysts highlighted how the sanctions are far from a matter of principles, of which the US labels itself as main bearer, and more of a way to keep on a leash the Russian economy for the ongoing years forcing it into a recession. Russia is either drowning or slowly fumbling towards the surface, a process that may take decades.

What is clear however from the ongoing events is that the BRICS are strong in their alliance. On the 25th of February Brazil officially announced no sanctions would have been imposed on Putin's Russia. Xi Jinping's China, despite not supporting the conflict, has become the single largest buyer of Russian energy, Chinese exports to the country rebounded after a quick and steep decrease, but it was mainly due to Russian economic weaknesses and not related to decisions at a governmental level. India has declared formal neutrality over the events, in a "subtle pro-Moscow position." South Africa's government response is in line with the other BRICS members. The strategic political and economic decision of avoiding sanctions perfectly fits with the desire to see the balance of forces change to reflect the rise of emerging powers, despite indirectly supporting the invasion of a country for expansion purposes.

How does the current state of the world compare to the past?

Many highlight how the current period shares many characteristics with the Cold War period, however the differences offset the similarities and make the two situations overall very different. The current "contenders" of our world not only are strictly connected to one another and, to some extent, dependent on each other, but also, they play according to the same rules. Important to remember, for example, is the fact that China owns an estimated $972 billion in US Treasuries, strategically keeping the value of the Yuan low, and it can do so only through the large amount of owned reserved currencies.

The second main trade partner of Brazil is the United States (17.78% partner share), the same is true for South Africa, of which 8.6% of exports are directed to the US. India's first trade partner is, again, the US. The fact that all the BRICS countries are interconnected with western countries makes the so-called "economic warfare" a battle for aristocracy rather than monocracy. This is the natural path of globalism, competition tends to balance out differences and makes it disadvantageous for a country to become a threat, both economically and politically. A nation that does not play by the rules is deemed to fail, and Russia is the most recent example. The BRICS remain allies, but the current economic state has damaged not only their reputation, but economic negative externalities hit them too. The latter shows that the best strategy is not to act recklessly and bossy as a single economic and political power, but rather create strong bonds and economic agreements with other countries to the best of everybody's interest. The New Development Bank in fact does not only operate for the BRICS countries, but holds members such as Bangladesh, Egypt, Uruguay, and the United Arab Emirates. Holding good relationships with smaller countries with good growth expectations, makes up the scaffolding for new economic poles in different continents.

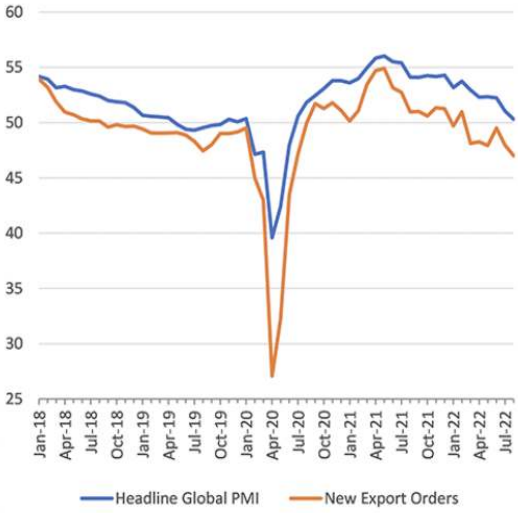
Everything considered, the BRICS are building up importance in the equilibrium of forces worldwide, attracting allies and widening their network of economic partners. Their objectives naturally clash with those of already existing powers, namely the US, the European Union, and their allies. The interconnection of today's economy discourages actions detrimental to others, as the backlash can turn out to be destructive, sanctions to Russia being the example. However, small actions such as remaining neutral in front of such delicate situations have the potential to add up over time and shift equilibriums in the long run, possibly leading to a more equal and multipolar world.

Is Globalisation a concept of the past?

By Philipp Ludwig

Current State of Affairs

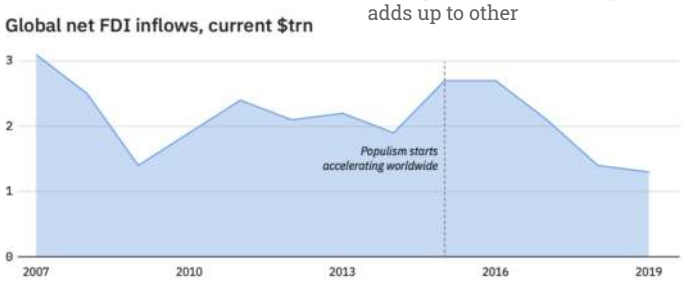
After the end of World War II, the world had not just entered a new chapter, it had begun a new book. The world order was completely rewritten, economic mechanisms were re-invented and world trade exploded in the centuries afterwards, with the highest growth of world trade of a total 300% over the two decades after. Globalisation was born and further expanded after the fall of the Berlin wall and the end of the Soviet Union. Our economic system as we knew it up until roughly three years ago was born and provided the western world with the comfort, we grew up in. The East, particularly China and Russia faced an impressive economic rise and increase in welfare. The outsourcing of production sites to other countries, such as China, was a key factor in the upscaling of businesses and brought the world further than one could have imagined after the battles and hostility in World War II.



However, not just, but in particular, after the election of Donald Trump, the world faced a challenge that became increasingly tough over the past years. "America First", to quote the former US president, illustrated threats to globalisation. It was followed by the COVID-19 crisis, a scenario no one was seriously considering, which shocked supply chains and created complete chaos in the world economy. Interrupted by a rather smaller issue of the blocking of the Suez-channel leading to another disturbance in global trade, tunnelling in the Russian-Ukraine War. This led to the complete isolation of the former soviet country and threw the whole EU, being dependent on Russian gas supplies, under the bus due to the explosion of energy prices. As figure 1 evidentially demonstrates, the Global Purchase Manager Index decreased more and more over the past years indicating a decrease in global manufacturing activity and trade of goods in general. Considering these events in recent years it seems like the economic system, as we know it, is at the verge of collapsing. But is that true?

America First

"The future does not belong to the globalists. The future belongs to patriots." A statement made by Trump in 2019 at the UN General Assembly. It clearly demonstrates how Trump's populism, and the views of his followers marked the beginning of an anti-globalisation movement from the very top of the economy, with the US being the largest economy in the world. His nationalistic politics focused on increasing America's power in the world and on making it "great again" in the sense of introducing a new type of protectionism. Soon he introduced several immense changes to the economic system of the US, which marked a step back from globalisation. This can be evidently seen by the sharp decline in global foreign direct investments of nearly one trillion US dollars, from roughly $2.5trn in 2016 (Figure 2). Trump's election, in line with other populist movements, marked the beginning of this decline. Apart from certain agreements that benefit the world in social matters, Trump also withdrew from the North American Free Trade Agreement, an agreement between the US, Mexico and Canada creating a free trade zone between them. Additionally, he began a trade war with China, where both parties imposed tax after tax on each other, heavily limiting the trade and therefore make companies in the US produce on their own. Furthermore, the trade war was also fought over intellectual property, it saw bans and restrictions in the US of Chinese brands such as Huawei and the limiting of Chinese investments in the US. Both countries isolated themselves from each other, leading to a rise of mainly tech investments in the Asian country itself than the US unlike before. One might think Biden has reversed the damage Trump has done and indeed he has re-joined the Paris Climate Agreement and created the USMCA, the replacement of the NAFTA, however, he also has introduced his own type of protectionism, "Bideonomics" as The Economist likes to call it. With his future as a president remaining unclear, considering his age and support from the US population, America has an unpredictable future. Meanwhile, Biden has continued to fight against the threat of a rising China, which led to investments as high as $1.7trn into inland assets, such as infrastructure or semiconductors. This has led to several resentful reactions from the EU side, for instance increasing investments in their own economic area, such as the chip industry. It becomes clear that Trump and Biden, both so different, yet so similar, have taken a step back from globalisation and increased protectionism of the US. And a major reason for this is the fear of being overtaken, economically speaking, by China.

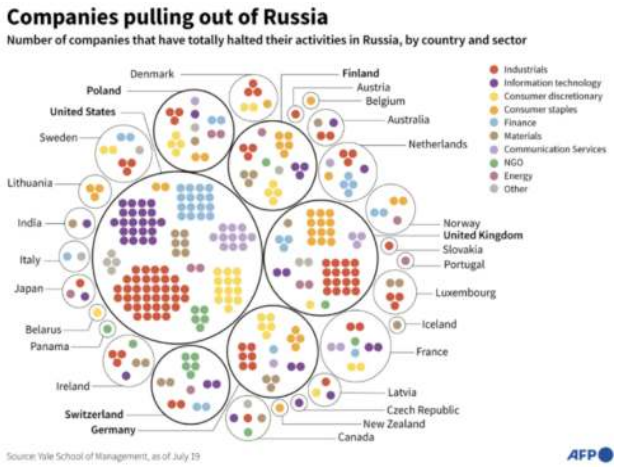


Lockdowns and iPhones

China is a marvellous example of how globalisation has the ability to create a global superpower from nothing. After opening up to global trade in the late 1970s it became one of the world's fastest growing economies, doubling its GDP almost every eight years and becoming a large holder of foreign exchange reserves. The obvious picture of China being a very important player in the globalised world economy arises. Despite their history of success, several factors are currently turning the table against China, of which some they have created themselves, others are due to a change in Western thinking.

"Designed by Apple in California. Assembled in China." A sentence many of us know, written by one of the world's most valuable companies, a company that embodies globalisation itself: Apple. Their main device, the iPhone, is made from parts from 43 different countries all over the world, excluding the supply of raw materials. All those components finally end up in a city called Zhengzhou, where their main factory, operated by their producer Foxconn, is located. However, just recently, at the end of November, violent protests at this plant occurred. It is not because of Apple or Foxconn themselves, but because of the actions of the Chinese government. The government has implemented a month-long restriction plan on the workers due to Xi Jinping's Zero-Covid policy, making their own people and workers suffer after a small outbreak of the disease in the factory. This is not a unique case but adds up to other events, such as the Lockdowns of major metropoles in the country, leading to foreign workers and businessmen fleeing the country. China is making itself unattractive. This does not result in the immediate pull back of any global company from the country, however, in addition to increasing prices of manufacturing, there is a noticeable shift. Continuing with the example of Apple: The world's largest smartphone manufacturer has already started producing some of their latest models in India, planning to increase the number to 25% by 2025. There are several reasons for this, such as the more attractive offers from the new manufacturing hub, but it is hard to ignore that production in China has become increasingly more challenging for global companies. Apple is not alone, other big players, such as Walmart, have announced similar actions in the past months. But not just American companies are having trouble with production in Asian countries, also European. Initially, when Covid started a shocking issue became evident in Germany: drug shortages. According to DW, 90% of active ingredients used in non-patented drugs come from China and a further 50% of patented drugs are at least produced with the help of the country. This outsourcing created the possibility of very low prices, which was inspired by health insurances. Shockingly, the last producer of Antibiotics in Germany closed down about four years ago. This created huge dependencies on China, which became an apparent issue during Covid when emergency storages were close to running out of stock. Clearly, a dependence in such crucial markets on countries on the other side of the world is not beneficial, especially when that country has a government as unpredictable as China does. This event marked how vulnerable globalisation made certain western countries and why this economic system bears huge risks. If China would eventually invade Taiwan and therefore trigger similar reactions to the ones the west had to Russia's invasion of Ukraine, the whole construct could collapse in itself, creating a world crisis never seen before.

Other Dependencies



However, the West is highly dependent on other countries for the production of many goods other than drugs. In order to run the energy system in the EU, especially in Germany, there is a tremendous demand for Gas and Oil, bought to 45% from Russia before the beginning of the war. It is obvious what happens if the biggest supplier of this good suddenly cuts its exports by 60%. Indeed, that happened in June 2022 as a reaction to the strong sanctions imposed on Russia by the EU. The results of this could be felt in the whole world when energy prices skyrocketed, driving inflation higher and higher, making the normal people's living more and more challenging. After Russia invaded their neighbour country, they triggered a global, mostly western, reaction of anger, resulting in the implementation of sanctions which isolated the aggressor from the whole western world. Globalisation became a concept of the past for Putin's country, seeing over 1000 companies leave the country in weeks. When in 1990 the first McDonald's opened in Moscow it was a historic step for the country towards the western world and was another link in the chain towards globalisation. Now, over 30 years later, the country stepped back from this historic event with McDonald's leaving the country again. These events illustrate another push towards protectionism of each individual country and the decrease of global partnerships in trade and knowledge.

The end or a new beginning?

After pointing out these issues, it might seem like global cooperation and trade must come to an end and has been a concept of the past. And indeed, in many aspects countries will have to change their approach. It is mandatory for governments to secure their supply chains, especially for goods that are crucial for people's health or the country's infrastructure, such as drugs or gas. Global players like China, Russia and the US have shown signs of drawbacks from the globalised world. However, this does not necessarily mean the end of international trade, but a reshaping of the structures we currently know. As the shift to new countries, such as India, creates new possibilities of global collaboration. The EU has proven its union in these past turbulent years. Perhaps now, following the peak of China, India will be the next BRIC country to rise. Alternatively, it might be the beginning of the increase of importance of the MINT (Mexico, Indonesia, Nigeria and Turkey) countries. Especially Indonesia, hosting this year's G20 summit, is a promising country to play an important future role in globalisation. We do not see the end of globalisation, but tremendous changes. Changes that do not just start a new chapter, but a new book. A book where every character has to determine its role. The coming years and decades will be determined by a different economic system, different politics and different international relations than those that shaped the last decades. This new book of the world after COVID-19 brings with it challenges and new opportunities.

How could the EU Taxonomy turn global trade upside-down?

By Claire Schumacher

The European Commission set a pretty ambitious objective with the 2030 Climate Target Plan of cutting greenhouse gas emissions to at least 55% below 1990 levels by 2030. And as the saying goes, desperate times call for desperate measures; this is where the EU Taxonomy comes into the picture.

What is the EU Taxonomy about?

The EU Taxonomy is a classification of sustainable activities. Indeed, to meet the EU's objectives, the countries need to allocate more resources to green activities. One could thus wonder: "what can be considered as green activities? How to discern them from more polluting ones or even ones that represent a threat to the environment?". This calls for a common framework listing the characteristics of sustainability: the one and only EU Taxonomy.
The classification is therefore common to all the EU countries and constitutes a benchmark to assess to what extent a specific job can be considered green. The stakeholders of the EU Taxonomy are the companies, investors and policymakers that are provided with the framework. As the consumers' behavior is changing towards a greener one, investments, which represent tomorrow's world economy, should adapt and act accordingly.
The EU Taxonomy surely calls for another step to be taken. Auditors are signing companies' financial accounts. In the very near future, sustainability auditors could also come into place. That is, auditors will sign and hence certify the company's green book together with its financial ones. Aligned with that prospect are the criteria that have to be met for an economic activity to be labeled "taxonomy-aligned".

Diving deeper into the concept of "taxonomy-alignment".
First and foremost, it should be highlighted that EU Taxonomy sets six environmental objectives: climate change mitigation, climate change adaptation, sustainable use and protection of water and marine resources, transition to a circular economy, pollution prevention and control, and finally protection and restoration of biodiversity and ecosystems.
That being said, let's dive deeper into how an activity can be labeled as taxonomy-aligned. The activity must simply satisfy three features. First, it has to "substantially contribute" (EU Taxonomy Regulation) to at least one of the 6 environmental objectives of the regulation.
In fact, each environmental objective relates more or less to a report in which the factors required for a single economic activity to be considered "substantially contributing to one of the six environment objectives" are mentioned. The list encompasses all the economic activities that a company in a particular industry takes part in, such as a company producing wood or cement. As a matter of fact, the criteria for such companies to fulfill one of the environmental objectives will differ. The taxonomy-alignment is measured based not only on technical screening criteria per economic activity but also on the objectives listed in the respective delegated acts.
Second, the economic activity has to follow the "DNSH principle" (DNSH stands for "Do Not Significant Harm"; EU Taxonomy Regulation). It stands for not doing any harm to any of the other 5 environmental objectives of Regulation – the 6th one being the one to which the economic activity contributes. The same reports as the ones for the "substantial contribution" are published to guide the stakeholders.
Finally, the entire economic activity needs to comply with the minimum safeguards, following the OECD and UN guidelines.

So, where are we at?

The reports on the first two environmental objectives (climate change mitigation and climate change adaptation) were published in December 2021 and are applicable from January 2022. For the last four, the delegated act will be published and enter into force respectively in 2022 and beginning of 2023. Note that a special note on nuclear and gas energy activities has been published in 2022 and will apply as of January 2023.
Moreover, as the EU Commission claims, "The EU Taxonomy is a living document that will be added to over time and be updated as necessary".
Also, it is not a mandatory document, but rather a very strong recommendation to follow.

The EU Taxonomy: a time bomb for international trade?

Obviously, we are going in the right direction, sticking to the shift in the consumers' behavior. Thus, not only companies but also investors will have to further change their activities accordingly. International trade will therefore surely turn more into green economic flows.
While the EU contains the wealthiest demand in the world, big polluting countries such as the US and China, which are more reluctant to adopt green policies, will have to at some point if they do not want to see their exports dive.
Moreover, supplementary regulations are adopted at the EU level according to similar matters that are all related to ESG criteria (e.g.: ban of products made by forced labor from the Single Market).
Clearly, the EU Taxonomy could become the backbone towards a more sustainable economy. When the time bomb bursts, it will surely splash green paint all over international trade.

Why is China holding an ambiguous position in the Ukraine war?

By Daniele Biondi

As both Russia and Ukraine seem far away from ceasing the hostilities, thus exacerbating the already terrible consequences of the war, both from a humanitarian and economic point of view, a major issue remains the role of China in this conflict.

Indeed, the country led by President Xi Jinping has not yet taken any clear official stance on which side to support: although it has often stated that the sovereignty, the integrity and independence of any country should be respected and has indicated dialogue as the right means through which a solution is to be found, China has never referred to the Russian attack as an invasion and still considers Vladimir Putin as a fundamental partner and ally.

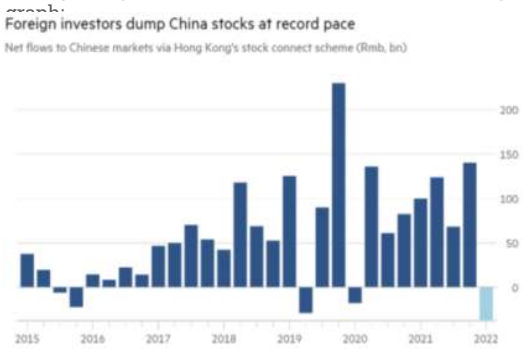
Conversely, the Russian President has recently publicly acknowledged the concerns Beijing has on the war, highlighting a difference between the positions of the two countries for the first time since the beginning of the conflict.
However, the Chinese government keeps avoiding tackling the issue directly in front of the public, whilst stressing its commitment to "work with Russia and fulfill their responsibilities as major countries".
Now someone might ask: why is China behaving in such an ambiguous way?
The answer, as it usually happens in politics, is anything but definite, although it is reasonable to assume that the aforementioned strategy is the most convenient for the Chinese government.
But then the question remains: why is this the case?
On the one hand, the alliance between China and Russia, recently defined as "limitless" by both parties, concerns a wide range of fields, such as national defense, foreign policy, energy and trades. It is undeniable that the most important common denominator between the two countries is the opposition against NATO and, more specifically, the US supremacy, to which both want to become a valid alternative in international relationships.
Furthermore, the situation between Russia and Ukraine is very similar to the one between China and Taiwan, an independent, democratic and economically flourishing island off the coast of the former and on which China has never concealed its expansionist ambitions.

Another extremely solid bound between the two powers is energy. Indeed, China has recently signed a two decade agreement to purchase oil and gas for a total value of $117.5 billion (according to Russian estimates) and a multi-year agreement to buy almost 100 million tons of coal from Russia.
Overall, the aggregate value of the bilateral trades accounted for 146.9 billions of dollars in 2021 (with a 35.9% increase from the previous year) and the two States have set the goal of achieving 250 billions of dollars in trades by 2024.

Finally, many firms, both Chinese and Russian, have tried to dodge Western sanctions by improving the trades with each other. For instance, Gazprom, the Russian biggest majority state-owned multinational energy corporation, has agreed to build the new gas pipeline "Soyuz Vostok" which will transport through Mongolia to China up to 50 billion cubic meters of gas per year.

But not all that glitters is gold and the alliance with Russia comes not only with advantages, but also with many downsides for China.
First of all, helping Russia both from a political and economic perspective might trigger the reaction of Western countries, which might decide to extend the sanctions imposed on Russia also on China. This would result in heavy losses for those Chinese firms, especially in high tech sectors, that rely on foreign equipment and technology for manufacturing, for instance the country's biggest chipmaker SMIC.

Moreover, China holds a great part of its foreign reserves in US Treasury Bonds, which makes the impact of potential sanctions even stronger. For all these reasons, the risk of western sanctions, together with the many strict lockdowns due to the spread of the Omega variant in the country, have induced foreign investors to dump $6 billion worth of Chinese shares in the first three months of 2022, hitting a negative record as shown in the following graph:

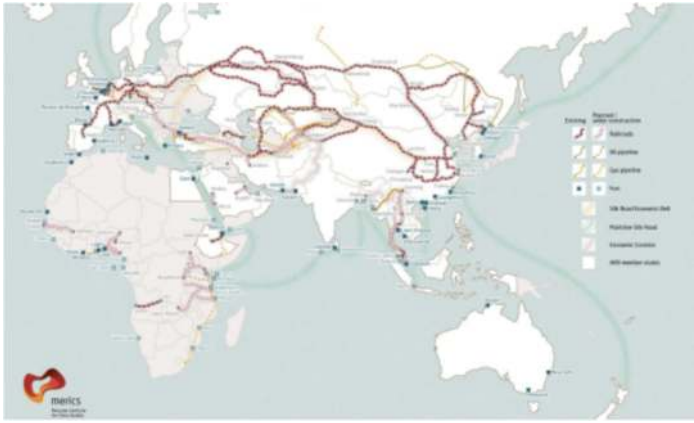


In addition, by so closely aligning its positions with those of Russia in this conflict, Beijing faces the risk of alienating Europe, thus renouncing to its "non-interference" policy and pushing continental countries further into the orbit of the USA, both from a political, as we have recently witnessed with new countries joining NATO, as well as from an economic standpoint, given the increased European dependence on US LNG to replace Russian gas.

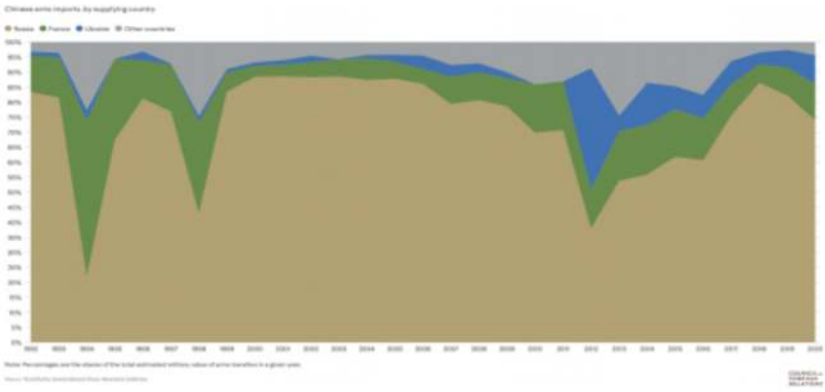
This might not only concern European States, but also the so-called "global south", with some Asian and African countries that have recently changed their mind about the war. For instance, India voted in favor of a virtual intervention of Ukraine's Prime Minister, Volodymyr Zelensky, and told Putin that "today's era is not of war".
The macroeconomic consequences of the war, such as rising food prices and disruption of the energy market, are also heavily damaging the Chinese economy, which already has to deal with internal problems such as the crisis of the real estate market and the dramatic drop in consumption and consumers' confidence. Furthermore, it should be recalled that China has many and robust interests in Ukraine. Indeed, from 2019 China has replaced Russia as the largest trading partner of Kyiv, becoming the top importer of Ukrainian barley and iron ore, whilst Ukraine is China's largest corn supplier and the third as far as weapons are concerned, with a considerably increasing trend in the most recent years, as shown in the graph below.

Last but not least, in 2017 Ukraine joined China's BRI (Belt and Road Initiative), namely a global infrastructure development strategy announced in 2013 and concerning 70 countries (see the graph below) and international organizations, whose aim is to foster international trades in Europe and Central Asia by creating a new Silk Road.
It is considered a centerpiece of Xi Jinping's foreign policy as it would allow China to assume a new and central leadership role worldwide.
Within this project, Ukraine is seen as China's main gateway to Europe and the two countries have so far signed BRI-related contracts worth nearly $3 billions.

To sum up, as the war between Ukraine and Russia seems to be still far away from its conclusion, the border between the two fronts is likely to become more definite, forcing those countries that are still neutral (at least from an official standpoint) to align with one of the two parties.



A question then arises: in the light of its interests in Ukraine and international political ambitions on the one hand and its strong bounds with Russia on the other, will China join the western countries in condemning the invasion, thus isolating its former ally Putin, or will it support its partner even against the threat of US and European sanctions?



Appendix :

BESA
Bocconi Economics Student Association

Credits to

An-Binh Bui,
Francesco De Luca,
Francesco Di Domenico,
Clément Fromageat,
Argyro Charizona,
Mohamed Maiteeg,
Alessandro Marti,
Duru Gülsaran,
Leonardo Bassino,
Philipp Ludwig,
Claire Schumacher,
Daniele Biondi,

And also to Alessio Dal Ri, Tess Coullon.