

OPINION

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The Straits Times says

Inching towards uncertain times

The US Federal Reserve's decision to nudge up the key interest rate by a quarter-percentage point ends an era of unprecedented cheap money that was put in place to tackle the global financial crisis, which was sparked by the bursting of the housing bubble and which spread through the US system to emerge as the worst crisis since the 1930s Depression, and thereafter roiled every Western market. Intimated months ago, the rate hike is a cautious endorsement of the health of the world's largest economy, which has emerged from its stupor to expand steadily, even if not spectacularly. As the recovery progresses, the Fed has signalled that it intends to lift rates by a quarter-percentage point every three months until next December.

President Barack Obama, who assumed office when the crisis was at its most severe, can look back with satisfaction that he is bequeathing a robust enough economy to his successor, unlike the situation he inherited.

The rate increase is appropriate to US circumstances. The employment situation there is healthy, although some would like to see wages improving, and more people who despairingly left the job market, returning. The housing market has gained colour in its cheeks. Indeed, some, like the investment pundit Marc Faber, think the Fed should have acted sooner. That it did not do so was partly because of fear of the impact it would have on global markets. The months of ad-

vance notice it provided were thus necessary. Asian markets have, on the whole, responded positively to the development. Who cannot but cheer the assurances that the market of last resort is in good health! Still, Asia will doubtless endure some capital flight as funds seek a safer haven that has started to offer better yields. This will have an impact on asset prices here.

Also, when funds were cheap, many companies racked up large amounts of dollar debt. American banks, flush with funds and looking for better returns abroad, even encouraged the phenomenon. Now, as the greenback strengthens, those loans will become less easy to repay. Emerging market debt purchased in dollars exceeds US\$3.4 trillion

(US\$4.8 trillion). A good part of it is here. Besides, the Asian economy is not looking healthy. Exports are slumping all round, leading to fear of competitive devaluations. China, even after a series of rate cuts, is expanding at its slowest in a quarter-century. Japan, where the pedal has been pressed to the floor for a long time, is running out of ideas to rev up its economy. India, less affected by the crisis and buoyed by cheap oil imports, is underperforming its potential nevertheless. Central banks in the region need to watch the situation and coordinate closely with finance ministries. They should also have a deep conversation with banks and other financial institutions with large exposure to real estate, commodities trading, and oil and gas.

By Invitation

Thucydides Trap? Prospects better than they look

Are the United States and China headed on an inevitable collision course that will lead to war? Not when shared threats and opportunities can guide leaders to an escape from the "Thucydides Trap", which predicts war between a rising and the incumbent superpower.



Chan Heng Chee

For The Straits Times

What sort of a world are we facing going forward? Will the United States and China go to war?

Globally, there is a sense of great unease as we see and palpably feel the strategic shifts unfolding before us. A recent meeting in Singapore organised by the Asia Society and the S. Rajaratnam Endowment gathered a number of distinguished current and former office-holders, diplomats, strategic intellectuals and business leaders from the Asia-Pacific to discuss the dynamics of "Asia Rising" and its impact in the region and the world.

Professor Graham Allison from the Harvard Kennedy School published a provocative article just before Chinese President Xi Jinping's visit to the US which set Washington abuzz.

In the article titled "The Thucydides Trap: Are the US and China headed for war?", Prof Allison argues that in his study of 16 cases of the rise of a new power in history, 12 ended up in war. "It was the rise of Athens and the fear of Sparta that made war inevitable."

He concludes that in the case of the US and China, while war is not inevitable, it is very likely. He warned: "A risk associated with the Thucydides Trap is that business as usual – not just an unexpected, extraordinary event – can trigger large-scale conflict."

His presentation in Singapore was more nuanced and he argued that wise leadership in the US and China could help avoid the conflict.

In fact, the meeting quickly recognised that the entire global scene needed careful tending. Deputy Prime Minister Tharman

Shanmugaratnam in his keynote address reminded everyone that the world was seeing several fragilities coming together, and this was not a passing phase.

In the economic realm, we see the growing insecurity of the middle class in the US and advanced countries. The world is also affected by China's slowdown and its shift to higher-value manufacturing, which means it produces what it previously imported.

In the political realm, the centre is weakening, with extreme views capturing a larger segment of society than at any time in the post-World War II period. Finally, terrorism will be a continuing global reality. It would take a long time to resolve conflicts within Islam, geopolitical fights in the Middle East and the social legacies of segregated immigrant communities in some advanced economies.

DPM Tharman noted that "geoeconomics unlike geopolitics allows us to look at the world not as a zero-sum game".

Geopolitics for the major powers sees power shifting to one at the expense of the other.

Geoeconomics is not zero-sum because everyone benefits from growth and enhanced interdependence. "It mitigates the inevitable tensions as the geopolitics shifts." But he also noted that there is now a growing disjunct between the central influence on global financial flows, which is the US, and the centre of global economic flows, which is increasingly China. The disjunct was a source of instability, especially for Asia's emerging economies, and it would take a long time to rebalance global finance.

It was China's rise that consumed the discussions. I came away with the distinct impression that while the participants heard war between the US and China was very likely, they thought more in terms of possibility, no one showed imminent anxiety.

Everyone recognised that China was not just another rising power.

Size matters. Size changes everything, even when intentions are good. China is the elephant entering the swimming pool and whether the elephant jumps in or slides into the pool, it displaces the same amount of water. So to ask if China would be disruptive or play along with the established order is perhaps asking the wrong question.

NEW WORLD ORDER

There was no disagreement that there is no settled world order any more. Rather, rising insecurity among nations and within nations describes the state of nations and economic interdependence does not preclude strategic competition.

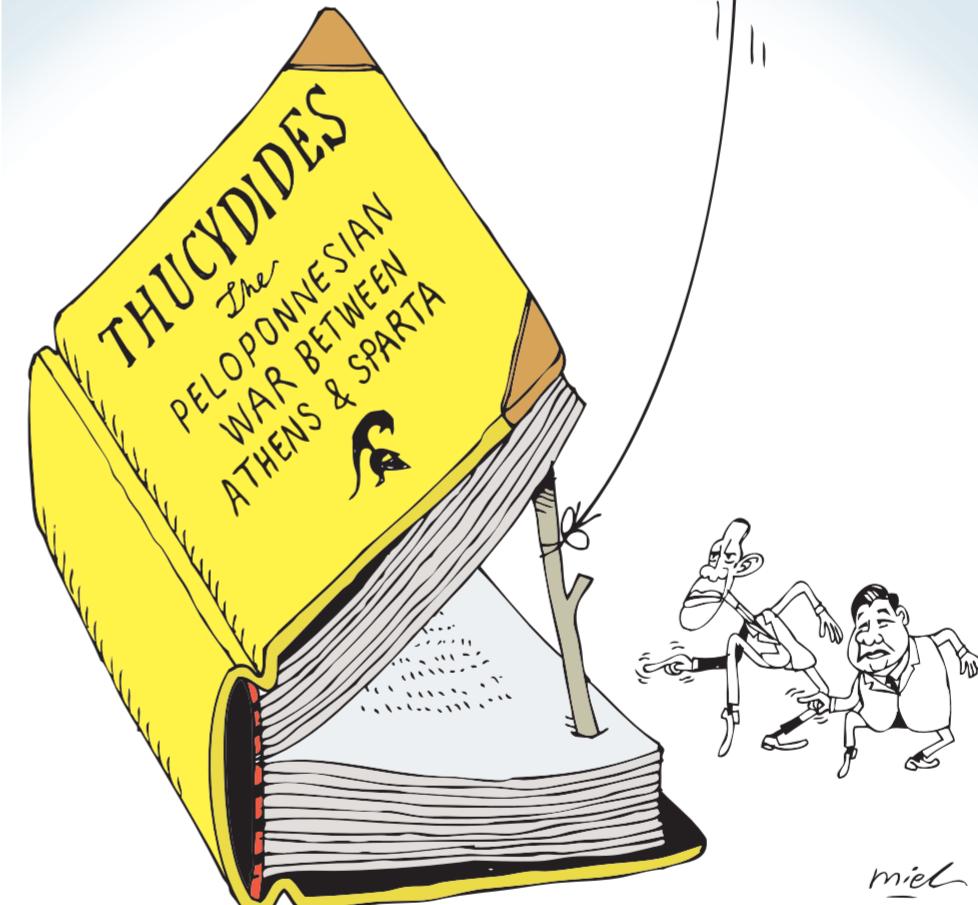
Ascendant nationalism in India, China and Japan will add to the unpredictability of the direction and outcomes of the strategic challenges as these countries work out territorial and boundary disputes.

One speaker claimed he remained optimistic about the strategic shifts because, based on their history, the Asia-Pacific countries are not motivated to re-create the world order. They are about restoring the old order. None of the new powers are missionary and want to convert others to their values. There is absent the "city on the hill" ideal which inspired America to actively promote its values abroad.

But China has just begun to discuss world order internally. China is asking itself what sort of order it wants. Chinese strategic intellectuals never fail to remind others that the world order was designed by the US for the Western world, and that during the Cold War, the Soviet Union was excluded from it. They see the world order today led by the US consisting of primarily three orders – one, the international economic system of which China is a member; second, the creation of a value system against which China is judged to be politically incorrect; and, third, a military alignment left from the Cold War which it has tolerated. We are told China has asked itself what it should do. Should they "open it (the order) up"?

Before one jumps to the conclusion that there lie the seeds of conflict, China has reiterated in many forums that it is not fundamentally challenging the US. I think it means it.

In fact, China has done well by the present order. The breathtaking growth of China as an economic power took place under the American-led world order. But China wants its new



reality and status acknowledged. Finding that new balance is the challenge of the times.

Dr Henry Kissinger, the former US Secretary of State, has described this task as "working for a transition which recognises the arrival of the new power and preserves America's integral role in Asia".

The rivalry seems to be centred on the South China Sea where several states have overlapping claims. So far, neither the US nor China is prepared to step over the line to end in conflict and rules of engagement have been put in place. China needs to work out the disputes with the four ASEAN claimant states. Disputes over sovereignty and territory are a matter between the disputants. Freedom of navigation and overflight in the South China Sea is a concern of all countries. But big power tends to suffer from "big power myopia" and do not grasp how small nations feel.

MUTUAL ASSURED DEVELOPMENT AND DESTRUCTION

So can the US and China escape the Thucydides Trap?

Prof Allison himself offered clues for the escape. He highlighted

"shared threats and shared opportunities" that could bring both powers to work together. The possession of nuclear power and the nightmarish potential of the doctrine of mutual assured destruction, climate concerns, mega terrorism and fear of chaos would head the list of shared threats.

It was no surprise that of the four cases of war accompanying the emergence of rising powers, all occurred at a time when the US, the Soviet Union, Britain, China and France possessed nuclear power.

During the Cold War in the 1950s to 1980s, when the Soviet Union was the rising power, the superpowers never went to war. They fought proxy wars instead. And we have seen the US and China work together on climate change for the Paris agreement.

The fear of chaos in international financial and monetary markets would be another instance when both the US and China would want to put their heads together.

On shared opportunities, Prof Allison spoke of the flip side of shared threats and gains in trade. It is the emphasis on the economy and mutual assured economic

development, and integrated supply chains, that would build interdependence. With the "One Belt, One Road" initiative generating much interest, it was even suggested that understanding the enormous need for infrastructure throughout Asia, US participation in the project should not be discounted further down the road.

Singapore's founding Prime Minister Lee Kuan Yew has written that one of his greatest concerns in the US-China relationship is that the United States and China underestimate each other.

The recent forum provided a platform for all the regional players to discuss the Thucydides Trap fully because, as one participant said, to define the trap is to stop falling into it. Taking everything into account, the prospects are better than they look.

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