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# **U.S. Strategy and Economic Statecraft: Understanding the Tradeoffs**

Christopher S. Chivvis and Ethan B. Kapstein



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## **Contents**

<b>Summary</b>	<b>1</b>
<b>Introduction</b>	<b>3</b>
<b>America First</b>	<b>5</b>
<b>Alliance Economics</b>	<b>7</b>
<b>Globalization 2.0</b>	<b>10</b>
<b>Striking a Balance</b>	<b>11</b>
<b>About the Authors</b>	<b>13</b>
<b>Notes</b>	<b>15</b>
<b>Carnegie Endowment for International Peace</b>	<b>17</b>



## Summary

Few would dispute that U.S. economic policy has enormous consequences for America's national security and role in the world. But economic policy is too often made without a clear picture of the strategic tradeoffs it entails. The purpose of this paper is to help clarify some of these tradeoffs by considering three alternative models of U.S. economic statecraft.

The first model examined here, America First, has several national security and economic disadvantages. It would not only antagonize some of Washington's key military allies but probably also undermine U.S. international competitiveness. It might even induce countries to turn their economic attention toward China, reducing the United States' global influence accordingly.

A better approach would be a blend of two other models, namely alliance economics and globalization 2.0. Together these approaches could help orient the United States for the geopolitical challenges of the next decade. By emphasizing commercial relations with U.S. military allies, such a blend would recall Article 2 of the North Atlantic Treaty, which calls for international economic cooperation among NATO member states. And by leading a reformed multilateral system, the United States would again put itself at the center of the rules-based global economic order that brought prosperity to millions.



## Introduction

Debates about U.S. economic policy often take place without a clear picture of the strategic and national security implications. There can be many reasons for this, including domestic pressures, the inherent complexity of trade and investment negotiations, the technical expertise that the design of economic policy requires, and so on. Yet how the United States uses its economic instruments has important consequences for U.S. national security and global influence. The weight of the U.S. economy in relation to the world economy as a whole, for example, is an often underappreciated element of U.S. global power, and the size and dynamism of the U.S. market generates enormous powers of attraction, especially in Europe and Asia, the world's two most important regions from a geopolitical perspective.<sup>1</sup> Economic policy also affects alliance relationships, and military strategy can have far-reaching economic implications.

This paper seeks to clarify some of the main tradeoffs that the United States faces between security and economics by examining three basic models or ideal types for U.S. foreign economic policy and outlining their key strategic implications.

- **America First:** would aim to unilaterally restore the competitiveness of U.S. industries, in part by delinking the country from the pressures imposed by the global economy
- **Alliance economics:** reconstitutes U.S. commercial relations through a network of partner nations that mainly share its democratic values, security concerns, and international policy commitments
- **Globalization 2.0:** implements reforms to help the free market and the multilateral order adapt to the needs of the twenty-first century

These models are intended as heuristics that reflect broad currents of thought and are meant to represent alternative conceptual frameworks or tendencies, rather than distinct strategic choices. It is very unlikely that the United States would ever adopt one of them whole cloth, nor would doing so be wise. While a pure America First model is the most unrealistic of the three from an economic perspective, it nevertheless can be useful to lay out the broad national security implications that such a model might entail. A more suitable approach for addressing the challenges of the twenty-first century would draw from both the alliance economics and globalization 2.0 models.

Table 1 below provides a notional summary of the top-line pros and cons of each approach, focusing especially on the intersection of economic policy and national security.

**Table 1. The Pros and Cons of Three Approaches to U.S. Economic Statecraft**

	<b>America First</b>	<b>Alliance Economics</b>	<b>Globalization 2.0</b>
<b>Pros</b>	<ul style="list-style-type: none"> <li>• Offers the highest degree of protection for politically sensitive industries critical to U.S. national security</li> <li>• Might help reduce trade-related economic inequalities</li> <li>• Denies China access to U.S. capital and trade, potentially slowing China’s rise</li> </ul>	<ul style="list-style-type: none"> <li>• Permits some economies of scale</li> <li>• Limits China’s economic opportunities and access to sensitive technology</li> <li>• Could strengthen ties with U.S. allies and partners</li> <li>• Might slow China’s rise</li> </ul>	<ul style="list-style-type: none"> <li>• Has the greatest prospects for spurring U.S. growth over the medium term</li> <li>• Could strengthen U.S. influence overseas</li> <li>• Could reduce incentives for great power war</li> </ul>
<b>Cons</b>	<ul style="list-style-type: none"> <li>• Least likely to foster an American economic revival</li> <li>• Disrupts relations with U.S. allies</li> <li>• Undermines the capacity of U.S. firms to maintain global market dominance</li> <li>• Greatly curtails U.S. global economic influence</li> </ul>	<ul style="list-style-type: none"> <li>• Would reduce economic exchange with China, lessening incentives for moderation in other areas of foreign policy (including national security policy)</li> </ul>	<ul style="list-style-type: none"> <li>• Has the most positive outlook for Chinese economic growth and potential for China to gain technology from the United States and its allies</li> <li>• Most likely to strain U.S. domestic politics, complicating foreign policy in other areas</li> </ul>
<b>Other Considerations</b>	<ul style="list-style-type: none"> <li>• Bolsters nationalism at home, and a more insular America might be less democratic</li> </ul>	<ul style="list-style-type: none"> <li>• Would likely result in U.S. allies resisting decoupling, so the model would probably have mixed results</li> </ul>	<ul style="list-style-type: none"> <li>• Appetite among Americans for new trade deals is limited</li> <li>• Requires more concerted economic adjustments and retraining measures than in the past</li> </ul>

# America First

America First economics, as it has emerged over the last few years, is skeptical about traditional international markets and other staples of globalization. It is most often associated with former president Donald Trump, but some aspects resonate across the political spectrum. Broadly, the distinctive features of an America First approach to foreign economic policy include:

- tariffs and nontariff barriers to protect import-sensitive U.S. industries
- buy America provisions to purchase domestically produced goods
- incentives to reshore supply chains to the United States
- reticence about new multilateral trade and investment agreements

Key objectives of an America First policy orientation include protecting jobs and decreasing American dependence on foreign supply chains for national security reasons. Such currents clearly reflect skepticism about globalization, which has intensified in many high-income democracies since the 2007–2008 financial crisis. They are neither unique to the United States nor unprecedented in U.S. history.<sup>2</sup> Nevertheless, the tendency toward America First policies is a departure from the mainstream thinking in U.S. political circles since the end of the Cold War, which involved supporting a liberal global trade and investment regime.

## The Tradeoffs of America First

What are the basic national security and geopolitical implications of this America First model? One conceivable geopolitical benefit is that a loss of access to U.S. markets and capital would hinder China's economic growth and thereby check its geopolitical rise. As discussed below, an abrupt loss of access to the U.S. export and capital markets would probably pose a real threat to China's economic stability, with potentially far-reaching consequences for the Chinese and global economies. If the closing of America's door were gradual, however—and this seems like a more plausible scenario—there is reason to doubt that the consequences would be anywhere near as severe. For example, some Chinese firms would probably find other outlets for many goods and sources of capital including domestically.<sup>3</sup>

The United States might also gain some short-term advantages from a widespread clamp-down on Beijing's access to U.S. technology, and this could impede China's military progress for a while and help U.S. technology firms sustain global dominance and an edge in future innovation.<sup>4</sup> But Chinese military progress will continue regardless of whether or not the United States suddenly denies China access to U.S. technology. There are other sources of advanced technology in the world—like Europe, for instance—and China's

own technological base is already much stronger than it was some years ago.<sup>5</sup> Meanwhile, reducing Beijing's access to U.S. technology would probably encourage the even more rapid evolution of China's domestic technological ecosystem.

Moreover, if the national security and geopolitical benefits of the America First approach are questionable, it also has significant geopolitical downsides. The economic effects alone would further weaken U.S. global power in a relative sense, especially if taken to an extreme. If protectionist measures, currency manipulation, or greatly increased budget deficits eventually led to a global turn away from the U.S. dollar as the main reserve currency, borrowing costs in the United States would greatly increase, restricting consumption and investment. By hampering U.S. domestic economic growth, an America First policy would also be a blow to the foundation on which U.S. national security and global military power are built.

The America First approach also tends to reduce U.S. foreign economic influence, which is a long-standing component of U.S. global power. It is not just the overall size of U.S. economic output that determines U.S. global might. U.S. power also flows from the presence of U.S. firms and capital in so many parts of the world and the promise of access to U.S. markets, both of which are alluring for so many countries. If the United States limits market access to foreign investment—or raises the specter of doing so—it is likely that other countries would respond in a tit-for-tat fashion.

Finally, the more the U.S. and Chinese economies are delinked, the fewer incentives the two countries will have to exhibit restraint in the event of a military crisis. For example, if such economic delinking were to occur and tensions between the United States and China over Taiwan were then to escalate into a military confrontation at some point in the next decade, there would be far fewer reasons for either side to err on the side of caution. One can debate how far this effect goes, and economic exchange alone is, of course, not a sufficient barrier to conflict, but it would be wrong to deny entirely the salutary effects of economic integration, especially in the early stages of a building military confrontation.

Almost none of the America First policy currents—reshoring, protecting specific economic sectors, and promoting industrial policy—as of now go so far as to involve a more severe delinking of the U.S. and Chinese economies. The idea of a more consequential separation is, however, sometimes floated.<sup>6</sup> An extreme version of this model might constrain Chinese economic options in the near term, but the extent to which it would impede China's economic and strategic rise is far from certain over the long term.

If the strategy puts strains on China's financial and banking sector, the effects could be unpredictable and far reaching. But if China survived the initial shock, it would likely recover, developing new outlets for its trade and investment in other regions, including Europe, Asia, Latin America, and Africa, all of which seek access to Chinese capital and markets. U.S.-China competition is already heating up in regions of the developing world where both countries seek to expand their respective influence.<sup>7</sup> This indicates that a

plausible Chinese response to America First could be a more “Global China,” with Beijing playing a more assertive role in world trade, investment, and regulatory policy and making gains accordingly.<sup>8</sup> China’s recent application for membership in the Comprehensive and Progressive Agreement for Trans-Pacific Partnership—the successor to the Trans-Pacific Partnership, the multilateral trade agreement from which Trump withdrew—illustrates the extent to which the United States’ absence from such arrangements offers opportunities to the country’s global competitors to gain market share and shape the economic outlooks of important U.S. allies.

Widespread economic delinking of this kind is nevertheless probably infeasible outside of wartime. It would be extremely costly, for example, for the United States to recreate a domestic supply of electric car batteries, whose demand is increasing in response to efforts to curb carbon emissions.<sup>9</sup> Further, for many goods and even services, the economies of scale associated with research, development, and production are so great as to call for global markets to amortize the upfront costs.<sup>10</sup> Many companies would be loath to give up on markets like China and India with their billions of consumers.

For all these reasons, a pure America First model seems unlikely to materialize in the near future, although it could be forced upon the United States in the event of a war or other global catastrophe. Nevertheless, elements of the America First approach are present in the contemporary policy debate and could have national security and geopolitical effects.

## Alliance Economics

A second model would focus on deepening U.S. foreign economic relations with key allies and partners by restructuring U.S. trade and investment toward countries that share America’s geopolitical preoccupations. This model also heavily emphasizes technology cooperation, especially with Europe. The Biden administration took a step in this direction earlier this year with the launch of the EU-U.S. Trade and Technology Council, which aims to strengthen trade and technology cooperation among like-minded nations that share a common security outlook.<sup>11</sup>

The idea of an alliance-focused economic policy is not entirely new. For example, Article 2 of the North Atlantic Treaty calls for allies to “eliminate conflict in their international economic policies and . . . encourage economic collaboration between any or all of them.”<sup>12</sup> U.S. and European trade and investment ties remain very close. Alliances also offer a framework for large defense undertakings, such as the F-35 Joint Strike Fighter, allowing a consortium of allies and partners to join together to purchase and produce a weapons platform by pooling risks and reducing costs (via longer production runs).<sup>13</sup>

Efforts to develop an economic counterpart to the revival of U.S. alliances might, however, go much further, aiming to reorient a greater proportion of U.S. foreign economic relations toward the allies most likely to share U.S. geopolitical interests and similar ideological outlooks in the coming decades. Indeed, U.S. Treasury Secretary Janet Yellen recently said that U.S. trade policy should emphasize “friend-shoring.”<sup>14</sup> Specifically, the United States could, for example, pursue trade and investment agreements through the imposition of preferential tariffs that are better than existing World Trade Organization (WTO) terms. Washington would not unilaterally impose trade and investment barriers (not to mention secondary sanctions) on other alliance nations. Meanwhile, countries outside this security envelope would receive less favorable treatment in any international economic arrangements, and in some cases such countries (or sectors within those countries) would be prevented from conducting economic transactions with alliance nations. This approach could challenge the order institutionalized by the WTO—but not necessarily. Regional free trade agreements, for example, can be pursued in the WTO context. Thus, a North Atlantic (or NATO) free trade area modeled on the North American Free Trade Agreement may be consistent with WTO disciplines. If such an agreement were reached, some sectors, such as sensitive technology sectors, would be sheltered or removed from exchanges outside alliance networks.

### **The Tradeoffs of Alliance Economics**

What are the geopolitical and national security pros and cons of this approach? If implemented, the alliance economics model would share some of the downsides of the America First approach, although to a lesser degree. For example, the emergence of more unified political-economic blocs might increase the tendency for military conflict between the blocs. Similarly, horizons for future economic growth and hence U.S. power and influence might be slightly constrained as compared with the pro-globalization approach discussed below, although this negative effect would decrease as the economic diversity of the coalition increased. Successfully opening India up to greater trade with the United States and Europe, for example, though difficult, might offer greater opportunities for future economic growth within this model. In other words, alliance economics depends heavily on network effects, whereby the benefits grow as more users join.

There are at least two geopolitical and national security benefits to this approach. First, it would foster a healthy economic foundation for alliance cooperation, while reducing the leverage that China, Russia, and other adversaries wield over U.S. allies and partners. As countries within the grouping further increased their economic interdependence, political ties would strengthen. This is not to imply that there would be no conflicts or friction between members. The more important effect would probably be the negative one of diminishing adversarial influence. China, Russia, Iran, and other rival states have multiple means of influencing the politics and policies of U.S. allies, including covert action, cyber operations, influence operations, and others. But economic leverage—in the form of energy ties and greenfield and brownfield investment, for example—remains an important instrument of power for them, as again revealed during the Russia-Ukraine war.

Second, this approach offers the chance to better protect the United States' technological edge without the downsides of a more nationalist approach. Cooperating with a select group of allies to sustain not just individual industries but a healthy overall technology ecosystem could provide an optimal balance between the risk of technology appropriation and the loss of technological dynamism. By keeping technology-based trade and cooperation aligned within alliance structures, the United States might still achieve the economies of scale to support a lasting dominance of key technology sectors, something that would be much more difficult under an America First model.

This approach could also be expected to lead to other consequences, especially if it were taken to its logical conclusion in the form of economically and geopolitically aligned blocs. The first is that it might force neutral or what used to be called nonaligned states to make choices about which economic camp to join, for fear of being shut out of one network or the other. For any number of emerging economies, including Brazil, India, and Indonesia, an American commitment to alliance economics could pose political and economic dilemmas. Do they wish to be in China's sphere of influence or America's? This question would be of acute importance to those that sought nonalignment to the extent that each bloc would offer tangible economic benefits to insiders.

A larger concern has to do with implementation. Most current and prospective U.S. allies are far from ready to reduce their economic interdependence with China, even if doing so would bring closer ties to the United States. As a result, if Washington attempted to build a global economy around its alliance structures, it might end up with half a loaf: its own economic ties oriented away from China, but not those of its allies. As a result, this approach might not end up doing much to slow China's economic rise, and it might not even do much to protect U.S. technology from falling into Chinese hands, especially given that China's acquisition of allied technology often takes place without the knowledge of the allied governments.<sup>15</sup>

There would also be internal frictions between bloc members in such an arrangement. Recriminations from France over Australia's September 2021 announcement that it would purchase U.S. submarine technology when it had previously committed to do so from Paris—a move the French foreign minister charged was a “stab in the back”—are a reminder of the frictions that can arise even among close military allies.<sup>16</sup> After all, allies are also economic competitors.

Finally, Washington might struggle to make credible commitments to the members of the alliance regarding its policies toward them, given the volatile political environment in which U.S. foreign economic policy is increasingly made.

## Globalization 2.0

The third model, globalization 2.0, would involve trying to reinvigorate America's commitment to market liberalization through global economic institutions. Specifically, the United States would reinvigorate efforts to expand global free trade and the worldwide investment regime and strengthen key institutions such as the WTO with reforms that give all states a fair voice. Washington would drop existing levies such as the Section 232 tariffs on steel and aluminum imports and eschew such measures in the future. The aim would be to strengthen the multilateral rules-based trade and investment system and encourage disciplined choices for trade and investment policy based on such fundamental concepts as reciprocity, national treatment, most-favored nation status, and peaceful and authoritative dispute resolution.

The United States would join the Comprehensive and Progressive Agreement for Trans-Pacific Partnership. New trade agreements and market expansion, in turn, would incentivize American firms to seek to maintain their competitiveness by investing in export-oriented operations and promoting research, development, and even education (given the importance of human capital to these activities). Trade agreements in such sectors as agriculture could provide an important fillip to growth across the developing world.

### The Tradeoffs of Globalization 2.0

One of the most important arguments in favor of the globalization 2.0 model is simply that it offers the greatest horizons for national economic growth—not just for China but also for the United States and its allies. That is particularly the case for the world's smaller economies, for whom foreign trade and investment are essential sources of growth. Of the three models examined here, globalization 2.0 would probably be the most beneficial for both the developing world—because it would offer the greatest opportunities for market access—and the large developed economies whose firms need global markets because of their economies of scale.

Meanwhile, a Chinese economy that is more intertwined with the rest of the global economy would probably be more favorable to diplomacy—over Taiwan, for example. The globalization 2.0 model obviously would not secure peace in Asia by itself, but it could help somewhat dampen regional and international tensions. Further, a renewed U.S. commitment to economic multilateralism might also help to stem the decline of American economic influence in Asia and thereby shore up the foundations of U.S. power in the region. If Washington is serious about competing with China, as both the Trump and Biden administrations have averred, the United States will need to engage with Asia economically to the maximum extent possible.<sup>17</sup>

Such a model would undoubtedly face resistance both domestically and abroad. Domestically, the political appetite in the United States for more trade agreements is clearly

limited—this skepticism about trade agreements, after all, is what drives America First tendencies. Meanwhile, at least some countries overseas may question the credibility of any U.S. commitment to multilateralism and thus hesitate in the face of any new U.S. initiative. Further, at least some of the countries that have benefited from an open international economic system, like China, may now wish to reform it in ways that would be difficult for the United States to accept, such as by giving Beijing significantly more voting weight in international institutions and perhaps a greater leadership role within them. Building momentum for a globalization 2.0 model could thus prove challenging and would require many compromises.

Globalization 2.0 nevertheless offers the prospect of recharging global economic growth and development. Whether this approach would exacerbate or alleviate America's own domestic political strains is uncertain. Sustained economic growth tends to contribute to a reduction in social tensions, but if the growth process exacerbates income inequality and hollows out certain manufacturing centers, which seems likely, it could further fuel populist and nationalist politics.<sup>18</sup>

## Striking a Balance

The most destabilizing of the three models is America First. Not only does this model seem suboptimal for reasons stated above, it is probably the most disruptive of the three for the international economy. The further the United States goes in this direction, the more other countries are likely to respond in kind. While the America First model seemingly responds to social and economic problems in the United States, it is also closely aligned with nationalist currents in America that point toward a more aggressive and less cooperative U.S. role in the world. Although it is sometimes cast as a strong strategic move, an America First agenda would in fact be a defensive move that could exacerbate weaknesses in the U.S. economy, while diminishing U.S. global power over time.

A more favorable approach would be some combination of alliance economics and globalization 2.0. Such a combination makes sense especially in light of future uncertainty and the inherent problems of operationalizing the alliance economics approach, as mentioned above. Alliance economics need not imply a Cold War–style division of the world, only a rebalancing away from excessive economic dependence on China. Taking alliance economics seriously, however, would require going far beyond the immediate initiatives presented at the U.S.–European Union (EU) meeting in Pittsburgh in September 2021, ideas which included the creation of working groups in such areas as technology standards and clean energy.<sup>19</sup>

Moreover, there are serious disagreements between the United States and the EU over basic policy issues, including digital taxation and regulation, an area that could otherwise be ripe for joint efforts.

It should be possible to explore options for building the economic basis for America's alliance network while still taking practical steps to rejuvenate the global multilateral trade regime. One idea, for example, would be to push more aggressively for reforms of the WTO appellate court, enabling it to serve its function of settling trade disputes.<sup>20</sup> And while new large-scale multilateral trade and investment initiatives are probably not realistic for the next few years, it should be possible to pursue a bilateral or regional agenda focused on key allies or prospective partners. This would offer a reasonable balance.

These three ideal-type models of U.S. foreign economic policy are intended to help clarify some of the connections between U.S. economic strategy and national security. Each framework has distinctive costs and benefits—tradeoffs that depend not just on the current dislocations and opportunities they would cause but also their future geopolitical and economic effects over time.

There are many reasons the United States would almost never enact any one of these models in a pure form, and U.S. policy will therefore probably reflect a mix of all three for the foreseeable future. America First, for example, confronts obstacles in terms of domestic costs (widespread protectionism and a broad-based industrial policy would be a colossal expense) and retaliation from even the closest U.S. trading partners. An alliance economics approach, beyond the challenges of redirecting trade patterns, confronts the reality of allies having different policy preferences, most importantly with respect to China. And globalization 2.0 fails to meet the blowback against free trade and investment that has characterized the U.S. political economy in recent years.

Experts and policymakers should nevertheless strive to keep these broader strategic and geopolitical contexts in mind when making foreign economic policy decisions and seeking to most effectively advance the United States' international interests and a coherent grand strategy. Surely, this is easier said than done, but the future of the U.S. role in the world depends on a collective ability to think across these fields and evaluate the economic, political, and international merits of these policy alternatives simultaneously. One of America's greatest assets is the attractiveness of participating in its economy; that strength should be used to good strategic effect.

## About the Authors

**Christopher S. Chivvis** is a senior fellow and director of the American Statecraft Program at the Carnegie Endowment. He has more than two decades of experience as a national security scholar and practitioner, most recently as the U.S. national intelligence officer for Europe. At Carnegie, Chivvis leads policy-focused research aimed at developing realistic U.S. strategy for an era of great power competition and building a foreign policy that serves the needs of the American people.

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