

## Can the liberal international order be saved?<sup>1</sup>

By

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### Abstract:

The Liberal International Order starts at home in the sense that citizens cherish economic openness and political liberties, which epitomize liberalism in a deep sense. Consequently, countries or blocs that apply it at national level will most likely pursue it at international level too. Building on the two-level game theory of Robert Putnam, we explore the domestic and international dimensions of the contemporary liberal order. As public policies need to consider losers at national level, the same logic should be extrapolated at the international level. Much of the erosion of liberal values at home is driven by the failure of policies based on market fundamentalism—increasing socio-economic disparities despite overall economic growth. This created frustration and anger, that led electorates to challenge fundamental democratic values in favor of populist and anti-establishment alternatives. However, despite an uphill battle in the coming years, we argue that Europe is deeply involved in the multilateral framework, as its very existence is built upon this foundation.

**Key words:** liberal democracy, nationalism, inward-looking syndrome, multilateralism, European Union, international order, multi-polar world

### Introduction

Top Trump administration officials assert that the United States want ‘fair trade’—an aim that was usually part of the developing countries’ rhetoric and policy framework. The rescinding of the Trans-Pacific Partnership, of NAFTA and TTIP were concrete steps of a new vision of American foreign economic policy, much more muscular and defined in national terms. Washington promotes bilateral trade agreements and uses tariffs in order to protect industrial sectors. Sanctions have also turned into a common tool of foreign economic policy. US companies have been encouraged to move operations back home and repatriate their profits. State secretary Mike Pompeo underlies countries’ legitimate pursue of national priorities first and foremost. All these statements and deeds represent a radical change of paradigm in international relations compared to the prevailing vision after 1945.

It is tempting to consider this US repositioning regarding multilateralism in international economic relations as either sudden—the product of a realignment of domestic policy, or temporary—an anomaly inherently reversible. Both judgements would, arguably, be wrong. As

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<sup>1</sup> Parts of this article have been published before as: Daniel Daianu, „The New Protectionism”, *Western Commerce Review*, 2017; Daniel Daianu, „What kind of EU economic sovereignty are we talking about”, *ECFR*, November 2018.

an astute pundit notes in a Foreign Affairs issue, “the liberal order has been fraying around the edges for years”<sup>2</sup>.

Threats to the liberal international order come not rarely from within major liberal democracies. Increasing social and economic *strain* in democratic societies percolate externally and, not unfrequently, ask for the use of policy tools to mitigate pain at home. Whether this demarche is successful is another story. But it not unusual and is not of recent vintage. Japan, for instance, provides an archetypical case of a country that used its exchange rate to bolster domestic economic activity for decades now; Tokyo officials used to say that foreign economic policy is foreign policy. And we see nowadays currency wars that are spreading among major economies; monetary policies, too, seem to be a proxy tool for currency wars.

One must highlight in this context the “dark side” of neo-liberalism, of *market fundamentalism*, with its epitome of unrestrained globalization. The latter can explain much of the current deep malaise in the industrialized world. Our paper adds its voice to a growing train of thought that market fundamentalism is inimical to the functioning of democratic societies

We submit that a liberal international order starts at home, in the sense that state-actors base their functioning on democratic values and an array of checks and balances that give voice to and empower citizens, who articulate their preferences politically. But this home order is not sufficient. The Bretton Woods system was an attempt to order things internationally after the second world war, on the values, primarily, of western societies. But, clearly, it was not devoid of flaws in the eyes of emerging economies, that castigated this system for reflecting an unequal balance of economic power and biases in International Financial Institutions (IFI) policies. To the extent globalization reflected the *Washington Consensus* and, often, interests of western powers, emerging countries’ complaints were not groundless.

History shows that hegemonic powers have always played a key role in ordering inter-state relations. *Pax Britanica* was followed by *Pax Americana*, with the latter having a counterpart in the USSR as the hegemon in the former Soviet Bloc, though China has always been an important actor in the global balance of power. Things seemed to get simpler after the fall of the Berlin Wall, but the overwhelming rise of China, economically and technologically, has ushered in a new era in global geopolitics. It is the first time in modern history when the economic supremacy of the western world seems to be undermined inexorably. Where is EU placed in a multi-centric and increasingly hectic world is a key question raised in this paper.

From G20 to G0/G-2 – hegemony plays a role in the control of resources and security. Developing countries, even very large ones, depend economically and geopolitically on larger powers. But unilateral dominance is not possible anymore. The world is turning multipolar, with two dominant superpowers: the US and China, and a EU that is seeking to recompose itself and find a global role. India can also be added to this cluster of influential state actors. And let’s not forget Russia, which is increasingly assertive with its military vectors.

The liberal international order is frequently associated with the transatlantic partnership. However, the reasons for the fraying support for an international liberal order differs across the

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<sup>2</sup> Gideon Rose, introduction to a special issue of Foreign Affairs, “Out of Order: The future of the International System”, January/February, 2017

Atlantic. The US have had a good economic experience with it over decades, when it was the clear dominant power. Yet, a negative reaction to free trade has come into the open based on years of growing inequalities amongst coastal states and the rest of the country, a stagnation of incomes of many American citizens. Likewise, globalization is viewed by not a few as a major driver of domestic economic and social fractures, of growing inequalities. The EU on the other hand, has an overall positive attitude to open trade based on decades of economic convergence amongst its member states through the *Single Market*. Yet, the EU has faced severe economic difficulties in the aftermath of the sovereign debt crisis—largely seen as a byproduct of a faulty designed euro area; and there has been divergence between the northern fringe and the southern fringe of the euro area. That the EU is feeling the pains of unrestrained globalization and of fragmentation inside its member states reveals less benign sides of the *Single Market*—as an integrated economic area.

For many, globalization has become linked to job losses and blatant market abuse (owing to concentration of power), lower standards for safety, health and the environment, tax evasion and avoidance, and an erosion of traditions and identities<sup>3</sup>. With the US retreating so visibly from the multilateral framework, how should the EU position itself? The key question of this article is: should Europe still rely on the transatlantic multilateralism and be a stern upholder of the liberal international order?

We argue that Europe is deeply involved in the multilateral framework, as its very existence is built upon this foundation. The Liberal International Order starts at home in the sense that citizens cherish economic openness and political liberties, which epitomize liberalism in a deep sense. Consequently, countries or blocs that apply it at national level will most likely pursue it at international level too. But, liberalism in international economic relations, that pays due regard to moral and social values, is not synonymous with market fundamentalism; the latter, as we stress in our text, is inimical to liberal values in a deep sense. And, as public policies need to consider losers at national level, the same logic should be extrapolated at the international level.

Much of the erosion of liberal values at home is driven by the failure of policies based on market fundamentalism—increasing socio-economic disparities despite overall economic growth. This created frustration and anger, that led electorates to challenge fundamental democratic values in favor of populist and anti-establishment alternatives.

The preservation of the multilateral consensus will be an uphill battle in the coming years, as the great powers—US or China, are increasingly engaged in a logic of confrontation rather than one of cooperation.

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<sup>3</sup> Daniel S. Hamilton and Teija Tiilikainen, eds., *Domestic Determinants of Foreign Policy in the European Union and the United States* Washington, DC: Center for Transatlantic Relations and Finnish Institute of International Affairs, 2018.

## **1. Demise of Multilateralism in an age of disruptions**

### **1.1 Roots of the Crisis of the Liberal International Order**

The erosion of multilateralism, the rise of protectionism in the developed world can be explained via the lenses of several perspectives such as:

#### **a) A flawed economic paradigm and market limitations**

What can be labeled as „the new protectionism“<sup>4</sup> involves increasingly more state intervention in economy in the first place, but also in society at large. The New Protectionism in developed countries comes, as a reaction to unrestrained, unmanaged globalization. More than a decade ago, Paul Samuelson suggested that the flow of factors of production may erode comparative advantages of industrialized states<sup>5</sup> ; he basically restated what David Ricardo considered to be the reverse side of the coin when capital, investments, or knowledge moves to countries where wages are pretty low. One can nowadays observe that had public policies been more attentive to the needs of those people and place that are on the losing side in global competition, social stress would have been lesser.

“A people's ability to engage with a digital world, that is not rooted in any given place, but that derives its value from global networks and communities of practice, is not just a function of their productive capacities“<sup>6</sup>. As Goodhart<sup>7</sup> says that the convergence of technology and globalisation have divided developed countries between those who see the world from *Somewhere* and those who see it from *Anywhere*. Goodharts Anywheres value autonomy, openness and are comfortable with social change. Whilst Somewheres are, less educated, more rooted in specific places and attached to symbols of tradition and continuity. Prior to Goodhart Rose described the shift away from class as the basis for socio-economic behaviour as follows:

For Settlers, the deep forces draw people to seek out safety, security, identity and belonging. For Prospectors, it is the yearning for success, the search for esteem of others and self esteem , while for Pioneers, the constant drive is for new ideas, the quest for connections waiting to be made, and living a life based on ethics.<sup>8</sup>

Rose (2011) shows how the deep-seated unmet motivational needs of Settlers are leading to growing extremism. As globalisation and technology converge and shift value creation out of productive spaces and places into digital networks, identities based upon connections between people and place are being challenged. For Settlers/Somewheres it is what the Philosopher Scruton<sup>9</sup> calls oikophilia (a deep attachment to place that is a call to cherish and not exploit) that

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<sup>4</sup> Daniel Dăianu, ‘The New Protectionism’, *World Commerce Review*, Spring 2017.

<sup>5</sup> Paul Samuelson, ‘Where Ricardo and Mill rebut and confirm arguments of mainstream economists supporting globalization’, *Journal of Economic Perspectives*, 2004

<sup>6</sup> Taylor A & Bronstone A (2019) *People, Place And Global Order: Foundations of a Networked Political Economy*. London: Routledge, p. 25

<sup>7</sup> Goodhart D. (2017) *The Road To Somewhere*. London: Hurst And Company.

<sup>8</sup> Rose C (2011) *What Makes People Tick: The hidden World of Settlers, Prospectors And Pioneers*. Leicester, UK: Matador, p. 16

<sup>9</sup> Scruton R. (2012), *Green Philosophy: How To Think Seriously About The Planet*. London: Atlantic Books.

is the basis of identity. Yet, as Rose (2011) says, Settlers lack of agency leads to a sense of powerlessness to resist what comes to look like a an abandonment of duties by economic and political elites.

Globalization is not an automatic, mechanical outcome of technological change, as some strongly argue –in the vein of a technological determinism of social and economic relations (by the way, Marx thought similarly when he wrote his Magnum Opus). Reversals can happen following social and economic distress. In addition, concerns vis-à-vis the loss of economic status can combine with worries about increasing technological and military vulnerabilities. This is why the new protectionism signals a return of more state economic intervention.

The backlash against unrestrained globalization goes to the heart of understanding the functioning of markets in society. Markets do not bring optimal results automatically. Market failures require government intervention. This has brought about, over time, the development of public sectors, the setting up of public and private institutions that insure against risks (pension systems, health-care systems, etc.), and mechanisms for the regulation and supervision of financial markets, including antitrust law (against collusion/oligopolistic agreements, rent-seeking).

The very functioning of the democratic state has required public policies meant to ensure basic public goods, among which defence and security, education and health (areas that should not be left in the care of the private sector alone), a judicial system based on the rule of law ('no one is above the law'), etc. History shows that where social cohesion is badly damaged, negative consequences arise and 'social capital' and 'social cement' get diluted, whereby cracks emerge in the democratic process that may give rise to social and political conflict. Yet, the role of the state, though asked to increase on solid grounds in certain fields, it is not uncontroversial for it can be a blunt instrument. Moreover, it is not the market or the state that are currently being rejected by many people. Rather it is the a remote, self-serving elite, based upon a set of progressive and individualistic values that are rooted nowhere specific and lack any sense of duty to *our* place and *our* people<sup>10</sup>. Whenever inequality crosses the frontier of what people/citizens perceive as tolerable, when the sense of 'social justice' and fairness is blatantly disregarded, it is democracy that bears the brunt.

We are currently caught on the horns of the "classic liberal dilemma of determining whether individual freedom or its consequences should take priority, with no obvious answer"<sup>11</sup>. Lacking agency and watching their jobs be outsourced and communities left behind by the construction of Anywheres<sup>12</sup> global village, Goodhart's Someheres and Roses Settlers, in their support for Trump, Brexit and LePen, are demanding more thought for consequence. It is not a rejection of the market itself, but of Market fundamentalism; it is a call for economics to enrich and not just exploit people and place and to nourish oikophilia. Ironically, given how they are mocked by Anywheres, Someheres seek their sense of place to be treated as a home and not just a

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<sup>10</sup> Taylor A & Bronstone A (2019)

<sup>11</sup> Taylor A (1998) *Property Rights And The Differentiating Countryside: A Case Study In South West England*. University of Wales, Cardiff: Unpublished PhD Thesis.

<sup>12</sup> Goodhart D. D. (2017) *The Road To Somewhere*. London: Hurst And Company.

house; for economics to be a means and not only an end in itself and for political economy to be based upon a sense of mutuality<sup>13</sup>.

A reinterpretation of globalisation, of global markets is, therefore, badly needed; one that takes into account the wide diversity of citizens' social and economic circumstances. In other words, a narrowly-understood economic liberalism, i.e. *market fundamentalism*, can pave the way for the erosion of the social foundation of democracy, i.e. the erosion of the middle class. Under such conditions, political extremism and exacerbated populism emerge. Market fundamentalism works against liberalism, against democracy, in its deep meaning.

### **b) Socio-economic strain**

Social fragmentation and anxiety mirror economic insecurity. Across Europe and America, socio-economic divides create the electoral basis for anti-establishment political agenda<sup>14</sup>. As recent events showed (e.g. Brexit referendum, US presidential elections), such popular sentiments can be fostered by new technologies and its questionable uses (e.g. Cambridge Analytica or Facebook 'big data') against a propitious background. This strengthens the case for government intervention, not only via regulatory steps. Initially hailed as drivers of transparency and democracy, we now see that new technologies can equally enhance illiberal methods in societal management, fragment societies, and be disruptive for them in general. There is also another point to make. Political and business leaders would do better to realise that until political economies construct relationships with technology and globalisation that nourish and strengthen communities of place Settlers/Somehweres rejection of the liberal order will only grow.

There is also a disconnect between economic developments and social and political dynamics, which are defined by fury at, and protests against the elites, especially the political establishment.<sup>15</sup> The role of fake news, disputing the 'truth' (scientific and of any other sort) need to be mentioned in this context. Likewise, the rejection of 'experts'<sup>16</sup>, who are blamed for failed public policies (e.g., the *light-touch* regulation paradigm when it comes to financial markets) should not be overlooked.

It is often said that people do not grasp the benefits of globalization. The problem with this assertion is that while benefits may prevail over costs at the aggregate level, at local/community level costs may be massive and social dislocations hard to bear.<sup>17</sup> And where communities are rife with losers, their interests can easily be articulated in a quest for protection.

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<sup>13</sup> Taylor A & Bronstone A (2019) .

<sup>14</sup> Fourquet, J. (2018). *Le nouveau clivage*. Les éditions du Cerf; Fourquet, J. (2019). *L'Archipel français*. Le Seuil. Hopkin, J. (2020). *Anti-System Politics: The Crisis of Market Liberalism in Rich Democracies*. Oxford University Press.

<sup>15</sup> Ruchir Sharma, 'Prosperity is no lock on popularity', *New York Times*, 27 April 2018.

<sup>16</sup> Nichols, T. (2017). *The death of expertise: The campaign against established knowledge and why it matters*. Oxford University Press.

<sup>17</sup> David Autor, *Trade and labor markets: Lessons from China's rise* (MIT, February 2016). See also his "Work of the past, work of the future", VoxEu, 19 March, 2019

Fear of the unknown (of all sorts), of insecurity in general, has to be factored in. People need to feel comfortable in a habitat where they have lived for a long time, and this sentiment cannot be divorced from habits and customs, from a sense of belonging to communities that share identities. But things can turn highly complex (even ugly) when identity, ethnic, religious aspects fuel illiberal impulses and hate. Here, the democratic process may easily go astray.

An increasingly controversial policy issue is immigration. The fact is that however much one is attentive to humanitarian concerns, massive flows of people can tense social and political relations in local communities, in recipient countries. A free flow of labour internationally is much more complicated and politically sensitive than the flow of capital or of goods. Capital comes in and goes out; people do not operate following the same logic. In the case of the Brexit in the UK, it is not immigrants themselves that are being rejected. They are simply the visible face of distant people and authority, which is imposing themselves upon this place and our people.<sup>18</sup> This is why, properly calibrated immigration policies are needed together with development policies in poor countries, or in countries ravaged by military conflicts.

It is no wonder that international institutions, like the World Bank, the International Monetary Fund, the OECD, the EBRD, etc., pay increasing attention to negative effects of globalization, and to a thinning of the social fabric and social fragmentation that can end in full-blown political disarray; there is even talk of the need to redesign the social contract in view of increasing distributional tensions and a spreading sentiment of unfairness in society<sup>19</sup>. Major central banks (the Federal Reserve, the Bank of England, the ECB, etc.) devote increasing attention to income distribution, a research topic one could hardly have imagined them focusing on not so long ago.

Things get more complicated in countries where political leaders justify public policies that entail high social costs by repeating constantly that ‘there is no other way’, or ‘that this is what international markets demand’. This type of argument is likely, in the end, to damage the institutional and political legitimacy of policymakers; and it can fuel social and economic pressure (on the part of local business groups) in favour of protectionism.

### **c) Geopolitical rationales, the rise of Asia**

There is a significant erosion of the US status in the balance of power globally, which is related to economic and military overstretch. It is worth noticing that economic and industrial strength underpins military and technological power;

For the first time in centuries the economic pre-eminence of the Western world seems to be at threat; the rise of Asia, especially of China, but also of India, are to be mentioned in this respect. Economic insecurity and its ‘illiberal’ fallouts can be related to a dramatic shift in the balance of power in the global economy, especially towards new economic powerhouses. Robert Kaplan alludes to this with a metaphor: ‘The Return of the Marco Polo World’.<sup>20</sup> Trade

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<sup>18</sup> Taylor & Bronstone (2019)

<sup>19</sup> Maurizio Bussolo, Maria Davalos, Vito Peregrine, and Ramya Sundaram, “Toward A New Social Contract”, Washington DC, The World Bank Group, 2018

<sup>20</sup> Robert Kaplan, *The Return of the Marco Polo World* (Random House, 2018). See also Kishore Mahbubani, *Has the West Lost It?* (Allen Lane, 2018).

disputes can mushroom in such an environment, not least due to geopolitical and security reasons (just think about the implications of artificial intelligence, or the use of G5 technology).

When people are looking for responses to overall insecurity, a sort of *demonstration effect* in both economic and politic regimes can be at work. There are world political/institutional structures which feature a single ruling party. These are not by definition closed systems. China has opened up its economy for almost four decades by introducing market-based reforms; these reforms have proved remarkably successful in modernising the country, even though the political system has remained that of a single party. Some go so far to argue that there must be something quite singular about the Chinese model –what former Polish finance minister Grzegorz Kolodko calls “Chinism”<sup>21</sup>, which seems quite odd as a view. There is also a sort of a fascination with the ‘economic model’ of Singapore, although this is a very small (city) state. And hands-on economic policies practised in not a few emerging Asian economies have explanatory power too, for it is hard to refute them analytically in view of their achievements. In addition, in times of economic and security strain, of major disruptions, or when facing major ecological challenges, the appeal of a less deliberative decision-making setups may be quite luring.

But it is one thing to use authoritarian, less deliberative processes within a democratic (liberal) framework, and another to alter the democratic nature of a system (society), to give up its liberal core; there is a red line to cross here, albeit one could argue about its outline and fine print. Even in China, inroads of political pluralism should not be ruled out over the long run, although authoritarian characteristics will probably remain there for a persistent time in view of the complexity of its society; pluralism will be more likely once citizens vie and get more *voice* (to use Alfred Hirschman’s concept<sup>22</sup>) in the running of their country.

To be fair with the latter remark, “voice” and legitimacy/accountability are getting at the forefront of public debates in western (advanced) societies as well. Why is it so? For many people feel that they have no longer a say in the running of their societies, or that they have been forgotten, that “elites” do not pay attention to their interests. In this regard, the rejection of mainstream parties can be interpreted through several lenses: the impact of the Great Recession and myopic public policies that have deepened social cleavages; a kind of institutional sclerosis (in the spirit of Douglas North and Mancur Olson Jr.’s writings<sup>23</sup>), which can occur in advanced capitalism as well <sup>24</sup>; a new industrial revolution, aging, and a shift of power toward Asia –all of which seem to confound elites and governments in western societies alike. It is quite surprising that in both the US and the UK –what one would consider to be the mainstays of democratic order in the world, a rejection of the international liberal order (in the UK by the vote for Brexit) is so strong.

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<sup>21</sup> Grzegorz Kolodko, “Capitalism, Socialism or Chinism?”, *EconoMonitor*, 18 January, 2018

<sup>22</sup> Alfred Hirschman, “Exit, Voice and Loyalty”, Cambridge (Mass), Harvard University Press, 1972

<sup>23</sup> Douglas North, “Structure and Change in Economic History”, New York, Norton, 1981. Mancur Olson Jr., “The Rise and Decline of Nations. Economic Growth, Stagflation and Social Rigidities”, New Haven, Yale University Press, 1982

<sup>24</sup> See for instance Steven Levitsky and Daniel Ziblatt, “How Democracies Die”, New York, Viking, 2018



#### d) Security, peace and protection of citizens

The role of the state as a guardian of public interests comes ever higher on the public agenda in the western world. The US was badly hit in September 2001 by terrorist attacks, which led to a review of concepts regarding ways to ensure citizens' and state security. Europeans have also been hit by terrorist attacks in recent years, which has triggered anxiety and claims to public authorities similar with the ones across the Atlantic.

Terrorism, unconventional threats (e.g. cyber-attacks, hybrid wars, etc.), fear for the future, big uncertainties, are pushing many citizens to ask for firm measures from their national governments to protect them and protect national interests. In France and Belgium state of emergency measures operate. New security measures are proliferating. The refugee/migrants' crisis in Europe has posed major difficulties for the Schengen space to function. And in the US the new Administration has a new approach, be it highly controversial, regarding immigration.

How open societies can answer to such challenges is an open question; without balanced policies, outcomes can be largely suboptimal.

Authoritarian temptations come up in liberal democracies during hard times – these propensities are similar to what happens to state conduct in times of heightened tensions, of war (*the war economy syndrome*). For there is a big difference between the fear for tomorrow as regards one's job and the one that is linked with terrorist threats and military conflicts. But isolation, exacerbated protectionism may act as a boomerang and worsen things – as opposed to the aimed ends.

One can imagine a trade-off between openness (i.e. economic freedom) and inward-looking drives as a quest for protection/security<sup>25</sup>. Protection/security and openness (i.e. economic freedom) are public goods. This may be illustrated as a social utility function which includes protection/security and economic freedom as an expression of economic openness, as public goods (see Appendix). A value/preference function would indicate levels of citizens' comfort in terms of these public goods. The substitution between protection/security measures and economic openness (i.e. economic freedom) has limits because these two public goods (as a state of the social and economic system) are not completely independent of each other; from a certain level, protection measures, or restrictions may distort open society (democracy) exceedingly. Likewise, a total openness of the economy/society, with no rules and protection measures, may cause enormous costs, social anomia. When times worsen a more inward-looking society emerges (see the appendix for more on this trade-off).<sup>26</sup>

#### 1.2 A European Union pulled apart by integration and fragmentation

EU is a complex institutional construction that is currently pulled by both tendencies of integration and fragmentation. The Union's economic gains hid for quite a while the incompleteness of its design (e.g. lack of a significant budget, as stipulated by the 1977 MacDougall Report). It is also threatened by persistent internal divisions (between West and East, but also North and South since the financial crisis) that get further amplified by the Russia

<sup>25</sup> See Daniel Daianu (2017)

<sup>26</sup> Daianu, D. (2019). Can Democracies Tackle Illiberal and Inward-Looking Drives. *Romanian J. Eur. Aff.*, 19, 5.

spectre in internal political competitions. Finally, in order for the EU to stand united as a global actor, a European form of sovereignty is needed.

European institutions do indeed suffer from a ‘democratic deficit’<sup>27</sup>. They are also affected by an inherent trade-off between the legitimacy of the policy output (i.e. swift decision-making and policy delivery) and the legitimacy of process (i.e. proper delegation of interests based on electoral mechanisms and principle-agent theory). Given the multitude of challenges the European continent faced since the dawn of the EU project, the majority of its accomplishments can be legitimised through the results and not the due process.

The financial crisis that erupted in 2008 underscored the shortcomings of its decision-making procedures. Financial assistance programmes for beleaguered eurozone countries (grappling with liquidity and solvency crises) have been implemented via *sui generis* methods and mechanisms. The latter have fuelled popular discontent and increased the amount of distrust in the functioning of national and European institutions. Austerity measures proved inadequate to solve deeper systemic troubles in Southern member states<sup>28</sup>. The EU commissioner for economic affairs, Pierre Moscovici, and other high-ranking European officials (e.g. Germany’s former finance minister Wolfgang Schäuble) were quite candid in noting that the decision-making framework in the euro area needs to be reformed as part of the push to streamline public institutions and policies, in order to give them more legitimacy.

There is also a fundamental contradiction in European integration, which is epitomized by Dani Rodrik’s trilemma: integration (globalisation via the ‘single market’) can hardly cohabit with autonomous economic policy and with democratic accountability<sup>29</sup> at the national level,<sup>30</sup> something must give in in this triumvirate. This trilemma may simplify reality, and trade-offs and compromises may be worked out. However, it poses a formidable challenge to the eurozone unless integration is backed by policies and mechanisms that can iron out excessive heterogeneity and competitiveness gaps between member states. The differences between European regions in terms of competitiveness remain very large, with the top ten performing regions coming from Germany, Netherlands and Sweden, while the bottom ten belonging to Romania, Bulgaria and Greece<sup>31</sup>.

In light of the need to reform eurozone institutions and policies a key question arises: can financial integration overcome economic fragmentation without fiscal arrangements, i.e. risk-sharing schemes? Fiscal integration implies more than institutional cooperation: it requires

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<sup>27</sup> Moravcsik, A. (2002). Reassessing legitimacy in the European Union. *JCMS: journal of common market studies*, 40(4), 603-624. Majone, G. (1998). Europe’s ‘democratic deficit’: The question of standards. *European law journal*, 4(1), 5-28. Follesdal, A., & Hix, S. (2006). Why there is a democratic deficit in the EU: A response to Majone and Moravcsik. *JCMS: Journal of Common Market Studies*, 44(3), 533-562.

<sup>28</sup> Blyth, M. (2013). *Austerity: The history of a dangerous idea*. Oxford University Press.

<sup>29</sup> The status of being accountable to the voters who gave a mandate to top public servants.

<sup>30</sup> Dani Rodrik, ‘The Inescapable trilemma of the global economy’, 27 June 2007 (personal blog). See also his essay ‘The Double Threat to Liberal Democracy’, *Project Syndicate*, 18 February 2018.

<sup>31</sup> Regional Competitiveness Index 2016.

institutional integration and a eurozone budget. This creates political problems, as wealthier/creditor countries fear a 'transfer union' (fiscal transfers), however much sense the latter makes in a monetary union. Beyond narrowly-defined economic interests,<sup>32</sup> there are indeed constitutional impediments to creating fiscal transfers. For the eurozone to be viable, both public and private risk-sharing schemes are needed. Here lies the greatest difficulty in reforming the eurozone.

Furthermore, within the European Union, the situation is even more complex on account of historical geopolitical threats. The liberal international order can be linked to the security of Central and Eastern European states vis a vis Russian influence. However, as the United States are increasingly falling back on their engagement in the multilateral framework, it is unclear how sentiments will evolve in the Central and Eastern Europe (CEE) region. For now, however, the US seem determined to stay engaged firmly in the Region, while Poland and Romania appear as lynchpins of this policy approach.

Internal political battles mirror the overall strategic dilemma of the European Union. The most powerful political actors in Western member states are either progressives or nationalists, which is very similar to the American political offer<sup>33</sup>. This division may be too crude analytically since being progressive (liberal) does not preclude inward-looking drives when conditions change dramatically. In contrast, in most of the CEE political actors stand divided by their European attachment: pro-Europeanists whose platform generally supports the liberal international order, and nationalists whose platforms gear not only towards religious conservatism, but also are quite cautious about liberal values. Some leaders talk openly about the virtues of "illiberal democracies". Russia tries relentlessly to use this state of affairs to its advantage according to the dictum *divide et impera*. While it may well be the same in the case of many nationalist parties in Western Europe (e.g. Rassemblement National, Lega Nord), it is within CEE that this situation brings back much of the Cold War anguish of being stuck on the wrong side of Europe. The events in Ukraine are a clear warning of what dangers are in front of Eastern member states, in both CEE and the Baltic regions.

By all accounts the agenda of the current radical nationalism in European member states is not aiming for building their societies (i.e. education, development), it is about conflict and confrontation: us vs. them<sup>34</sup>. A false sense of protection is derived from isolationist policy. Rising tides of extremists in Europe spell trouble in the years ahead, as the peace so ardently achieved by the EU can unravel before our very own eyes. Peace and security were built upon the premise of economic interdependences, if one takes away such interdependences, one takes away the very foundations of the European project.

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<sup>32</sup> The euro functioned as an undervalued Deutschmark and guilder, fuelling exports; the euro operated also as an overvalued lira, escudo and peseta. This fostered the emergence of large imbalances between north and south in the eurozone.

<sup>33</sup> Balfour Rosa (2018) Polarization in Europe: Public Opinion and EU Foreign Policy, in Daniel S. Hamilton and Teija Tiilikainen, eds., *Domestic Determinants of Foreign Policy in the European Union and the United States*, Washington, DC: Center for Transatlantic Relations and Finnish Institute of International Affairs (FIIA).

<sup>34</sup> Bremmer, I. (2018). *Us vs. them: The failure of globalism*. Penguin.

The European Parliament's political groups mirror eloquently the growing divergences in the European Union with regards to multilateral engagement and different visions regarding the future of the Union. Dividing lines are not only between political families, but also between the delegations of the member states. For example, on the commitment to transatlantic partnership, Eastern European member states are most supportive, while Western counterparts are quite ambivalent<sup>35</sup>. Eastern Europe is very much committed to the transatlantic partnership mainly for security reasons, as it regards NATO, much more than the EU, as a guarantee against Russia. In contrast, regarding the support for environmentally progressive policies, the situation is reversed<sup>36</sup>. The latter is increasingly important, as the Paris Agreement has been often used as an example of Europe's commitment to multilateralism at a global stage. And in view of the natural disasters caused by climate change worldwide, this policy issue will put its imprint on EU politics ever more. CEE are opposing the environmental progressive policies because they are ill equipped economically to pursue the transition to greener sources of energy in the intended timeframe. Therefore, it may be that the EU budget and other EU policies need to play a stronger role in order to bring the advanced and the emerging economies of the EU to a common denominator in this respect.

EU sovereignty is needed to counter isolationist tendencies and be a powerful global actor.

One of the most prominent issues in the EU today is the management of sovereignty, both conceptually and practically. Ever since its inception, the EU strived for a shared sovereignty. Current challenges (e.g. immigration, protection of borders, terrorism, cyber-attacks, climate change) have pushed the EU towards an inward-looking drives. 'European sovereignty' also leads to the idea that the EU needs more room of manoeuvre in world affairs, not least in economic terms. The EU is in fact committing to actively promoting European interests and values on the global stage in the coming years<sup>37</sup>.

As the world stage becomes less multilateral, and more multipolar, it becomes more stringent for the EU to stand as a consolidated single bloc. In international trade, the EU stands firmly amongst the top three powers, surpassing USA in exports, and China in imports. Taken individually, amongst the member states only Germany could have a significant clout on the international market—as it represents approximately two thirds of European trade, but it would not be a strong enough contender to USA and China.

Decades ago Richard Cooper wrote a book on what underpins the transatlantic economic and political community<sup>38</sup>. The Cold War was a period that reinforced the links between Europe and the US, in economic and military affairs. In spite of inevitable economic rivalries, ever deeper economic ties were a strong lynchpin for containing the Soviet Bloc and for expanding western democracies' interests worldwide.

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<sup>35</sup> Based on Votewatch predictions of voting behaviour in the current legislative.

<sup>36</sup> Idem fn. 35.

<sup>37</sup> European Commission (2019) A New Strategic Agenda 2019-2024

<sup>38</sup> Cooper, R. N. (1968). Economics of Interdependence: Economic policy in the Atlantic Community. McGraw-Hill

But the world today seems to have turned upside down. Whereas emerging economies have been traditional advocates of fair trade, currently some advanced economies, with the US in the lead, argue that global trade is not a level playing field, that unfair practices favor emerging powers – China in the main. The escalating conflict between China and the US, coupled with the latter's increasingly bilateral dealing, leaves Europe to find its own stance.

In the context of the demise of multilateralism, EU is heavily disadvantaged in this regard, for several reasons. Unlike the US, it is not a federal state, and its decision-making mechanisms are much more cumbersome. The euro is not a commensurate rival for the USD in critical respects, and this is illustrated by the share of the American currency in world reserves and in world payments. As long as the euro area will continue to have an incomplete design and inadequate policy arrangements, is it hard to think that the euro can be as robust as the USD. The euro area does not benefit on an own, joint safe asset, which is a prerequisite for a liquid markets and, ultimately, for financial stability. For the latter, a common "fiscal capacity" being also a must. Finally, EU might well be the largest trading bloc in the world, but it is also fraught with currents of fragmentation and a growing divide between the North and South in the euro area, between West and East; as mentioned before, member states have different opinions on such issues such as immigration, the 'rule of law', international trade, or how close the ties with the US should be.

Acquiring more 'policy space' is a commendable aim for EU policy-makers, but this has to be defined in realistic terms. Arguably, more policy space should not cause more confrontation areas with the US. Europe is too fragmented and weak internally to afford itself to fuel tense relations with Washington. Provided the EU gets more cohesive, more united its quest for more economic and geopolitical relevance gets bolstered.

When it comes to defense, Europe (and this is felt in the eastern EU members states in particular) needs the US. Having said this, the EU clearly needs more capacity to cope with military threats; and here cooperation with post-Brexit UK is pretty essential. In addition, the UK can be a bridge between Europeans and Washington in order to control too much damage. It is also fair to stress that Washington's confrontational acts and rhetoric should change in order to have a good and functional EU-US relationship.

## **2. What is looming ahead?**

While the current posturing of some developed states suggests that they are seeking to regain former power status, it is also worth looking into future trends. At global level, the realpolitik competition between great powers will intensify and will likely replace multilateral collaboration. At European level, divisions in the EU, both across and within member states, menace to continue to erode the EU project.

The global economy seems set on a multipolar path. The multilateral consensus will, arguably, no longer be the norm. What seems to be going on now in the United States is to be judged in conjunction with rivalries that are growing in an ever more uncertain world. As in the Cold War decades, the control of the transfer of sensitive technologies may gain relevance and will be adapted to the new context. Trade blocs may proliferate simultaneously with an erosion of multilateralism. As a matter of fact, the EU is a de jure and de facto commercial bloc, be it of a benign sort and attached to multilateralism in world economic affairs.

Unrestrained globalization has brought benefits, but it has also damaged social cohesion by neglecting distributional effects. The socio-economic disparities left much of electorates feeling unrepresented by mainstream parties, which gave political advantage to anti-globalist, isolationist actors<sup>39</sup>. Not least, the cultural backlash of Settlers/Somewheres (the losers from the convergence of technology and globalization against cosmopolitan international integration was an equally powerful force in support of the rising tide of populist and nationalist political actors<sup>40</sup>.

The world features a revival of national interests (nationalism, economic nationalism etc.) as Settlers<sup>41</sup> reject neoliberal constructions of the global village that are not rooted somewhere and are imbued with market fundamentalism<sup>42</sup>. A world faced with large disruptions (i.e. disorder), and with the redistribution of economic power (i.e. multipolar equilibrium) is what Ian Bremmer calls 'G-0'<sup>43</sup>. However, China is increasingly viewed as exploiting its access to the international economy to pursue "national security advantage and accelerate its growth as an economic and military superpower"<sup>44</sup>.

The post WWII institutional economic arrangements (i.e. Bretton Woods's arrangements) are under siege due to alternative accords and institutions promoted mainly by China. This gives rise to an additional level of uncertainty in the world order, as it is not only a question of separation between large powers (i.e. multipolar), but also of confrontation. Some even raise the question of an inescapable confrontation between the US and China, given the size of their economic and military power<sup>45</sup>, with conventional and unconventional threats that proliferate. Some experts refer to this confrontation as G-2, in which both US and China redraw completely from any role or responsibility at the global level<sup>46</sup>. A world without a liberal hegemon is most likely a dark challenge for developing countries depending of resource distribution from the west.

The role of public policies will be greater than ever in mediating social peace. If those who lose in the global economy and inside their societies are not given the chance to socio-economic inclusion, as exclusion gets deeper and more generalized, tensions will rise and conflicts will

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<sup>39</sup> Hopkin, J., & Blyth, M. (2019). The global economics of European populism: growth regimes and party system change in Europe (The Government and Opposition/Leonard Schapiro Lecture 2017). *Government and Opposition*, 54(2), 193-225. Hopkin, J. (2020). *Anti-System Politics: The Crisis of Market Liberalism in Rich Democracies*. Oxford University Press.

<sup>40</sup> Norris, P., & Inglehart, R. (2019). *Cultural backlash: Trump, Brexit, and authoritarian populism*. Cambridge University Press.

<sup>41</sup> Rose C (Op.cit., 2011).

<sup>42</sup> Goodhart D. (Op. cit.2017).

<sup>43</sup> Bremmer, I. (2012). *Every nation for itself: Winners and losers in a G-zero world*. Oxford University Press.

<sup>44</sup> Chalmers, M. (2019). *Which Rules? Why There is No Longer a Single 'Rules-Based International System*. RUSI Occasional paper.

<sup>45</sup> Allison, G. (2017). *Destined for war: can America and China escape Thucydides's trap?*. Houghton Mifflin Harcourt.

<sup>46</sup> Arvind Subramanian, Josh Felman (2019) The G-Minus-2 Threat, Project Syndicate, Jul 26, 2019; Bergsten, C. F. (2018). China and the United States: Trade Conflict and Systemic Competition. *Peterson Institute for International Economics (PIIE)*.

intensify. Inter-ethnic and religious conflicts add to the social and political picture of the coming years.

Security rationale and geopolitical rivalries will make optimization at global scale (e.g. global supply chains) less relevant; supply chains will tend to become more “regional”. The EU as a “bloc” may reveal this quite glaringly. Competition will thus turn a purported win-win paradigm of multilateralism into a win-lose game of the great powers. This is likely to occur especially when economic growth is quite feeble and income distribution becomes an acute social and political issue. Likewise, the New Industrial Revolution will make economic shocks harder to manage. In this context, protectionist propensities are likely to increase.

What would be the result of a „New Protectionism” as an economic defence response? It may probably open the door to a prolonged interregnum, with a corrosion of international, global institutional arrangements. ‘Realpolitik’ will make a comeback as a way to articulate foreign policies. This will be done at the expense of placing moral values and the interests of what is called the international community at center stage. Such an evolution is likely to lead to a precarious power balance, an unstable equilibrium in international relations.

There may also be **an optimal degree of economic openness** that varies according to circumstances. The New Protectionism may be tied to tides of economic openness in the inter-state system, with alternating upswings and downswings along secular cycles.

The EU will continue to be strained by centrifugal forces. However, it is likely that the reaction after Brexit will be to pursue deeper integration, amid growing dangers in the global arena. For the EU, solidarity and deeper integration make up essentially the only sensible solution in the new global context. But nationalism is back in Europe too. What would one have to see in relations with the need for deeper integration?

The resurrection of national interests in Europe (as in America) is not only linked to the economic circumstances of the member states. Whilst the UK and France gravitate back to national interests in a context of relative industrial decline and Germany remains a strong supporter of economic globalization given its overperforming industrial structure. The latter benefitted greatly from the eurozone that helped it boost its exports and keep its jobless rate low; its current account surplus, nearly 8.5 percent of the GDP currently, is by far the largest in the world. But what would happen were this economic situation to change significantly with ensuing high unemployment? The current economic slowdown in Europe, in Germany (which sees the limits and risks of being over-dependent on external markets could be ominous in this regard. Fortunately, Germany is still a stronghold of the liberal order while being the economic mainstay of the EU. In several emerging economies from Central and Eastern Europe (CEE), national prerogatives are getting stronger despite their EU membership.

Forms of illiberalism in Europe can also be related to waves of immigrants during the past two decades; in some developed EU member states there is growing discontent over the free movement of labour from CEE, even though that human capital inflow was positive for host countries. But it is fair to acknowledge that macro data may be at odds with some granular, micro data.

Illiberal propensities should be judged not only in commercial terms. A bunch of crises (i.e. social, geopolitical, identity-driven) demand a state to intervene more in the economy.

Consequently, the crisis of European and global integration should be examined from an ampler perspective, one that goes beyond economic issues.

Central and East European countries would suffer a double blow: via global arrangements that are cracking because of protectionist measures; via what may happen in the EU. Globally, the effects on trade and investment flows, technology transfers are to be taken into account. Within the Union, the Single Market functioning, changes in the EU framework, the fate of the EU budget, are to be examined.

Emerging EU economies would suffer following a deteriorating context in Europe and across the world. A steady dilution (not to mention a dismantling of the EU) would be dramatic for Europeans if we consider what the Union meant for economic recovery and peace after 1945. Terrorism, other unconventional threats, increase citizens' needs for protection; safety is more valuable in peoples' preferences and this could lead to restraints on economic openness. It remains to be seen how such a possible evolution will impact open societies. The deterioration of trade relations on a large scale is likely to fuel animosities and mistrust and may cause conflict.

To conclude, at global level, a transition towards a new international regime, a new order seems to be under way; it is vital that big conflicts and large damages be avoided. At European level, the EU is a public good in itself, and it has to be saved despite tendencies that undermine it. As Javier Solana put it, the EU may be the world's best line of defence against what threatens the multilateral, liberal order. It is nevertheless true that the EU itself needs reforms; it has to be reinvented in order to survive.

The liberal order, as it was set following the WWII, is questioned severely. It should be emphasized however, that a liberal order is not synonymous with market fundamentalism.

The world that we seem to be bumping into shows signs of fragmentation, with societies more polarized. Not a few developed states feel threatened and seek self-protection via various measures; protectionist measures are part of a return of the state in the economy. Beyond the competition of great powers, there is also a competition between the developed world and the one that is arising, and this contest will need its own set of rules. And rules imply a (new) world order.

### **3. What Can Be Done to Save the Liberal International Order?**

Liberalism at its core identifies itself with democracy, the rule of law, fairness, and respect for fundamental human rights. Yet, when globalism, as a vision and paradigm, leads to unrestrained liberalization by disregarding market failures and losing sight of those who lose in economic competition as notions of stewardship of people and place are cast aside<sup>47</sup>, and when the disruptive impact of new technologies is underestimated, democracy is jeopardised and "radicalism"<sup>48</sup> of all sorts gains ground. This happens because the social fabric is worn thin, the middle class (its social basis) withers, confidence in the ruling elites fades away, and, ultimately,

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<sup>47</sup> Goodhart D. (2017)

<sup>48</sup> Wolfgang Munchau, too, roots the rise of radical ideas in the failure of neo-liberalism, of unmanaged globalization ("The Future belongs to the left, not the right", Financial Times, 25 February, 2019)



a crisis of democratic governance is brought about. Simultaneously, authoritarian propensities and endeavours crop up.<sup>49</sup>

**Markets have to be judged, therefore, in their social and cultural context, while society is to be understood as more than a competition among individuals and company level profit-maximizers.** Highlighting the social responsibility that many companies talk about is not sufficient in this regard. Rediscovering Karl Polany's outlook on the "markets know best paradigm"<sup>50</sup> and Max Weber's emphasis on ethical conduct (which can be linked with Adam Smith's *Theory of Moral Sentiments*) makes sense in trying to figure out a way out of a seemingly historical conundrum. A recent statement of leading CEOs regarding the social responsibility of their companies, the responsibility vis-à-vis stakeholders (as against shareholders' and the deficiencies of short-termism in profit maximization) may be a welcome wake up call. But let us see what genuine actions stand behind it and not a simple and hypocritical PR demarche<sup>51</sup>.

Neither do markets care about ecological threats. Nicholas Stern, years ago and, at the time, being the chief economist of the World Bank, pointed out that the inability of our models and policies to pay due regard to climate change and ecological menaces is, quite likely, the greatest market failure in human history<sup>52</sup>; this, simply put, is a strong criticism of practiced public policies and of underlying cognitive approaches. What happens currently with ecological disasters and major disruptions make up an existential threat; it is mind-boggling to see politicians and top policy-makers who question the ecological threats and refuse to alter bad public policies. What happens in Brazil, the massive deforestation of the Amazonian forest, is a stark reminder as to what poorly devised public policies can bring about. President Emmanuel Macron is right to say that what happens with the Amazonian forests (which is not of recent vintage), is a global threat to mankind.

It is refreshing to see that major central banks ask for action in factoring in climate change in our banking models, but much more needs to be done in this regard. Public policies in their entirety need to change in order to deal with the existential threat of climate change. It is also good that in the European Parliament green parties have gained more political traction. In Central and eastern Europe, as EU member states, ecological concerns need to be widely disseminated and political parties have to consider them very seriously. It is expected to see the next EU Commission paying more attention to climate change and required public policies in this regard. The EU should be a steady promoter of climate change policies worldwide. The Paris Climate Accord should be followed by firm actions.

Real change that is both ecologically and socially sustainable, as well economically viable, will come from policies which encourage and enable global digital networks to enrich and cherish

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<sup>49</sup> See also 'The End of the Democratic Century' by Yascha Mounk and Roberto Stefan Foa, *Foreign Affairs*, May-June 2018. This issue contains a set of texts listed under the generics 'Is Democracy Dying?'

<sup>50</sup> In his "The Great Transformation" (New York, Farrar and Reinhart, 1944) Karl Polanyi highlights the need for society to protect itself against unrestrained markets.

<sup>51</sup> See also Jeffrey Sachs, *The Crisis of Anglo-American Democracy*, Project Syndicate, Jul 25, 2019.

<sup>52</sup> Nicholas Stern quoted by *The Guardian*, 29 November, 2007

connections between people and place. This will need to transform how we think about energy, transport, finance and much more. Whilst Taylor and Bronstone<sup>53</sup> provide some insights into how top down policies and bottom up initiatives can bring about change, the window of opportunity for leaders of the liberal order to seize the initiative is clearly closing.

**In the European Union (and the eurozone) reforms are needed to increase the legitimacy of – i.e. the democratic nature of – its institutions; markets need to be viewed in their social embeddedness.** In order to avoid worst-case scenarios, pragmatic public policies need to reconcile the requirements of a free economy with what political and social inclusion mean in a democracy.

**Working on a “new social contract” is a must for making our societies more inclusive, for averting their further radicalization.** A new social contract would have to redefine the boundaries of the welfare state, restore the principle of “equal opportunities” at the centre of social policies, find ways to foster social inclusion (minimum wage is an idea to be considered), adapt education to what new technologies entail in their cultural and social impact, combat economic (power) concentration that is inimical to sound competition and that leads to market abuse, reduce (if not eliminate) the range of “winners take all” competition, rein in finance, punish tax evasion and tax avoidance resolutely, encourage community and commons based initiatives, etc.

**It may be that we are going through the downward phase of a very long-term economic cycle (i.e. Kondratiev, Schumpeter<sup>54</sup>). Such a phase can explain the ‘inward looking syndrome’ (a resurrected nationalism) one sees in industrialized societies;** the Great Recession (the global financial crisis) belongs, admittedly, to the downward phase of a secular cycle. The new industrial technological revolution and the emergence of new global economic powerhouses play an important part in such dynamics, which are increasingly non-linear and disruptive. What Gideon Rachman calls the “*rise of the civilisation state*”<sup>55</sup> compounds the geopolitical and a related political and economic *regime* completion/confrontation.

The strain in society which is caused by economic conditions can be compounded by inter-ethnic and religious conflicts. “The clash of civilizations” that Samuel Huntington forebode a couple of decades ago seems to find concrete forms in various parts of the world. Wars and geopolitical tensions do exacerbate “civilizational” misunderstandings.

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<sup>53</sup> Taylor A & Bronstone A (2019) *People, Place And Global Order: Foundations of a Networked Political Economy*. London: Routledge.

<sup>54</sup> Nikolai Kondratiev, a renowned Russian statistician who passed away in a Soviet gulag. He identified successive secular (very long-term) cycles (40-60 years) driven primarily by technological developments; these cycles would mirror social tensions and culminate in major conflicts. Joseph Schumpeter also thought in terms of long-term cycles in his ‘Theory of Economic Development’ (1911), where he emphasises ‘revolutionary’ technology clusters that change society’s technological foundation.

<sup>55</sup> Gideon Rachman, “China, India and the rise of the “civilization state””, Financial Times, 7 March 2019

For world peace **it is vital to prevent major conflicts, trade wars, and the destruction of the multilateral system that was created in the aftermath of World War II** (starting with the Bretton Woods system). This does not mean that major stakeholders in a global order cannot proceed to reform the multilateral order and inter-country relationships.

**One can imagine the emergence of a several bloc based international economic system, which should prevent the complete dismantling of an orderly, rules-based global system.**

The liberal order of the world, as established after the victory over Nazi Germany and its allies, is being severely tested.<sup>56</sup> But the liberal idea still has much support in the industrialized world. However, if its power to shape people's minds and conduct is to continue, **an enlightened version of liberalism ("embedded liberalism"<sup>57</sup>) needs to operate and political elites need to show more respect for their fellow citizens.** "Winners take all games" and extreme income inequality have to be fought against if democracy is to survive.

**The resilience of nation states needs to be considered in regional and international arrangements. This must be taken as a key datum in dealing with the tense relationship between nation states and global markets<sup>58</sup>.** The demise of nation states, as it was postulated by some pundits a couple of decades ago<sup>59</sup>, has proved to be a false dawn<sup>60</sup>. This reality poses major challenges in the European Union, for avoiding its further fragmentation against the backdrop of a seriously strained transatlantic relationship, trade conflicts, and a shifting balance of economic power toward Asia<sup>61</sup>. Those who advocate a "European sovereignty" in order to deal with future challenges imply, one way or another, a form of *European nationalism*. However, the latter rests on reconciling national with EU level interests, which in turn requires elites to provide a stake in the new order for Settlers.

Ever since the 80's, international relations analytics and derived policies have benefited from the two-level game theory. As Robert Putnam presented it, national decisions and political

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<sup>56</sup> See also Richard Haass, 'Liberal World Order, R.I.P.', *Project Syndicate*, 21 March 2018. Haass examines the Trump administration's attitude towards the order established after World War II, and its global impact.

<sup>57</sup> As put by John Ruggie, who is quoted by Jack Snyder (Op.cit, p.54)

<sup>58</sup> For Yael Tamir, the problems are rooted in the growing clash between nationalism and neoliberal globalism ("Building a Better Nationalism", *Foreign Affairs*, March-April 2019, pp.48-53). It is telling that this issue of *Foreign Affairs* has on its frontcover and as its leading topic "The New Nationalism".

<sup>59</sup> Kenichi Ohmae, *The End of the Nation State, The Rise of Regional Economies*, New York, Free Press, 1995

<sup>60</sup> William Pfaff seems to have had a much more acute sense of history in this respect (in his "The Wrath of Nations", New York, Simon & Schuster, 1993). See also my "Economic Vitality and Viability. A Dual Challenge for European Security", Frankfurt am Main, Peter Lang, 1995 (chapter 3 in particular)

<sup>61</sup> EEAG (European Economic Advisory Group), "A Fragmenting Europe in A Changing World", CESIFO, Munchen, 2019. Quite tellingly, the last chapter is called "Looking outward: Western disarray, China rising".



preferences influenced the choices countries make in the international arena<sup>62</sup>. Unsurprisingly, this is more visible nowadays than ever. **The Liberal International Order begins at home: if politicians are not committed to liberal values at national level, one can hardly expect them to do so in the multilateral agenda.**

**To sum up: Just as one can talk about ‘illiberal democracy’, one can identify ‘undemocratic liberalism’.**<sup>63</sup> This happens when people feel that they no longer have a grip on their lives, when they lose trust in their leaders, and when they ascribe decisions to the power of money (i.e. government capture by interest groups which are seen as illegitimate). **Elites and governments need to overhaul national and international policies so that they be able to “manage capitalism”<sup>64</sup>, reform it for the benefit of society at large.**

To the dismay of many, a fragility of democracy (i.e. of liberal values) is now all too apparent. This is all the more reason to learn the lessons of ancient and recent history, to be candid and honest about mistaken policies, and to be bold in trying to amend them. Democracy, with its liberal genes, is the best political regime mankind has come up with, at least in the West. Remembering Winston Churchill’s words is as timely as ever.

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<sup>62</sup> Putnam, R. D. (1988). Diplomacy and domestic politics: the logic of two-level games. *International organization*, 42(3), 427-460.

<sup>63</sup> Yascha Mounk, *The People vs. Democracy* (Harvard University Press, 2018). See also Dani Rodrik, ‘The Double Threat to Liberal Democracy’, *Project Syndicate*, 13 February 2018.

<sup>64</sup> Jack Snyder observes that over the past 30 years liberalism has become “disembedded”; that “elites in the US and Europe have steadily dismantled political controls that once allowed national governments to manage capitalism. They have constrained democratic politics to fit the logic of international markets and shifted policymaking to unaccountable bureaucracies...” (“The Broken Bargain. How Nationalism Came Back”, *Foreign Affairs*, March-April 2019, p.54)

**Appendix: The trade-off function of the “inward looking syndrome” (D. Daianu, 2017)**

Dilemmas an open society has when facing threats and trade-offs may be captured by economic analysis. More specifically, one can relate protection/security to openness (economic freedom) as public goods. This may be illustrated as a social utility function which includes protection/security (S) and economic freedom (O) as an expression of economic openness, as public goods. A function  $F = F(S, O)$  would indicate levels of citizens’ comfort in terms of the these public goods; it could look like  $F = ((1- a) xS + a xO)$ , where (a) would be a variable in consonance with people’s attitude toward the two public goods; this variable could not be higher than 1 and not lower than 0. The substitution between protection/security measures and economic openness (economic freedom) has limits because these two public goods (as a state of the social and economic system) are not completely independent of each other; from a certain level, protection measures, or restrictions may distort open society (democracy) exceedingly. Likewise, a total openness of the economy/society, with no rules and protection measures, may cause enormous costs, social anomia.

The graph below illustrates citizens’ growing need for protection in times of hardships, when threats abound. Various combinations of (S) and (O) may be imagined so as to ensure a degree of citizens acceptance that would minimize discontent/discomfort in given conditions. An optimal combination is where the price line (S, O) is tangent to the preference (social choice) curve (I). The (a) point refers to an initial level of economic freedom –as flows of capital, workforce, investment, and the range and scope of regulations. At point (a) things are relatively good, calm, and this is revealed by the price line between (S) and (O); a steeper slope,  $P_a$ , shows that (S) is regarded as being sufficient (people feel safe) and economic openness as a public good is in high demand.

When times worsen a more inward-looking society emerges; such a turnaround is revealed by the change in preferences in favour of (S). When the need for protection measures grows, the change is reflected by a less steep slope of the relative price, ( $P_b$ ), between (S) and economic openness (O); this may involve protectionism and other restrictive measures and their combination is indicated by point (b) on the indifference (utility) curve.

The graph below simplifies reality not least because it refers to people in general. However, *who* decides and *how* decisions are made regarding the two public goods brings politics into the limelight, as citizens may have different options, may share different political views or values; a community may be made up of different ethnical groups and religions, a large part of the population could be made up of immigrants, etc. In a democracy, one is tempted to say that the social collective option is given by the majority vote. But things are much more complicated if society is profoundly divided and diverging values are guiding people’ choices<sup>65</sup>.

It is also a fact that the way people value protection vs. openness may vary over time. What is abnormal, unpalatable today, may be termed differently at another moment in time; it may be that people adjust to different circumstances, their habit change.

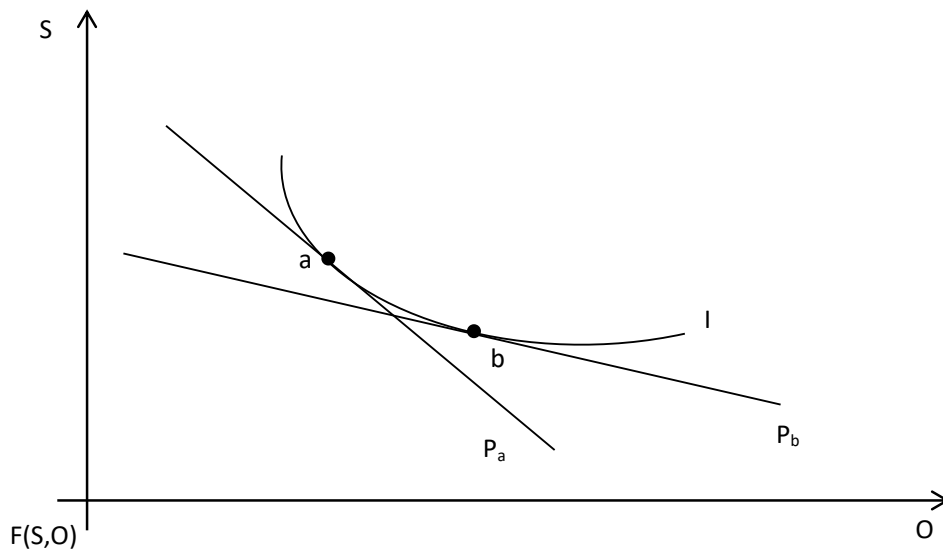
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The Nobel Prize winner John Kenneth Arrow explained the difficulties of building social utility functions in his “Social Choice and Individual Values”, Wiley, 1951

Protection measures can trigger similar responses from partners --and trade wars will likely lead to damages for all parties involved. Therefore, any measures at a national level should be pondered given potential answers from partners. Widespread protectionism comes along with significant dangers; beggar your neighbour policies can easily backfire. It is worth recalling that the globalism of the XIX century Victorian Era was followed by commercial and "hot" conflicts.

**Graph: The relation between protection (S) and economic openness (O)**




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