

# The Path to Minimizing Geopolitical Risks

By Masakazu Toyoda

The cover story of this year's White Paper on International Economy and Trade prepared by METI is, unsurprisingly, the impact of Russia's aggression in Ukraine. Until last year, "rising geopolitical risks" in general terms were considered as only one among about four major trends (the others being "digital transformation", "emphasis on common values" such as climate change, and "shifts in government industrial policy"). The geopolitical risks quickly moved to the top of the list.

Why are geopolitical risks rising? What are the implications? What should be done in the future?

Although the White Paper itself does not analyze the causes of the Ukrainian crisis, the consensus among experts seems to be that they reflect the contradictions inherent in an authoritarian state. What are those contradictions?

First, criticism of the regime is not allowed. Opposition parties are not nurtured, and the media are controlled by various means to restrict criticism of the regime. Second, the provision of information is controlled. Only information that is favorable to the regime is disseminated in such a way that the public mindset is gradually manipulated to suit the regime. Social media, which can be an important means of control, are allowed only if considered useful to the regime.

Third, as criticisms of the regime become scarce, the leaders are surrounded by nothing but "yes-men". Before long, the world, as seen by the regime, becomes detached from reality. With statements such as "Ukraine is invaded by neo-Nazis and must be liberated", "NATO's expansion is a threat to Russia" or "Ukraine is a threat", Russia is failing to understand that it is itself a threat to the world. The method of defending the regime determines the path it will take and the current crisis in Ukraine is a typical example of this process. Unfortunately, the resulting economic sanctions will severely impede the development of the global economy.

The White Paper on International Economy and Trade presents the IMF's latest economic outlook for 2022. Relative to previous estimates, the world economy in 2022 will decline by 0.8% to 3.6%. The Russian economy will be negatively affected by more than 10%, from a growth of 2.8% to a negative growth of 8.5%. For Ukraine it is even worse. In addition to the loss of civilian lives and a destroyed infrastructure, the Ukrainian economy is projected to drop by nearly 40%, from a previously anticipated growth of 3.6% to minus 35%. Is this really what the Russian administration has set out to achieve?

Democracies, however, also suffer from many contradictions and social divisions. In the United States, for example, the gap

between the rich and the poor is widening, while the middle class is shrinking. As the rich and the poor seek different policies, the magnitude of the differences in positions on globalization and climate change is astonishing. Moreover, a president's own refusal to recognize the results of an election could lead to a denial of democracy itself. Europe is facing a similar situation as the spread of social media appears to be fueling widening social divisions between the right and the left. Japan is no exception in terms of social fragmentation. The major ruling party, the Liberal Democratic Party (LDP), has rarely won a majority in the Upper House, in particular over the past 10 years. But in the House of Councilors election held on July 10 this year, the LDP secured slightly more than 50%, some 63 seats out of the 125 seats up for grabs. It was the first time in eight years it had reached the 60-seat level.

So what can be done about these differences between democratic and authoritarian regimes?

In the first place, we should assess if the division between democracy and authoritarianism is appropriate and classify regimes according to whether they are rules-oriented or not. Each country's social system has evolved and been built up based on its own history, national characteristics, and geographical tensions. Both democracy and authoritarianism present their own sets of problems.

In the midst of geopolitical uncertainties, it is very important to coexist peacefully, respect international rules and avoid needless confrontations, let alone needless wars. A natural strategy for companies to avoid risk and make long supply chains strong and flexible is to decentralize manufacturing bases and suppliers. Governments need to dig much further than simply decentralizing supply chains. They need to adhere to international rules to overcome the differences in social regimes and must recognize the different directions in which countries are heading. In areas where international rules are inadequate or insufficient, it is important to speed up the process of rule-making itself.

The cover story of the White Paper sends a clear message about the dire consequences of downplaying geopolitical risks. Governments should find ways to minimize geopolitical risks themselves by adhering to international rules.

Some say "Today's Ukraine is tomorrow's Asia." Those of us living in Asia need to keep this in mind.

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