

March 16, 2015

## **The New World Order: Part I**

As our regular readers know, we have been focusing for several years on the issue of the uncertainty surrounding America's superpower role. It has been our position that the U.S. has lacked a coherent foreign policy since the Cold War ended in the early 1990s. Although we cannot definitely say that a new policy is in place, the trappings of one does appear to be emerging.

Historians tend to adopt one of two methods to analyze history. One method is the "Great Man" theory, which looks at history as a progression of key personalities that change and shape the world. The other is the "Great Wave" theory, which suggests that social, economic and political factors work their way through history and individuals simply play their role by supporting or opposing the wave.<sup>1</sup> I lean toward the latter. Although exceptional people matter, history is littered with great people trying to make changes at the wrong time and failing miserably. Changes that the "failure" had attempted may eventually get made because the timing was right. Given this position on how history unfolds, the personalities matter less and thus, this is why I don't focus on people as much as trends.

The focus of this paper is how policy seems to be evolving and why; if this assessment is correct, who wins the next election has only

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<sup>1</sup> See WGR, 1/13/2014, [The Great Man or the Great Wave](#).

a marginal impact. Instead, it makes more sense to concentrate on the trends that are emerging and project how they are likely to evolve.

Although this report details my own analysis of emerging trends, it is greatly supported by the research of others. I want to especially mention George Friedman of Stratfor. His book on the next decade<sup>2</sup> and his firm's recent decade update<sup>3</sup> were instrumental in this analysis.

This will be a four-part report. Part I will begin with the evolution of U.S. foreign policy, focusing on the 25-year cycle pattern that has exhibited itself between the adaptations to new circumstances. Part II will recap the superpower role and the American adaptation of that role. Part III will examine why the current policy configuration is no longer adequate for the task. It will analyze the economic and military costs of the current policy and argue that the costs have become too high to maintain the current role. At the same time, it will conclude that no other nation can replace the U.S. in the hegemon role. Part IV will discuss the emerging policy configuration, including its key features that will allow the U.S. to maintain some degree of global influence and yet also make the costs more manageable. This analysis will include the winners and losers in this new order. And finally, as always, we will conclude Part IV with market ramifications,

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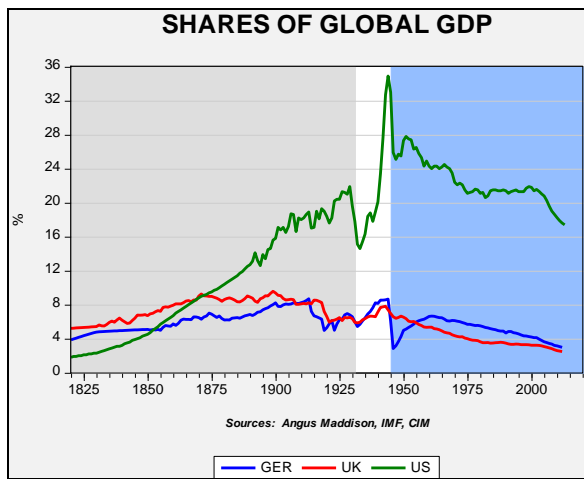
<sup>2</sup> Friedman, G. (2011). *The Next Decade*. New York, NY: DoubleDay.

<sup>3</sup> Stratfor Global Intelligence. Decade Forecast: 2015-2025. (2015, February 23).

which are many and significant if our view is correct.

**The Evolution of American Foreign Policy**

It should be noted that American foreign policy evolves and, in the face of major events, it often takes time for policymakers to develop a workable foreign policy stance. The U.S. was a rapidly rising power from the mid-1850s but really didn't begin to exercise power on a global stage until the late 1890s, despite becoming the world's largest economy in terms of GDP in 1870.



This chart shows the shares of global GDP from 1820 to 2013. By 1870, U.S. GDP had exceeded that of Britain; however, the latter remained the global hegemon.

Theodore Roosevelt was critical in shaping the new foreign policy that was more outward-focused than the previous policy. It should be noted that he could not have accomplished this change had the U.S. not experienced significant economic growth that established the country as a major power. In a sense, the expanding U.S. economy was the “wave” that supported the change in foreign policy.

Roosevelt’s strategy was to secure the Port of New Orleans by ousting Spain from

Cuba,<sup>4</sup> acquire colonies in the Far East and greatly expand the Navy. Until this policy change, U.S. foreign policy was mostly about the Western Hemisphere and North America. Matters of Europe were generally ignored. In effect, the U.S. was “punching below its weight” in terms of its economic power until Roosevelt changed policy. In a nutshell, the new policy stance was outward-looking but unwilling to shoulder major international burdens. American colonization was limited and the U.S. was more than willing to allow the European powers, especially Britain, to carry the burdens of global hegemony.

The U.S. reluctantly intervened in WWI, but waited until the conflict had reached a stalemate. Germany’s unrestricted submarine warfare against American civilian shipping led the American public to support entering the war.<sup>5</sup> President Wilson was reluctant to enter the conflict, seeing it as a European matter that was best solved by those powers. However, the attacks on shipping became a *casus belli* and led to America’s entry into the war. In addition, the collapse of Russia and the Bolshevik revolution meant Germany was fighting a single front war. The fear was that by shifting troops from the eastern front, Germany might win the war. Instead, U.S. intervention ended the stalemate and led to the Allies winning the war in 1918.

<sup>4</sup> See WGR, 1/5/2015, [The Cuban Thaw](#).

<sup>5</sup> The most famous case, the *Lusitania* in 1915, is considered one of the key events that turned the American public against Germany. However, it still took two more years and the Zimmerman Telegram, which offered a German promise to Mexico to support its retaking of former Mexican areas now controlled by the U.S., for President Wilson to ask Congress for a declaration of war. Interestingly enough, most historians now believe the *Lusitania* sunk quickly because a German torpedo detonated armaments, which it was carrying for the Allies.

However, U.S. policymakers decided to retreat from the world after the war. Congress refused to support Wilson's League of Nations and his successor, Warren Harding, won on a platform of a "return to normalcy." The U.S. became isolationist and left Britain to return to its superpower role.

Unfortunately, Britain was struggling to maintain this role. Its economy was severely hurt by the war and it was finding it difficult to maintain its colonies and provide the global reserve currency. The inability of Britain to provide the global public goods usually supplied by the hegemon and the U.S. refusal to accept that role was one reason for the onset of the Great Depression.<sup>6</sup>

After WWII, U.S. policymakers, for the most part, accepted the role of global hegemon. However, there were important dissenters. Senator Robert Taft, the eldest son of President William Howard Taft, feared that the deep involvement in world affairs would forever change America, forcing it to engage in policies that were diametrically opposed to democracy and small government. In general, as we will discuss next week, he was right. However, the alternative, which was probably forfeiting the world to communism or fighting WWIII, led the majority of policymakers to accept the burden of hegemony.

The U.S. held this role and shared in a global superpower duopoly with the Soviet Union from 1945 to 1990. In 1990, communism collapsed and the Cold War ended. Since then, four administrations

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<sup>6</sup> This thesis was developed by Charles Kindleberger. Kindleberger, C. (1986). *The World in Depression, 1929-1939*. Los Angeles, CA: The University of California Press.

have struggled to create a new foreign policy model. For the most part, all four have been wooed by the "siren song" of Wilsonian<sup>7</sup> foreign policy solutions which has led to "humanitarian" military operations in Somalia, Kosovo and Libya,<sup>8</sup> and wars of occupation in Afghanistan and Iraq. These conflicts were, at best, modestly successful and, at worst, debacles. It is arguable that all four presidents struggled to prioritize policy aims. President G.H.W. Bush was masterful in his execution of the First Gulf War but was consistently behind the curve on the collapse of communism and "wandered" into Somalia with disastrous results.<sup>9</sup> President Clinton's foreign policy was mostly focused on economic policy. The North American Free Trade Agreement was passed on his watch and both the Peso Crisis (1994) and the Asian Economic Crisis (1997-99) were managed by his administration. However, a deal between the Palestinians and the Israelis failed to materialize and the Kosovo Air Campaign halted Serbian aggression there at the cost of poisoning relations with Russia.<sup>10</sup> President G.W. Bush's War on Terrorism did prevent another 9/11 but it also led to an inconclusive war in Afghanistan and a disastrous war in Iraq. President Obama has engaged in air campaigns against Libya<sup>11</sup> and Islamic State and has clearly struggled with developing a consistent foreign policy. His vacillations with Egypt, the on-again, off-again moves against the Assad regime

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<sup>7</sup> See WGR, 1/9/2012, [The Archetypes of American Foreign Policy](#).

<sup>8</sup> For a critical analysis of Libya, see: Kuperman, A. (March/April 2015). Obama's Libya Debacle. *Foreign Affairs*, volume 94, number 2.

<sup>9</sup> See the "Black Hawk Down" incident, both movie and book: Bowden, M. (1999). *Black Hawk Down: A Story of Modern War*. New York, NY: Signet Books.

<sup>10</sup> Putin has argued that Kosovo set the precedent for the Russian invasions of Georgia in 2008 and the Crimea in 2014.

<sup>11</sup> Op. cit., Kuperman.

and his permissive policy with Russia have all raised concerns about his overall foreign policy.

Although these presidents have all struggled, my position is that they are caught in a developing wave. If one observes how new policies are developed, they seem to take about 25 years to evolve. For example, although the U.S. became the largest economy in the world by 1870, it didn't start playing a major global role until the late 1890s, about 25 years. The U.S. probably should have taken on the superpower mantle in 1920, but it wasn't until 1945, again, 25 years later, that the U.S. accepted the global hegemon role with the U.S.S.R. And now, about 25 years since the fall of communism, we may be seeing the glimmers of a workable hegemon policy developing.

### **The Next Step**

Before we discuss how this new policy is developing, it is important to lay the groundwork to fully understand the issues surrounding the superpower role. These issues entail a description of the basic global public goods that the superpower provides and a history of how the U.S. has provided those goods since 1945. Understanding these two factors are critical to our view of how new policies are developing. These two issues will be examined in next week's report.

Bill O'Grady  
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*This report was prepared by Bill O'Grady of Confluence Investment Management LLC and reflects the current opinion of the author. It is based upon sources and data believed to be accurate and reliable. Opinions and forward looking statements expressed are subject to change without notice. This information does not constitute a solicitation or an offer to buy or sell any security.*

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