Interdependence as a Constraint Upon State Behaviour

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Interdependence as a Constraint Upon State Behaviour: The Lessons of the 1973 Oil Crisis

This paper contends that realist interpretations of structural anarchy within the international system are inaccurate, and consequently, realism is ineffective as an explanatory framework. This paper advances the neoliberal theory of complex interdependence espoused by Keohane and Nye (2004) as a more accurate depiction of International Relations (IR). Through a critical analysis of the concepts of globalisation and sovereignty, this paper contends that globalised economic structures have served to foster a system characterised by interdependence. Via an evaluation of the theoretical paradigms of neoliberalism and structural realism, this contention will be advanced via a critical assessment of the 1973 oil crisis. For the purposes of this paper, realism refers to the theory of structural realism, as this represents the prevailing theory of IR (Grieco, 1988, p. 485). Similarly, the term 'Liberalism' is used to convey neoliberal theory, as opposed to traditional Liberalism.

Research Aim 1: Critically assess the assertion that international trade has mitigated structural anarchy as an obstacle to interstate cooperation

The theoretical study of International Relations (IR) is characterised by two antithetical perspectives: Realism, and Liberalism (Betts, 1992). Of these divergent theoretical paradigms, it is realism which has been traditionally dominant (Grieco, 1988, p. 485). The central theoretical assertion of structural realism is that the international system is defined by permanent structural anarchy (Ruggie, 1983, p. 263; Waltz, 1993, p. 59). In an anarchic system, the distribution of resources and capabilities within the system is such that an ordered relationship between the actors within the system is impossible. Therefore, systemic actors compete to ensure survival, which both realist and Liberal scholars assume to be the primary concern of rational actors (Morgenthau, 1985, p. 453; Carr, 2001, p. 78). States are considered the most significant of systemic actors, because the state is, by definition, the sole monopoliser of legitimate force in a given territory (Hobbes, 1999, pp. 103-228). However, other actors, most notably Multinational Corporations (MNCs) and Non-Governmental Organisations (NGOs) are present within the international system. Nonetheless, realists argue these actors are subordinate to states, because whichever given territory they operate in, they do so under state authority (Morgenthau, 1985, p. 531-533). Ultimately, realism is pessimistic about cooperative relations due to the systemic competition for security between actors, primarily states. Thus, realists consider structural anarchy to provide a constant check upon the behaviour of systemic actors.

This has been illustrated on several occasions, realists argue, by the failure of state attempts to institutionalise a collective security system as a forum for the resolution of international disputes (Grieco, 1988; Mearsheimer, 1994-95). This was most notably demonstrated by the failure of the effective operation of the League of Nations, an organisation formed to institutionalise cooperative interstate relations as a means of preserving peace (Betts, 1992, p. 18). The ultimate consequence of this failure was World War Two (Kolb, 2007, p. 223). However, theories of International Political Economy (IPE) provide an alternative explanation for the outbreak of World War Two. This assertion is based upon the contention that the creation of protectionist economic policies by European governments during the 1930's had prevented trade across the continent. This manoeuvre forced states to consider alternative means of achieving economic growth. It is argued that this need for development directly contributed towards an aggressive German foreign policy of territorial expansion, which inevitably led to conflict (Helleiner, 2006, p. 687; Martin *et al*, 2008). Nonetheless, this perspective is consistent with realist assertions, that states are inherently competitive, and that economic development is subsumed within the state interest of survival (Morgenthau, 1985, p. 453).

The principle alternative to realist theory is provided by the Liberal school of thought (Keohane and Martin, 1995, p. 48). Liberal theory is most significantly different from realism in that liberal scholars assume systemic actors to hold primacy over the international structure (Kupchan and Kupchan, 1995, pp. 54-55). As a consequence of this assumption, Liberal scholars assert that structural anarchy can be overcome (Keohane and Martin, 1995). This is best represented by the neoliberal theory of 'Complex Interdependence' forwarded by Keohane and Nye (2004). Through this model, Keohane and Nye argue that the state centric approach of realism is too simplistic, and inadequate in attempting to explain the distribution of power within the international system (2004, p. 22). A further criticism, provided more broadly by neoliberal theory as a whole, is that realism mistakenly takes the state to be a single entity, as opposed to an amalgamation of different groups and interests (Hermann, 2001, p. 48, Hudson, 2005, p. 1). Consequently, realism 'black boxes' the state as a unitary actor, when the reality is more complicated (Houghton, 2007, p. 29; Hudson, 2005, p. 3). More specifically, the theory purported by Keohane and Nye is derived from three core assumptions: societies are connected by various avenues in addition to interstate relations; there is no hierarchy of issues within the system; military force has declined in importance as a means of resolving international issues (Keohane and Nye, 2004, pp. 20-25). Keohane and Nye do not argue that the model of complex interdependence is always applicable in IR. However, they do argue that in several important fields, complex interdependence provides a superior theoretical framework for explanation than structural realism (Keohane and Nye, 2004, pp. 86-109).

This is most notable when assessing the inter-state relations within Europe that have developed since World War Two (Buzan, 1991, p. 432). As opposed to economic protectionism, Europe is defined by a single market, with many countries sharing the Euro as a currency (ECB, 2011a). Subsequently, the stability of the Euro is ensured by the European Central Bank (ECB, 2011b). In turn, this is operated by the European Union (EU), a supranational governing entity, which continues to grow, both in membership and in legislative power (Keohane and Martin, 1995, p. 48). Beyond regional structures such as the EU, international trading patterns have become integrated to such an extent as to facilitate interdependent partnerships (Keohane and Nye, 2004, pp. 143-182). Even realists admit that the use of force is damaging to modern states, with material gains less discernable than during World War Two (Van Evera, 1998). Trade is a more efficient source of development than conquest. Thus, even states acting according to realism will eschew conflict in favour of trade (Schneider and Troeger, 2006). A prevailing example of this is the current relationship between the governments of the USA and China. Though realism suggests that these states should be in direct competition (Morgenthau, 1985), their trading relationship ensures a system of interdependence. American banks increasingly rely upon Chinese credit to fund investment, with China the greatest overseas owner of US Government debt (US Treasury, 2011). At the same time, Chinese economic growth is fuelled principally by the export of goods to the United States (US Census Bureau, 2011). This framework of political and economic integration is incompatible with realist theory (Jervis, 1978).

Another direct result of increasing international trade is that MNC's have grown in significance (Klein, 2007, pp. 385-406; Strange, 1985, p. 235). As noted previously, realists argue that MNC's are subordinate to the political authority of states, and are therefore inferior (Krasner, 1995, p. 357). However, this does not sufficiently explain the distribution of power and capabilities in the international system (Keohane and Nye, 2004; Wallerstein, 1980). For example, several multinational companies have greater economic power than many states (Forbes, 2011). Moreover, there are instances of states becoming reliant upon foreign multinationals via economic dependence (Cardoso and Faletto, 1979; Eloy and Casagrande, 1996, pp. 122-123).

A notable example of this is the operations of the oil multinational Exxon Mobil in Indonesia. Whilst the company glean huge profits from its operations within the province of Aceh, the local people remain impoverished. Despite this situation, the Indonesian government is unwilling to exert pressure upon Exxon Mobil for a fairer distribution of wealth, due to a dependency upon the company for the existing revenue gained from taxation (Keys *et al*, 2006, p. 198).

Under a realist system of structural anarchy, such a distribution of power is not possible (Mearsheimer, 1994-95).

Therefore, it is reasonable to assume that anarchy is not as absolute as realists would assert (Wendt, 1992). Moreover, it is inferred that trade interdependence has played a central role in overcoming such an anarchic structure, though this assertion will be further examined.

Research Aim 2: Evaluate the claim that globalisation has diffused the sovereignty of nation-states

The broad understanding of globalisation is that, similarly to the first theme of complex interdependence, it refers to a widening network of connections surrounding political, economic and social systems and issues (McGrew, 1998, pp. 300-302). However, as Keohane and Nye state, complex interdependence is a condition, whereas globalisation is a process (2004, p. 229). The specific nature of that process is debatable, though the contestation of globalisation as a term can be narrowed to three divergent theoretical perspectives (Hirst, 1997; McGrew, 1998). The first of these is known as the hyperglobalist perspective. Hyperglobalists argue that globalisation represents a process of increasing interconnection between societies, MNC's and individuals, contributing to an altered structure of international relations whereby the influence of the state is steadily decreasing (Beck, 2006; Clark, 1999; Strange, 1996). This is disputed by globalisation sceptics, who contend that the process of globalisation is actually strengthening the state as an actor (Hirst *et al*, 2009; Wiess, 1998). Sceptics assert that governance over international issues is weakening, and as a response to this change, the nation-state is becoming more prominent (Hirst, 1997; Yeung, 1998, p. 297). Sceptics fiercely refute hyperglobalist assertions of international society, and argue that this is limited by cultural factors (Huntington, 1998). Transformationalists constitute the third perspective, but limit their position to observable processes, as opposed to an argument regarding potential outcomes of the globalisation process (McGrew, 1998). Significantly though, transformationalists represent the consensus between hyperglobalists and sceptics in asserting the existence of a significant transformation throughout international processes.

Globalisation is at once both complicated and enhanced by the notion of sovereignty. The idea of sovereignty is closely tied to concepts of power, both formal and informal. Thus, contestation over the meaning of the term is inevitable (Friedrichs, 2001; Jackson, 2007). Nonetheless, it is widely accepted that sovereignty equates to supreme political authority (Hobbes, 1999; Jackson, 2007, p. 297). However, the issue is complicated by questions over who holds sovereignty within a state. For example, as explained previously, the state is the greatest legitimated political entity. Therefore it stands to reason that the head of state holds sovereignty. However, this is not the case in Britain, where the head of state is the queen, yet decision-making power is held by Parliament (British Parliament, 2010). Thus, sovereignty is, by its very nature, diffused. As such, realist claims of a monolithic state, represented in the international system as a single actor, are false (Houghton, 2007). Furthermore, with the merging of political, social and economic structures that has been accelerated by processes of globalisation, sovereignty could equally refer to a monopoly on legitimate authority in a given issue area (Rudolph, 2005). Much as power can be construed in different forms, the conceptualisation of sovereignty as a political term is a narrow definition (Friedrichs, 2001; Jackson, 2007; Rudolph, 2005).

The debates surrounding the conceptualisation of these terms are enhanced by the widespread economic shift that occurred in the 1970's. This was spearheaded by the monetarist theory of Milton Friedman, as a result of a broader shift in economic policy within capitalist economies (Friedman, 1968; 2009). More specifically, the salience of monetarism is attributable to the 1973 oil shock, though this will be critically assessed the third section of this paper. The central aim of monetarism, or economic neoliberalism, is to control inflation through efficient expenditure (Wilkinson, 2000, p. 648). Theoretically, this process is assumed to result from industrial privatisation, because the necessity for companies to compete in a 'race to the bottom' prompts increased competition. This in turn leads to lower prices for consumer goods, countering the effects of inflation (National Archives, 1973). The ultimate theoretical implication of these principles is international economic deregulation, promoting a freedom of trade between states and markets (Strange, 1985, p. 235). As a result of this process, theoretically, economic liberalisation creates greater political interdependence, thus preventing conflict escalation (Keohane and Nye, 2004, pp. 20-33; Martin *et al*, 2008). The previous example of the European Union, along with the stated trading relationship between the USA and China, appear to validate this assumption. However, one of the consequences of this globalised deregulation is that isolated economic crises quickly become systemic (Stork, 1974, pp. 14-15).

The most recent financial crisis has provided a powerful illustration of this (IMF, 2009, p. 2). The specific case of

Iceland provides a good example. When the economic crash hit, the Icelandic government was too small and indebted to act as an effective lender of last resort to bail out the domestic banking sector (European Commission, 2011). The reason that the extent of this debt was so great is that the Icelandic financial sector is part of a wider global banking structure, which developed as a result of the adoption of neoliberal economic policies outlined in the Washington consensus (Yeung, 1998). The knock on effect of this is that financial crises are global in scale, though there is debate as to whether this is a new phenomenon (Wallerstein, 1980). In this instance, Iceland has recently applied for full European Union membership, in order to stabilise the economy. This manoeuvre will result in the Icelandic government ceding a great extent of its political and economic decision-making power to the EU. However, this move is undemocratic, as it is opposed by a majority of Iceland's population (BBC, 2011; European Commission, 2011). Whilst the Icelandic government does have the sovereign right to reject EU legislative demands, this would prevent Iceland from attaining EU membership. As demonstrated, this is a necessity in order to avoid a greater economic crisis. Thus, this example emphasises how the globalisation of financial markets results in the significant weakening of the nation-state, and diffuses sovereignty (Friedrichs, 2001; Yeung, 1998).

However, economic neoliberalism is not universal (Helleiner, 2006; Garrett, 1998; Giddens, 1998). Moreover, despite economic neoliberals advocating reduced state involvement as a means of development, statistical evidence conveys protectionist policies as the best means of economic success (Strange, 1985, p. 248-250). A notable example of a state that achieved rapid economic growth and success as a direct result of this policy is South Korea (Strange, 1985, p. 248). By building protective tariffs around its nascent automotive industry, South Korea was able to develop products for export which were able to compete successfully within foreign markets. As a result of this, South Korea's domestic economy achieved a currency surplus, which led to subsequent long-term economic growth (Strange, 1985, pp. 248-249). Significantly, it is important to note that economic protectionism, as previously demonstrated, was utilised extensively by industrialised European states (Strange, 1985, pp. 235-238). Such practices consequently illustrate how governments can be capable of retaining economic sovereignty. Nonetheless, for reasons previously explained, liberal economic policies have become widely adopted. In addition, even those countries that gained from protectionist policies have largely liberalised their economies, with South Korea notably committed to free trade policies through the World Trade Organisation (WTO, 2008).

Ultimately, the dual processes of economic liberalisation and globalisation, of finance in particular, have served to erode the sovereignty of the nation-state (Yeung, 1998). However, the success of protectionist policies illustrates that governments have the ability to retain economic sovereignty via centralised decision-making (Strange, 1985). Nonetheless, a growing trend of economic interdependence is clearly established (Friedrichs, 2001; Keohane and Nye, 2004; Strange, 1996). Furthermore, this can be directly attributed to economic neoliberalism, and a ceding of centralised decision-making power to external institutions.

Research Aim 3: Analyse the contention that the 1973 oil crisis demonstrated the limitations placed upon state sovereignty by 'complex interdependence'

The oil crisis of 1973 was caused by the deliberate fall in oil production initiated by the governments of several Middle Eastern states, directed towards several Western governments that had economically supported Israel during the Yom Kippur War (Licklider, 1998, p. 206; Stork, 1974, pp. 5-6). Acting as the Organisation of Arab Petroleum Exporting Countries (OAPEC), the governments of Saudi Arabia, Iran, Iraq, Abu Dhabi, Kuwait and Qatar launched a coordinated price raise, in addition to production cuts (Yetiv, 2004, p.141). The reasons for this manoeuvre are grounded in the historical antipathy many Arabs hold towards the state of Israel, which they see as illegitimate (Yetiv, 2004, pp. 147-150). However, this specific use of the so called 'oil weapon' was derived from the economic support that Israel received, primarily from the United states, during the Yom Kippur War (Licklider, 1998; Yetiv, 2004, p.141). Whilst the war itself was the result of a normative ideological conflict, the coordination of the Organisation of Arab Petroleum Exporting Countries (OAPEC) as a cohesive opposition to the states backing Israel can be simply framed in realist terms (Jervis, 1978).

Using Walt's theory of alliance behaviour, the actions of the OAPEC states can clearly be framed as balancing behaviour against the threat of Israeli aggression (1987). This theoretical explanation is supported by security dilemma theory, which accounts for the escalation of conflict on the basis of security fears (Jervis, 1978). Security dilemma theory is applicable in this situation due to the fact that the previous Arab-Israeli war in 1967 was derived from such a cause, resulting in pre emptive Israeli action (Walt, 1987, pp. 88-148). Thus, the actions of the Israeli forces in the 1967 war reinforce Walt's assertion of a balance of threat as a cause for the actions OAPEC, even though OAPEC is not a military alliance. In addition, realists would argue that by raising the price of oil and cutting production, the OAPEC member states sought to enhance internal security by increasing revenue (Morgenthau, 1985, p. 531-533). This contention is enhanced by the subsequent success of the Saudi government in attaining a controlling stake in Aramco, which currently controls and produces more oil than any other company in the world (Financial Times, 2006). This has therefore allowed the Saudi state to attain a powerful position of economic sovereignty. However, such a theoretical framework is weakened by an inability to explain the close interdependent political and economic factors that were emphasised by this crisis (Stork, 1974). The immediate effect of the 1973 oil crisis was, if not to cause, then to exacerbate global recession, inducing stagflation in several domestic economies (BP, 2011, p. 15; Yetiv, 2004, pp.140-144). Economically, the long term result of the oil crisis, and a direct consequence of stagflation, was a shift in western states towards the neoliberal economic policies that have been previously outlined (National Archives, 1973; Stork, 1974, pp. 14-15).

As demonstrated by the previously highlighted case of Iceland, the result of this has often been the loss of economic sovereignty to external actors. This phenomenon has led to the theoretical contention by several scholars that the international system is characterised by structural dependency (Cardoso and Faletto, 1979; Frank, 1969; Klein, 2007). This argument is based around the assertion that the conditional measures of international institutions such as the World Bank (WB) and International Monetary Fund (IMF) prevent economies from developing by creating trade deficits (Santos-Paulino and Thirlwall, 2004). Though these institutions originally held the purpose of providing short and long term financial assistance to state governments, during the 1970's this became conditional upon the adoption of neoliberal economic policies (IMF, 2011). Economic neoliberals argue that adoption of these policies creates more competitive domestic industries (Winters, 2004). However, in practice, this does not happen because localised businesses are unable to effectively compete with multinational companies (Keys *et al*, 2006, p. 201; Tausch, 2010). Subsequently, this creates an ever-increasing national trade deficit, because national exports tend to be products of a lower value than those which are imported, weakening the value of domestic currency (Santos-Paulino and Thirlwall, 2004). However, with the alternative often being no financial aid at all, state governments suffering from economic crises logically choose to accept these terms in order to prevent greater ruin (Tausch, 2010).

Structural theories of dependency thus provide an interesting explanation for global trading patterns, and are worth consideration. However, as a means of explaining political relationships between systemic actors, complex interdependence provides a superior theoretical framework, because this model considers a wider range of factors (Keohane and Nye, 2004, pp. 20-28). Moreover, the contentions of Keohane and Nye, as opposed to those of dependency theorists, were largely validated by the long-term effects of the 1973 oil crisis. This is conveyed most markedly by evidence that both oil exporting and oil importing states were damaged economically by the embargo (Stork, 1974). As Yetiv (2004, p. 142) acknowledges, the inflation caused by the use of the oil weapon pushed up the prices of goods imported from those countries that had been targeted. Though Saudi Arabia was able to overcome this issue, many OPEC states were impoverished due to a need to import goods, particularly those produced in the United States (Santos-Paulino and Thirlwall, 2004; Yetiv, 2004, p. 144). This reflects a clear demonstration of an interdependent trading relationship between exporters and importers, and further erodes the notion of sovereignty as an absolute concept.

Notably, as conveyed by the previously illustrated example of Indonesia, some states are more sovereign, in terms of *de facto* authority, than others. Furthermore, the Iraq war of 2003 represents a stark reminder that military power still underlines this division, contrary to theoretical assertions of complex interdependence (Acharya, 2007). Nonetheless, the most salient effects of the oil crisis have been a deepening and widening of integrated relations between states, and perhaps more significantly, markets (Stork, 1974, pp. 14-15). Furthermore, those states which bucked this trend, such as Saudi Arabia, represent exceptional cases (Yetiv, 2004, p. 144). Therefore, the 1973 oil crisis served to convey how the development of relations between systemic actors has become characterised more by systems of complex interdependence, than by realist assertions of anarchic power balancing. This assertion has been reinforced by the increased globalisation of neoliberal capitalism, in conjunction with a broad diffusion of national sovereignty. Thus, it is interdependence, rather than anarchy, that principally constrains and defines state behaviour.

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