

# International Economic Policy for the Polycrisis

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## **1 International economic policy – theory and practice**

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# 1 International economic policy – theory and practice

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## **Introduction**

In theory, international economic policy includes the study of different schools of economic and political thought, such as economic liberalism, protectionism, trade balance theories, and approaches based on game theory and institutional theory. In practice, it refers to specific actions taken by states and international institutions to manage their economic relations with other states, global corporations, and international institutions. This includes the conduct of independent, to a certain extent, macroeconomic policies in a global context, negotiations and entering into trade agreements, government interventions on issues affected by competitiveness and trade, the management of foreign exchange, and influencing monetary and tax policies.

In the theoretical discourse, international economic policy differs from the practical dimension, although the justifying function of simplistic neoclassical economic theory has been embedded in the political discourse of the last few decades. It can be even argued that neoliberal economics with the idea of a free market<sup>1</sup> and a flawed indicator of progress reflected in GDP has played a key role in the politics and shaping of international economic relations. After all, allocative efficiency reflects the use of available resources but only selectively maximises welfare, where quasi-competitive efficiency is often determined by state interventionism rather than the free market. Finally, international economic policy is about not only competitiveness centred around economic productivity but also a hard political and market game backed by a given ideology and strong protectionism, or even outright economic or military force. This chapter presents the processes shaping globalisation and international integration as the extension of international economics and its theory, international trade policy from a systemic perspective, and political economy in the discourse of macroeconomic global analysis and its significance within international economic policy. It proposes a new definition of deglobalisation and outlines theories of international politics, characteristics of international economic policy, theories of international trade in international economic policy, and classification of models for measuring and analysing international economic policy. It concludes with the analysis of competitiveness in international economic policy, with the so-called superpowers, such as the United States, China,

the European Union, India, and Russia, as identified on the basis of a prior review of the literature on the subject in terms of economic and military potential. On the basis of aggregated data from the World Bank database reflecting all variables for the study of the world economy, six variables were identified on the basis of correlational significance: (1) GDP (in billion, rate of economic growth); (2) GDP *per capita* (PPP, rate of economic growth *per capita* according to purchasing power parity); (3) M EXP (military expenditure); (4) TRADE S (trade in services); (5) TRADE (total trade of a country, i.e. exports and imports); and (6) TNR (total natural resources rents, per cent of a country's GDP relative to the uncertainty index (World Uncertainty Index – WUI, denoted below as U-index<sup>2</sup>), with WUI based on an additive model with fixed effects depending on six economic variables. The aim of the first phase of the research was to build a panel model of the world economy based on nearly 1,500 parameters from the World Bank database, looking for both a fixed effect (FE) model and a random effect (RE) model. No significant relationships were found as a result of the modelling, so separate linear regression models were performed for the five entities/countries under study (including the EU). Based on the regression coefficient, this made it possible to determine the strength of the influence of the variables studied and the significance.

### **Globalisation and international integration**

Globalisation has a history of more than a thousand years and stems from armed conflicts and competitive struggles between powers, although it went unnamed for many centuries. It was not until the 15th century that the noun “globe” appeared in use in English to denote a round (spherical) earth.<sup>3</sup> The adjectival term for the global sphere came into use in the 17th century (and globally in the 19th century).<sup>4</sup> The term “globalism” did not enter global circulation until the 1940s.<sup>5</sup> In internationalist terms, globalisation, through international politics, international trade, and economic cooperation (including investment), refers to a more global and interconnected world where the physical boundaries between countries are blurring in light of an increasingly widespread flow of information, goods, services, capital, investment, and people.<sup>6</sup>

Globalisation is inherent in the political power accompanying conquests and the emergence of international trade networks over the centuries. The principles of globalisation stem from the dominance, at a given time, of a particular superpower imposing its values and laws on other countries.<sup>7</sup> Examples of such superpowers in the history include the Mongol Empire, territorially the largest in all history (the 13th century), the Ottoman Empire (the 15th and 16th centuries), the Spanish Habsburg Monarchy (the 16th and 17th centuries), the British Empire (the 18th and 19th centuries), and the so-called associated European powers, that is, France, Germany, and Russia (the 19th century). The 20th century belonged to two superpowers – the United States, economically unparalleled, and Russia (the Soviet Union), burdened by problems of regime change. The 21st century is seen as a century of several superpowers, including the United States, China, the European Union,

India, Russia, and Japan, the latter not having superpower subjectivity but remaining a key player in international politics due to its political and economic position.

Thanks to the development of trade, global financial centres were born. Amsterdam (1780–1794) lost its dominance of maritime trade after losing a naval war (1784) and handed over primacy to London. The Port of London concentrated on trade in goods, on specialised banking activities on the basis of the Bank of England established in 1694, and on marine insurance. Trade through London was directly supported by the colonies of the British Empire, which, between 1784 and 1840, included British Raj (today's India, Pakistan, and Bangladesh), Canada, Australia (including New South Wales, Victoria, and Wales, among others), New Zealand, colonies in Africa (today's Zimbabwe, Zambia, Kenya, and Nigeria, among others), and the Caribbean (including Jamaica, Barbados, and Trinidad and Tobago, among others). Income from foreign trade proved the strength of the state, and military expenditure was the largest part of public expenditure for many centuries, not only in European countries.<sup>8</sup> Customs duties on foreign trade under King Henry VI of England in the 15th century accounted for 50% of public revenue. In the 18th century, Britain's military expenditure represented 70% of public expenditure.<sup>9</sup> At the time, Britain was in a struggle for colonial domination and control of strategic areas of the world with Austria, France, Spain, and Russia, culminating in the Seven Years' War (1756–1763). The war ended with Britain's victory (with Prussia as its coalition partner) and the weakening of France and Spain.<sup>10</sup> In a sense, Britain monopolised the importation of goods into the colonies by means of the so-called Navigation Acts. They allowed only traders and manufacturers from the colonising country to import goods into the colonies, while all other goods produced in a country other than the colonising country (Great Britain) not only had to pass through the coloniser's port but were taxed in there at a rate of 20% (the so-called royal fifth)<sup>11</sup> and other high tariffs, which were applied largely until the middle of the 19th century. This model of a far-from-liberal industrial and trade policy in international integration was implemented in the 19th century by France, Germany, and the United States.<sup>12</sup>

In fact, until the First World War, Paris was the world's second largest financial centre next to London and the world's second largest colonial empire. The Second World War significantly weakened the economic and financial role of Berlin and London, making New York the global financial centre of the world between 1945 and 1980 (in constant competition with London). The period from 1981 to 2009 was marked by increasing globalisation (not only financial), with Hong Kong, San Francisco, Singapore, Los Angeles, Shanghai, Beijing, Paris, and Tokyo becoming major players in the sphere of global financial centres in subsequent years (in addition to the leaders, i.e. New York and London). Recent systemic changes and one-off events, such as Brexit, the COVID-19 pandemic, the US–China trade war, and Russia's full-scale war with Ukraine, are likely to lead to a further weakening of the global financial centre in London in favour of Amsterdam, Dublin, Frankfurt, and Paris (and possibly Warszawa). These new centres also weaken a major player in the United States (New York), also lessened by China, provided that they

build an increasingly effective coalition of dependent and cooperating states. Singapore's dominance in Asia seems equally likely, with Hong Kong increasingly losing its position as a global financial centre.<sup>13</sup>

In essence, globalisation concerns economic, political, and cultural categories in which the role of the Western-centric world order has been called into question, especially in the second decade of the 21st century. This is called re-globalisation or deglobalisation where, in light of a new balance of power, the very concept of globalisation is being redefined, its directions are changed, and various processes are revised.<sup>14</sup> Another narrative of globalisation defines the following approaches<sup>15</sup>:

- a) hyper-globalisation – the acceleration of cross-border flows of population, capital, culture, ideas, or technology influencing a country's socio-economic policies and negatively affecting national sovereignty (the literature is dominated by both review and commentary, critical,<sup>16</sup> and enthusiastic<sup>17</sup> approaches);
- b) anti-globalisation – neoliberal approaches and trends to globalisation and countering the negative effects of globalisation;
- c) alter-globalisation – incorporating social justice, inclusivity, and supposedly democratic modes of globalisation;
- d) re-globalisation – the globalist response to populism and nationalist attitudes, promoting the post-neoliberal direction of globalisation.

In a sense, the global economy is at odds with the idea of nation states, although it can function well in such a system. It is up to nation states to decide which political system they will choose. In this respect, they have to realise that economic globalisation can be avoided but at the price of limiting the global nature of markets. Note that it is impossible to reconcile the three variables of globalisation: political democracy, national sovereignty, and full capacity for self-determination with hyper-globalisation.<sup>18</sup> Attempting to reconcile these variables will always lead to some, large or small, deficits in decision-making, sovereignty, and democracy.

A competing narrative, emerging more broadly in the 1990s and centred around the further course of globalisation, is deglobalisation. The pioneering work in this area was developed by S. Amin (1990),<sup>19</sup> who questioned development policies based entirely on the subordination of a country's development strategy to the goals of globalisation. He proposed auto-centrism and the internal reconstruction of the national economy, disregarding global factors and rejecting the neoliberal models of globalisation in favour of the construction of economic sovereignty, the strengthening of cooperation between developing countries (so-called South-South cooperation), and the democratisation of international relations as part of greater participation of developing countries in the international institutional system.

Deglobalisation is generally analysed in three dimensions: (a) as a series of processes reversing globalisation; (b) as a decentralisation of the West; and (c) as a temporary wave of change in global politics.<sup>20</sup> Deglobalisation is a less interconnected world,<sup>21</sup> or a differently interconnected world, in which the hitherto familiar global international institutions still exist, but their role is determined not only by

West-centric thinking. It seems clear that deglobalisation will serve to the greatest extent those states that are militarily and economically strongest and that the very process of deglobalisation may be detached from social justice.<sup>22</sup> In terms of international economic policy and geopolitical insecurity,<sup>23</sup> deglobalisation may mean greater use of domestic factors of production for the needs of one's own economy and reduced dependence on foreign direct investment and export production.<sup>24</sup> However, while the first part of this thesis may be correct under certain assumptions, the second implies challenges, prompting the identification of the risks of a global polycrisis, understood as the simultaneous occurrence of at least three systemic risks in social and natural global systems, leading ultimately to a drastic deterioration of humanity's prospects. "A global polycrisis, should it occur, will inherit the four core properties of systemic risks – extreme complexity, high nonlinearity, trans-boundary causality, and deep uncertainty – while also exhibiting causal synchronisation among risks".<sup>25</sup> This complexity is certainly closer to the times of deglobalisation, variously defined, than hyper-globalisation. Therefore, this chapter redefines deglobalisation in the international economic policy as a process of polycrisis pluralisation of the functioning of individual national economies – incorporated into greater manifestations of protectionism, preferences, and global trade destinations – in which domestic production is more self-sufficient or, conversely, dependent on another country, foreign expansion is targeted, and foreign direct investment is dependent on affiliation groups, economic, technological, and military strength, and relations with major global powers. It should also be noted that the impact of geopolitical events on the withdrawal of trade globalisation has not been proven, but the nature of globalisation itself is different.

Globalization has been pronounced dead many times before, but none of those predictions has come to pass. Global integration has long evolved in waves – and recent developments triggered by the pandemic and geopolitical tremors are not necessarily an exception. The widely-used indicators of globalization, such as international trade and capital flows, have rebounded strongly, despite the fears of discriminatory fragmentation and protectionism.<sup>26</sup>

The most possible scenario for international trade is the development of the digital economy and digital partnerships. Despite the significant increase in customs barriers to international trade in recent years (58.9%), the predominance of technological barriers over customs barriers is noticeable. In addition, the growth of high-tech dynamics (74.94%) is clearly visible, which in this scenario drives both the increase in the globalisation index and the increase in digital competitiveness.<sup>27</sup> The technological breakthroughs of the world's largest producer country (China) will have a positive impact, at the micro and meso levels, on reducing dependence on foreign suppliers for Chinese companies in the high-value-added product (HVAP) sector. This means that China, by adapting to its evolving supply chains, will bet on financing technological breakthroughs and subsequently significantly increase its share of the global high-tech market.<sup>28</sup>

## Theories of international politics

Theories of international politics have played and continue to play a key role in international relations. Perhaps the key theories include realism (and later Kenneth Waltz's structural neorealism<sup>29</sup>), liberalism, constructivism, hegemony theory, dependency theory, and game theory in international relations. Based on or parallel to them, other theories have grown up, such as security theory (security studies),<sup>30</sup> cultural dialogue theory,<sup>31</sup> intersectional theory,<sup>32</sup> post-colonial theory,<sup>33</sup> and feminist international theory.<sup>34</sup>

Realist thought focusing on the centrality of power, competitiveness between states, and the adoption of the primacy of state action through self-interest and security was already taking shape in the 16th and 17th centuries thanks to Niccolò Machiavelli and Thomas Hobbes. However, its attribution to the canon of international relations materialised in the mid-20th century through one of its main precursors, Hans Morgenthau.<sup>35</sup> In realism, it is states that are the main actors in international relations, seeking to assert power, security, and survival. They always show a tendency towards conflict and competition, rejecting the existence of a centre of international power. The second half of the 20th century clearly demonstrated the emergence of international centric structures where power begins to be distributed among states and stability is determined by the existence and influence of global hegemons. This gave birth to Kenneth Waltz's structural neorealism in the 1980s. The approach emerged as a critique of classical realism and a development and modification of classical realism, identifying the international structure as the main determinant of states' behaviour, leaving aside their individual characteristics.

Liberalism had its episodes in the 18th century through Immanuel Kant,<sup>36</sup> but liberal concepts in international politics have been shaped since the late 19th century and beyond with an emphasis on the promotion of democracy, human rights, international cooperation, and the free market and trade. Liberalism also implies interdeterminism according to which states are active in shaping the international order and not merely subject to structural forces.<sup>37</sup>

Constructivism in international relations emerged in the 1980s. It focuses on the importance of ideas, norms, and social constructs in shaping the behaviour of international actors and in creating international systems and institutions. In this approach, social constructs are determined by values, experiences, and beliefs and formed through evolution, while certain situations and events are seen from the perspective of identification and perception, with the emphasis on individual and collective identities.<sup>38</sup>

The theory of hegemony in international politics, which contributed to the development of key works and analyses, was developed in the 20th century. It examines the role of one state or group of states (the hegemon) in shaping the international order and the impact of this dominance on the stability and functioning of the international system. Its main assumption is that there is a dominant state (the hegemon), which is the central actor with a significant military, economic, technological, cultural, or political advantage over other actors in the international

system. In this model, the hegemon plays a stabilising role and provides security but, in return, imposes its own norms and values. The hegemon ensures the equilibrium of the international system by controlling and influencing the actions of other states that could in some way threaten the existing world order. The theory assumes the cyclical nature of hegemonic cycles, which means that a change in the structures of the international system results in a change in the conditions and balance of power and the emergence of new hegemons.<sup>39</sup>

Dependency theory in international politics focuses on the analysis of inequalities between developed and developing countries resulting from historical processes, colonialism, and imperialism as well as on the impact of relations between them on the formation of the international order. It points out that the global economic system maintains structural inequalities and economic dependencies determined by economic relations with dominant countries. Inequalities are maintained through mechanisms that give rise to external debts, asymmetric investment relationships, and low commodity prices in dominant countries in the exploitation of cheap labour, markets, and natural resources. Dependency theory criticises traditional approaches to development, emphasising the need to change socio-economic structures to redress international inequalities.<sup>40</sup>

Game theory in international relations applies game models from game theory to analyse interactions between states and their decision-making in the international context. Its main assumption is that there are strategic interactions between states whereby decisions made by one state influence the decisions of other states and vice versa. Game theory analyses the risks and rewards of a given strategy by assuming that states are rational (which in itself would have to be contested) and seek to maximise their interests in the context of certain conditions and constraints. It should be noted that game theory makes use of various game models, such as zero-sum games, non-zero-sum games, repeated games, cooperative games, and non-cooperative games. These models help analyse different scenarios of international interactions and predict possible outcomes. Game theory in international relations is a useful analytical tool for studying and predicting the behaviour of international actors and the outcomes of their interactions. With mathematical models and appropriate inference patterns applied to them, it is easier to understand the dynamics of international relations, decision-making processes, and possible consequences for global stability and security.<sup>41</sup>

### **International economic policy**

The international economic policy of non-power states can be determined by two main priorities – stability in the region and the maintenance of territorial and political sovereignty as the most important aspect of security.<sup>42</sup> Furthermore, “economic policy deployed for national security or geopolitical purposes, sometimes called *geo-economics*, can make countries weaker, poorer and less secure”.<sup>43</sup>

The current division of international economic policy centres around two superpowers (China and the United States) and two so-called soft power superpowers (the European Union and India). Russia, which is certainly counted as a superpower



due to its nuclear potential but, due to a certain dependence on China, it is rather sidelined, also runs for this position.

International economic policy, understood through the lens of globalisation and the increasingly free movement of goods, ideas, capital, and people as part of greater social and economic integration that has evolved into fragmentation and deglobalisation, can be conventionally divided into six stages<sup>44</sup>:

- a) Industrialisation era (1870–1914) – a period of industrial development that originated in Britain and occurring under the so-called gold standard, dominant in Europe, North America, Australia, Argentina, and Canada. It contributed to the development of spinning machines, steam engines, and assembly lines, affecting the efficiency of the economy. It saw the transition from an agricultural economy to an industrial economy, with the development of the transport system and the separation of new social classes (working class and capitalist class).
- b) Interwar era (1914–1945) – a period of reversal of globalisation trends and directions that saw regionalisation and discriminatory trade barriers as a result of the two world wars and the emergence of totalitarian regimes in Germany, Italy, and the Soviet Union. The turbulent political and geo-economic changes of this period were marked by the Russian Revolution of 1917, the transformation of Russia into a communist state, the signing of the Treaty of Versailles of 1919, regulations obligating Germany to disarm, pay reparations, and cede part of its territory, the Great Depression (1929–1939), that is, an economic downturn initiated by the stock market crash of 1929, and the Spanish Civil War (1936–1939).
- c) Bretton Woods era (1945–1980) – the key objective of the Bretton Woods agreement was to create a stable financial system after the end of Second World War. The main effects of the agreement include the creation of global international institutions to pursue coordinated socio-economic policies and increase international cooperation (e.g. the International Monetary Fund – IMF) and to ensure exchange rate stability by providing short-term financial assistance to member countries to ease payment difficulties. Other institutions include the World Bank, a financing institution for developmental projects in member countries, especially those affected by the devastation of war, and the Standing Monetary Committee to monitor exchange rates and help maintain international stability. Under the agreement, participating countries undertook to maintain fixed exchange rates against the dollar, and the US dollar was equated with the price of gold. This system lasted until the 1970s when it fell apart due to various economic tensions.
- d) Liberalisation (1980–2008) – the end of the Cold War and the removal of trade barriers in international economic cooperation, ultimately leading to the greatest international economic cooperation, mainly through the General Agreement on Tariffs and Trade (GATT) and the subsequent World Trade Organization (WTO) agreements (since 1995). This period saw deregulation and privatisation, leading to increased competitiveness on the one hand and deeper global integration

on the other, especially through the development of large emerging markets, such as India, China, Russia, and Brazil. New free-trade areas were created under the EU, the North American Free Trade Agreement (NAFTA), and the Association of Southeast Asian Nations (ASEAN). It should be noted that the liberalisation period created simultaneous trade and economic asymmetries and difficulties with adaptation for many countries and economic sectors.

- e) Slowbalisation (2008–2015) – shift away from liberalisation towards slower processes of international trade, economic integration, and foreign investment. The key moment marking the beginning of this period was the 2008+ Global Financial Crisis (GFC), which led directly to increased protectionist attitudes and trends in trade flows, foreign investment, and capital flows. The first symptom of the GFC was the financial crisis resulting in a significant increase in public debt, which was particularly acute for the United States, Greece, Portugal, Spain, Hungary, Iceland, and Italy. These countries observed an increasing decline in debt-driven productivity in the beginning of this period.<sup>45</sup> Protectionism was combined with economic nationalism, protecting national economic interests, technology, and production. As a result, the production was moved back to home countries or, closer, to markets, changing trade patterns and reducing global supply chains. Some societies became aware of the fact that globalisation and increased international economic policies also bring the negative effects, such as environmental degradation and increased inequality.
- f) Deglobalisation (2018–present) – the date is contractual, marking the fragmentation of the global economy. The process began with the US announcement of a trade war with China in 2018 (but was preceded two years earlier by then US President Donald Trump’s announcement of plans to counter unfair trade practices by China<sup>46</sup>).

In early 2018, the US raised tariffs on a few large import items – washing machines, solar panels, steel, and aluminium. While these tariffs did not discriminate by origin, it soon became apparent that US trade policies were targeting China. The US subsequently increased tariffs on thousands of products from China between 2018–19, ultimately targeting roughly \$350 billion of imports from that country. China retaliated over several tariff waves, targeting about \$100 billion of US exports. The two parties signed an agreement to halt further tariff escalations in January 2020, but the existing tariffs remained in place as of 2021.<sup>47</sup>

This period saw the global crisis of globalisation triggered by the UK Brexit based on the Brexit referendum in 2016.<sup>48</sup> As of 2016, the United States and the UK lost their previous position in the international socio-economic order in favour of China (and Russia) and other rising powers of international actor states whose national sovereignty was far from the democratic legitimacy of power and where the politics of the authoritarian power decides, in supposed defence of its own national sovereignty, on the sovereignty of other states.<sup>49</sup> Deglobalisation manifested itself in even more trade protectionism and the

narrowing of labour markets, and deviations from global agreements, for example, US withdrawal from the Trans-Pacific Partnership in 2017, the Paris Agreement in 2017, the Iran Deal in 2018, and the NIL Intermediate-Range Nuclear Forces Treaty in 2019, and Turkey's withdrawal from the Istanbul Convention in 2021 on preventing violence against women. Another sign of deglobalisation was the COVID-19 pandemic, which accelerated deglobalisation trends and changes in economic policies around the world. It should be emphasised that deglobalisation is driven by hard-to-measure factors of resilience and national security and not by economic efficiency, as is the case for globalisation.<sup>50</sup> Note that the *laissez-faire* economics driving globalisation at the end of the 20th century needs to be significantly revised, especially in the context of limiting the negative effects of globalisation.<sup>51</sup> The deglobalisation factor model includes eight components: globalisation, pandemic (COVID-19), migration, nationalism, international trade, income inequality, manufacturing, and poverty.<sup>52</sup>

International economic policy is determined by foreign policy, represented in both the institutional stream and the activities of multinational corporations. It refers to the process of conceptualisation and the fulfilment and implementation of specific political and economic agendas according to that vision of the world that is represented, at a given moment, in the government of a given state or in the decision-making bodies of international integration groupings. This dimension is strongly marked by historical, cultural, social, and psychological factors,<sup>53</sup> often in isolation from the rationality of realist theories and a strong desire to shape asymmetries in economic relations.

### **International trade theories in international economic policy**

Between 1600 and 1700, global trade grew at a rate of 1% per year. In the 19th century, trade dynamics accelerated significantly to 4% per year. In 2022, global trade in goods grew 10% (y/y) and global trade in services recorded 15% growth (y/y).<sup>54</sup> As Rodrik (2015) rightly argues,<sup>55</sup> the increasingly extensive international economic integration resulted from the adoption of liberal ideas by individual governments as well as the use of historically developed patterns of expansion. It is difficult to dispute that opening up trade increases exports for those companies that export (goods, services, and capital) and thereby increases a country's foreign reserves, raising productivity and expanding markets.<sup>56</sup>

Empirical studies have repeatedly shown that economic integration at the global level leads to profit maximisation, influencing the specialised production and greater simplification.<sup>57</sup> International trade resulting from lower trade barriers has a positive impact on economic growth, promoting welfare.<sup>58</sup> However, trade openness only partially affects global competitiveness as it is also driven by such factors as the human capital held, foreign direct investment, technology, the financial system, the economy innovation rate, and the status of an economy within a group of countries integrated by trade and/or association agreements.<sup>59</sup>

In simplified terms, trade theory comprises classical trade theories and modern trade theories. The classical trade theories include the following:

- a) Mercantilism, dominant in Europe in the 16th to 18th centuries, believed that a country's wealth was measured by its holdings of gold and silver, advocating for policies such as tariffs and subsidies to promote exports and restrict imports in order to achieve a trade surplus.
- b) Absolute Advantage Theory proposed by Adam Smith<sup>60</sup> assumes the production of more efficient goods through specialisation and an absolute advantage over other countries.
- c) Comparative Advantage Theory,<sup>61</sup> based on the concept of absolute advantage, assumes that even if one country can produce all goods more efficiently than another country, both countries can still benefit from trade if they specialise in the production of goods in which they have a comparative advantage (i.e. where they have the lowest opportunity cost of production).
- d) Heckscher–Ohlin model argues that countries will export goods that make intensive use of factors of production that are abundant in their country, while importing goods with intensive use of scarce factors of production.

The modern trade theories include the following:

- a) New trade theory<sup>62</sup> assumes production flexibility and economies of scale, product differentiation resulting in a wide range of prices and differences in customer preferences, generation of network effects for the firms located along the supply chain, and the scaling up of internal trade on a global scale on the basis of developed internal patterns, including the development of industrial clusters and the concentration of production.
- b) Specific-factor model of trade<sup>63</sup> is an extension of the Heckscher–Ohlin model. It assumes the existence of two factors of production (e.g. labour and capital), mobility of one of the factors of production between sectors of the economy, fixed production technology guaranteeing invariability of scale, and specificity of production factors for a given industry or sector of the economy. It takes into account specificity of factors of production by analysing factor shifts in international trade patterns.
- c) Gravity-based models focus on more complex factors, such as product differentiation, scaling of production, network effects, and the geography of trade.

In general, gravity models are commonly used in the literature to analyse patterns of international trade, migration, tourism, and cross-border capital flows. Since income levels as a proportional function of economic size and the volume of balance trade flows do not fully explain geopolitical and geo-economic processes, it has become necessary to supplement these models with extensions of other social and economic variables.<sup>64</sup> However, the contemporary literature and practice of international economic policy use a number of theoretical and modelling approaches, often complementary as part of an interdisciplinary and

proof-of-concept methodology. Therefore, this chapter proposes the original list of international trade theories as models for measuring and analysing international economic policy (Table 1.1).

The 20 groups of models for measuring and analysing international economic policy show not only the multiplicity of methodological approaches to the problem-solving evaluation of socio-economic issues at the state and corporate levels but also the need to use different analytical approaches in parallel. This applies not only to the planned impact on the trade balance, investment growth, and competitiveness, but also to responses to the negative effects of benefit asymmetries, dumped imports, exclusion, and loss of regulatory and trade sovereignty. As argued by Findlay and O'Rourke (2007, p. 324),<sup>65</sup> integration into the global economic system can mean de-industrialisation, distortions in the exchange rate regime (if own currency is used), and/or restrictions in purchasing power as well as the loss of independent trade policies.

An example of this is multilateral free trade agreements (FTAs), burdened with long implementation periods for liberalisation procedures, which are not a fair and even stimulator of economic benefits for all member states as signatory partners. There will always be winners and losers for these agreements. However, a unilateral loss or win in all trade policies and leading specialisations is not always the case (in fact, it is usually not).<sup>66</sup> It should be remembered that, in a world of polarised zones centred around powers, such as the United States and China, the powers seek to exert as much leverage as possible and prefer, as a rule, to enter into bilateral agreements rather than multilateral ones, which require longer negotiations and the consideration of different interests. Other states should bear in mind that the economic choice or the choice for security need not be the only one, and it is necessary to seek alternative by compromise and balance in providing multilateral security and multilateral economic relations.<sup>67</sup> Well-negotiated agreements or the use of the Bertrand's competition model can be such an alternative. In such a case, the theoretically economically weaker state, wanting to balance the adverse impact of the agreement, has to provide differentiated production instead of homogeneous production.<sup>68</sup>

### **Competitiveness and power of influence in international economic policy**

Competitiveness in international economic policy refers to factor productivity, that is, more efficient use of resources.<sup>69</sup> It includes resilience to shocks and efficiency in the functioning of global value chains, financial stability directly resulting in effective risk management, and focus on quality.<sup>70</sup>

The main structural factors of the international competitiveness of national economies include the degree of diversification of the production structure and the strength of domestic production linkages, which are directly related to the technological structure of exports resulting from the level of technological and industrial development of an economy. Assuming that The Technologically Advanced Domestic Value-Added in Export (TADVA) basically reflects the above structural

Table 1.1 Models for measuring and analysing international economic policy.

Name of model/model category	Characteristics/parameters studied	Selected authors
Heckscher–Ohlin–Samuelson (HOS) model	It explores patterns of international trade, focusing on countries' productive resources. It concentrates on differences in factor endowments (such as labour and capital) as determinants of trade. The model is more theoretical in economic policy but allows to measure effects with regard to (a) resource allocation, (b) production structure, and (c) income.	Heckscher, and Ohlin (1933); Krugman (2001)
Gravity model of trade	It is similar to the gravity law, assuming that countries that are more similar geographically, economically, and culturally are more likely to trade with each other. Examples: Rose's gravity model, and Anderson–Wincoop gravity model of trade.	Anderson and van Wincoop (2003); Isard and Peck (1954); Capoeni (2023)
Exchange rate models	Factors influence exchange rates between countries. This category includes a number of models, such as short-run equilibrium models and long-run equilibrium models. Exchange rates are checked against (a) monetary policy (Interest Rate Parity) as well as (b) fiscal policy, financial crises, trade policy, and stabilisation policy.	Krugman and Obstfeld (2018); Baye and Prince (2016); Raczkowski and Klepacki (2024)
Capital demand model	It describes how foreign investment is attracted through differences in capital levels, interest rates, and other aspects of investment attractiveness. The demand for capital is checked against the interest rate, investment risk, capital trade and financial liberalisation, and other macroeconomic factors. Examples: production specialisation model, real interest rate differential model, asset demand model, labour force model, and simultaneous equations model.	Obstfeld and Rogoff (1996); Betermier <i>et al.</i> (2023)
Trade policy models	The impact of various trade actions, such as tariffs, subsidies, and trade agreements on a country's economy is taken into account. Theoretical models include Linder's directional coefficient model, Krugman's new theory of international trade, models of the dynamics of trade policy expectations, and country-group models. Other models include empirical models, trade policy analyses, and protectionist models.	Krugman <i>et al.</i> (2017); Finger and Krugman (1976); North (1990); Alessandria <i>et al.</i> (2021)
Phillips curve model	It analyses the relationship between inflation and the unemployment rate. It can be used in an international context to understand how economic policy affects employment and inflation. The model is divided into five basic sub-models (short-run, natural rate of unemployment, inflation expectations, adaptation, and volatility of the inflation rate and unemployment rate over different time periods).	Phillips (1958); Coibion <i>et al.</i> (2018); Ball and Mazumder (2011); Gudmundsson <i>et al.</i> (2024)

(Continued)

Table 1.1 (Continued)

<i>Name of model/model category</i>	<i>Characteristics/parameters studied</i>	<i>Selected authors</i>
Global macroeconomic models (with shocks)	They integrate macroeconomic data from different countries, allowing the analysis of global trends, such as global business cycles and the interdependence of economies (including as part of economic shocks). They include Global VAR (Vector Autoregression) models, Global Dynamic Stochastic General Equilibrium (DSGE) models, Global Computable General Equilibrium (CGE) models, the Global Trade Analysis Project (GTAP) model, the Global Integrated Monetary and Fiscal Model (GIMF), the Oxford Global Model (OxGEM), the United Nations Global Policy Model (UNGPM), and the Federal Reserve Board's Global Model (FRB/Global).	Dixon and Rimmer (2002); Obstfeld and Rogoff (1996); Smets and Wouters (2003)
Development models	They focus on the analysis and forecasting of development processes in developing countries. They cover various factors, such as human capital, institutional structure, and economic policy. Examples: development policy model, international trade theory model, technology transfer model, theory of economic growth model, and macroeconomic indicators model.	Friedman (1962); Sen (2009); Stiglitz (2012); Rodrik (2008)
Spillover effects model	It analyses how changes in one economy affect another, both positively and negatively. Examples: Mundell–Fleming model, trade policy interaction model, and financial regulation spillover model.	Krugman (1991); Blanchard and Milesi-Ferretti (2012)
Economic models of globalisation	They examine the effects of globalisation on countries' economies, analysing economic integration, capital flows, international trade, and other phenomena related to globalisation. Examples: multi-level governance of globalisation, networked globalisation, global village model, global values and cultures model, capital globalisation model, and interpretive structural modelling of globalisation/deglobalisation.	Gereffi and Humphrey (2005); Dicken (2015); Garg and Sushil (2021)
Model for political action in international trade	It analyses political factors that influence the formation of trade relations between countries, such as the impact of government decisions on international economic policy. Examples: degree theory model, strategic trade theory model, game theory model for trade negotiations, interest group influence theory model, anti-dumping theory model, and conflict/trade war generation model.	Krugman (1987); Dorn and Hanson (2016); Liang and Ding (2022)

(Continued)

Table 1.1 (Continued)

Name of model/model category	Characteristics/parameters studied	Selected authors
Political risk model	It analyses the impact of political factors on foreign investment, trade, and overall economic stability. Examples: institutional model, political change and uncertainty model, geopolitical model, macroeconomic model, and political risk model for international trade.	Baldwin and Evenett (2009); Acemoglu and Robinson (2006); Alesina and Perotti (1996); Besley and Persson (2018)
Panel econometrics model	It uses panel data (observations for different temporal and spatial units) to analyse relationships between economic and political variables. Examples: fixed effects model, random effects model, difference-in-differences model, fixed effects time series model, and common effects model.	Wooldridge (2010); Plümper <i>et al.</i> (2005)
Human development models	They use indicators, such as life expectancy, education, and <i>per capita</i> income, to measure the level of economic and social development. Examples: freedom model (Amartya Sen model), human development indicators (HDI) model, social capital model, sustainable development model, and socio-economic development model.	Sen (1999); Sachs (2015); Deaton (2013)
Institutional background model	It analyses the role of institutions, such as law, corruption, and regulatory systems, in shaping the economy. Examples: institutional trade theory model, financial institutions model, political institutions model, regulatory institutions model, and international institutions model.	Keohane and Martin (2003); Acemoglu and Robinson (2012); Rodrik <i>et al.</i> (2004)
Digital economy models	They focus on analysing the impact of digitisation, information technology, and innovation on international economic policy. Examples: digital platform model, digital innovation model, platform and sharing economy model, e-commerce and globalisation model, and digital economic growth model.	Digital Dividends (2016); Kenney and Zysman (2016)
Convergence model	It examines the process of convergence or divergence between countries in terms of living standards, production, and other indicators. Examples: Solow-Swan model, new growth theory model, beta convergence model, absolute convergence model, conditional convergence model, and deep equilibrium model.	Barro and Sala-i-Martin (1992, 1995); Stiglitz <i>et al.</i> (2010); Ling <i>et al.</i> (2023)

(Continued)



Table 1.1 (Continued)

<i>Name of model/model category</i>	<i>Characteristics/parameters studied</i>	<i>Selected authors</i>
Political and economic games model	It analyses the interactions between political and economic decisions, particularly in the context of international negotiations and trade agreements. Examples: game theory model for trade negotiations, prisoner's dilemma model, Cournot competition model, Hegel's hegemony model, Bertrand's competition model, and public good model.	Grossman and Helpman (2019); Olson (1965)
Sustainable development models	They analyse the impact of economic activities on the environment and sustainability, combining economic, social, and environmental aspects. Examples: "three dimensions of sustainability" model (broader in meaning than ESG), inclusive development model, resource-based economics model, sustainable consumption and production model, and corporate social responsibility model.	Sachs (2015); Zhang (2019)
Economic models of war	They examine the impact of warfare on the economies of the countries involved, taking into account changes in production, trade, inflation, and employment. Examples: war resources model, cost of conflict model, economic model of terrorism, trade effects model, financial effects model, and post-war economic consequences model.	Hirshleifer (2003); Blomberg and Hess (2008); Dube and Naidu (2018)

Source: Author's own elaboration

factors, by including input–output analysis and global value chains in the methodology of this study, the economies at the top of the ranking of international structural competitiveness are as follows: Japan, Taiwan, Germany, South Korea, the United States, and China (India ranked 28 and Russia ranked 38 according to TADVA). In the European Competitiveness Index (ECI) measure, China’s economy ranked only 17th, India were slightly worse than in TADVA (ranked 35th), and Russia took a similar position (ranked 39th), which shows that the international competitiveness of the Russian economy is low, regardless of the measure used. It should also be noted that the research reflects data from 2014<sup>71</sup> and much has changed in the global economy since then.

The overall competitiveness index in 2023 looked different against the current account balance (% of GDP, 2022 data) proving that there are winners and losers in international trade. The first group (winners) included Taiwan, the UAE, Saudi Arabia, Qatar, Norway, and other countries in Asia and West Asia, the Pacific, Africa, and South Asia that increased their level of competitiveness (positive current account balance). The losers included the UK, Hungary, Peru, Estonia, and a significant number of Eastern European economies. Both the United States and China were in the middle of the index. The polycrisis in the international competitiveness of individual economies resulted from instability in domestic energy production, volatile supply chains, and a negative current account balance.<sup>72</sup>

It seems that despite the grand and not always sensible ideas related to adjusting environmental and economic policies at all costs to reduce CO<sub>2</sub> emissions and achieve zero-carbon (which are only of declarative and not factual nature), macro-economic geopolitics and pragmatic approaches to poverty and inequality will win out (at least in the short and medium terms) by applying economic policy realism to international economic policies. However, there will be winners and losers here as well. This is due to the unequal distribution of the benefits of globalisation as well as the exclusion and marginalisation of certain societies or regions.<sup>73</sup>

Assuming that competitiveness can be equated with the strength of an economy’s influence and its relevance to other countries in the global system, it is reasonable to compare statistics for GDP (PPP), annual percentage growth rate of GDP, trade (share in GDP), trade in services (US dollars), total natural resources rents, military expenditure data as defined by NATO (position), and GDP *per capita* (US dollars) in the five countries under study, including the integration grouping of countries (the United States, Russia, China, India, and the EU) from 1990 to 2022 (Figures 1.1–1.7), and use linear regression econometric models to determine significant regression coefficients (Figures 1.8–1.15).

For the actors under study, linear regression models were performed, and the following parameters were marked on the graphs:

- U-index (uncertainty index);
- GDP G (billion) – GDP growth %;
- GDP (PPP) – nominal GDP;
- M EX – military expenditure;
- TRADE S – trade in services;

- TRADE – trade balance;
- TNR – total natural resources rents (% GDP);
- GDP PC – GDP *per capita*.

Comparative nominal GDP dynamics for China, the United States, India, Russia, the European Union, and the euro area from 1990 to 2022 shows that Russia and India recorded moderate economic growth relative to the comparison group over the period studied. Particularly noteworthy is China’s trajectory of dynamic economic growth from 1995 onwards, which was in line with the trend of economic growth in the United States from 2012 (Figure 1.1). However, the category of economic growth based on value *per capita* (GDP *per capita*) creates four clustering areas: (a) the leader (the United States), (b) the European Union and the euro area, (c) Russia and China, and (d) India (Figure 1.2). For China, this trend was in line with the annual percentage growth rate of GDP at market prices based on a constant local currency (US dollars) from 2004 to 2022. For Russia, the dynamics of this variable strongly deviated in 1990–2000 (Figure 1.3). The trade of the countries under study as a share of GDP (Figure 1.4) showed that the European Union and the euro area dominate globally in this model over the other countries in the peer group, showing an inversely proportional trend relationship in 2011–2019.

The same category of EU and euro area dominance applies to trade in service in 2009–2019 (Figure 1.5). The leader in generating total natural resources rents as a per cent of a country’s GDP is Russia (Figure 1.6) whose economy reflects

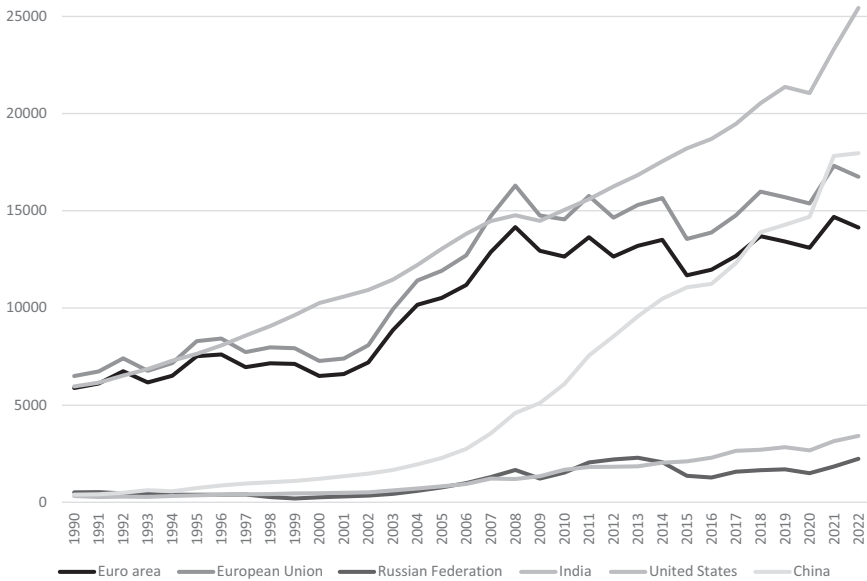


Figure 1.1 Comparative nominal GDP dynamics (in billion US dollars).

Source: Author’s own elaboration based on the World Bank database

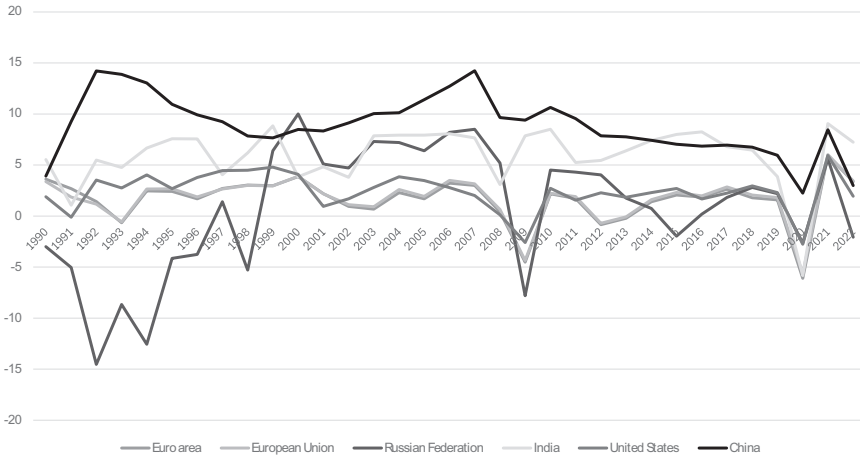


Figure 1.2 GDP per capita (US dollars).

Source: Author's own elaboration based on the World Bank database

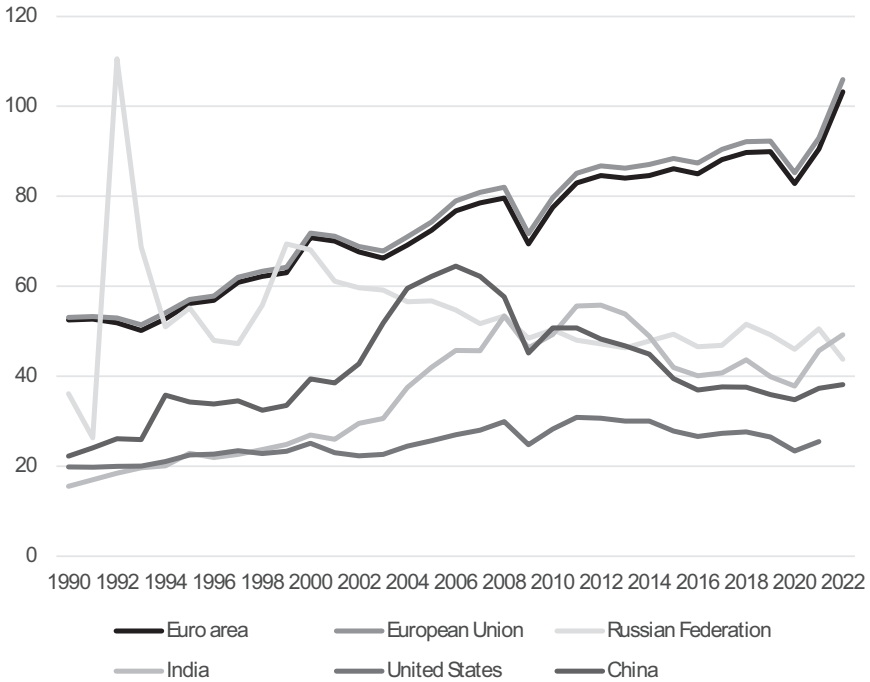


Figure 1.3 GDP growth – annual percentage growth rate of GDP at market prices based on constant local currency (%).

Source: Author's own elaboration based on the World Bank database

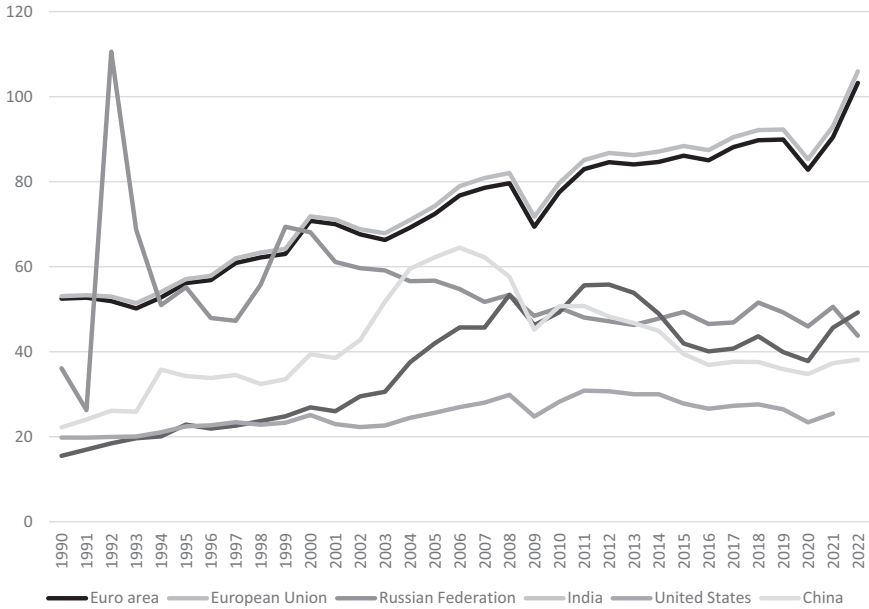


Figure 1.4 Trade balance (% GDP).

Source: Author’s own elaboration based on the World Bank database

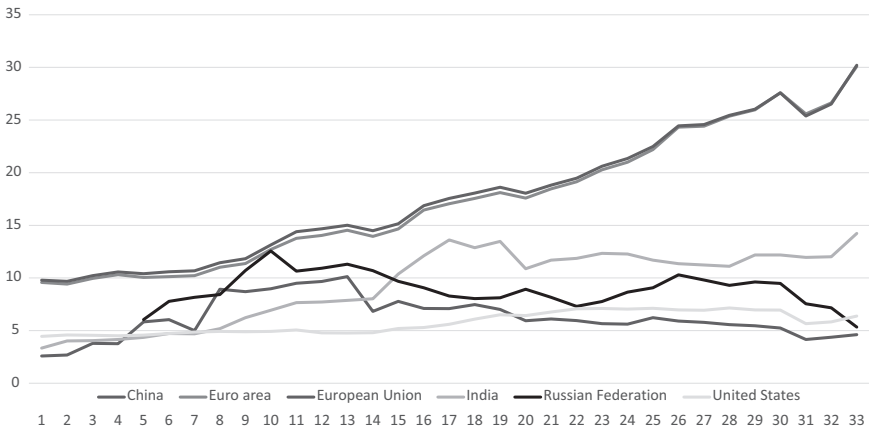


Figure 1.5 Trade in services (% GDP/USD).

Source: Author’s own elaboration based on the World Bank database

the contribution of the raw materials sector, including production and exports of oil, gas, metals, timber, and other natural resources, to total national income. The high volatility of this category is due to the exposure of the raw materials sector to global price fluctuations, which can lead to income volatility and vulnerability

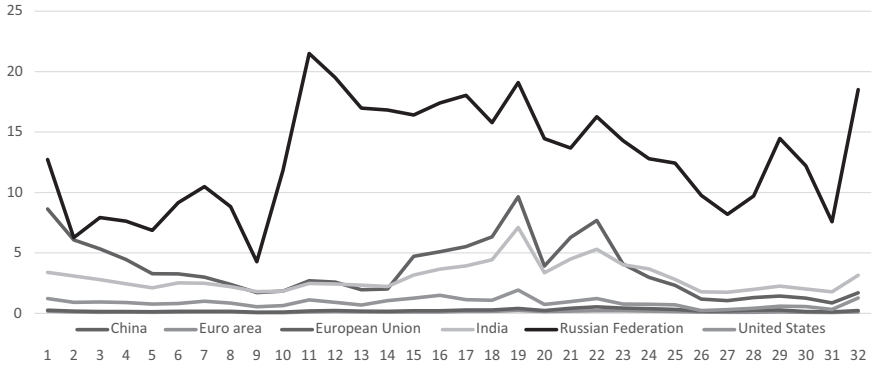


Figure 1.6 Total natural resources rents (% GDP/USD).

Source: Author's own elaboration based on the World Bank database

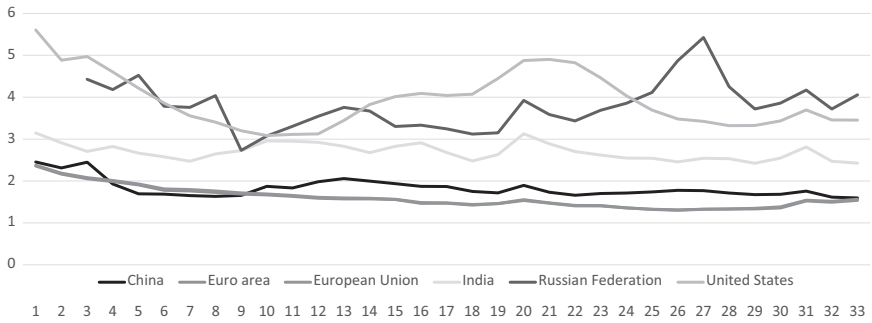


Figure 1.7 Military expenditure data as defined by NATO (% GDP/USD).

Source: Author's own elaboration based on the World Bank database

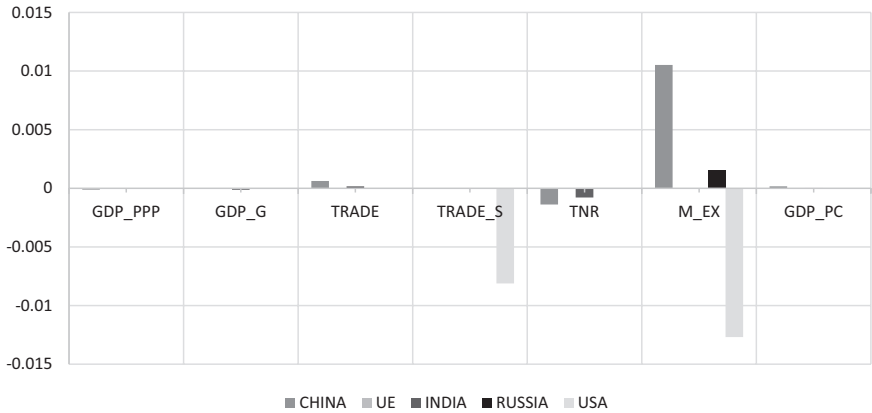


Figure 1.8 Influence of variables studied on the uncertainty index.

Source: Author's own elaboration based on the World Bank database

to global changes in supply and demand. In addition, the economy’s overdependence on natural-resource exports can hinder the development of other sectors of the economy and make the economy less diversified and more vulnerable to external shocks if new markets are not found in a timely manner and production is not diversified.

Another variable analysed is military expenditure, calculated according to the NATO definition, in which Russia for many years could rival with the United States. However, since the start of the annexation of Crimea in 2014, Russia has dethroned the United States becoming the undisputed leader in military expenditure (Figure 1.7).

Based on linear regression econometric models, significant regression coefficients were determined for the variables studied in five groups (the United States, Russia, China, India, and the EU).

For China and Russia, military expenditure has the strongest positive impact on the growth of the uncertainty index. For the United States, military expenditure has the strongest negative direction of dependence. The United States is also the only country/group of countries with the strongest negative impact on the “trade in service” uncertainty index. It is worth noting that in the case of Russia, only military expenditure has a significant impact on the level of the uncertainty index.

The level of GDP significantly reduces the uncertainty index (the United States, the EU, China), most in China and least in the EU. Country wealth calculated as GDP *per capita* significantly increases the level of the uncertainty index, most in China and least in the EU again.

In China and India, TRADE is a significant stimulant of the uncertainty index, and TNR is a significant destimulant.

An increase in the uncertainty index significantly reduces the value of GDP (PPP) in China, the United States, and the EU. The EU is a group of countries that

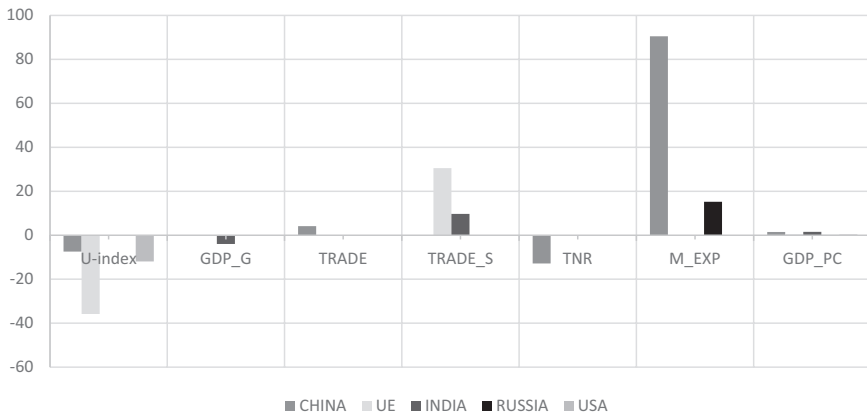


Figure 1.9 Influence of variables studied on nominal GDP.

Source: Author’s own elaboration based on the World Bank database

is most sensitive to this factor. An increase in military expenditure has the strongest positive GDP stimulation in China and Russia. TRADE has a significant positive effect on the level of GDP only in China. Trade in services significantly stimulates GDP in the EU and India. TNR is a significant destimulant in China only.

China is most affected by the level of economic growth in the variables studied (as many as three variables, i.e., total natural resources rents [% GDP], trade balance, and trade in services). The uncertainty index and trade in services significantly reduce the rate of economic growth, while TRADE significantly increases the level of economic growth (GDP\_G). Total natural resources rents as a per cent of a country’s GDP influence the level of economic growth, as measured by the economic growth rate (GDP\_G), in India and Russia, but in opposite directions, positively in Russia and negatively in India (natural resources and overexploitation of natural deposits have a destimulating effect on economic growth). In the EU, the level of economic growth is stimulated by trade (an increase in the Trade value by one unit affects the average economic growth rate by 0.5 units).

All variables significantly affect the level of the trade balance (Trade) in China. The level of TNR positively affects Trade, most in the EU and least in Russia. Trade in services has the strongest stimulating effect in the United States and the EU. The impact of military expenditure on the level of the trade balance (Trade) is destimulating and strongest in the EU and China.

Clearly more factors have a significantly statistical impact on the level of trade in services in the EU. The level of military expenditure and the uncertainty index have no significant effect in any country/country group. In all countries, the level of trade in services is significantly positively affected by trade (most in India and the EU). This means that if a country in the EU has natural resources, it is less interested in developing advanced and highly processed production.

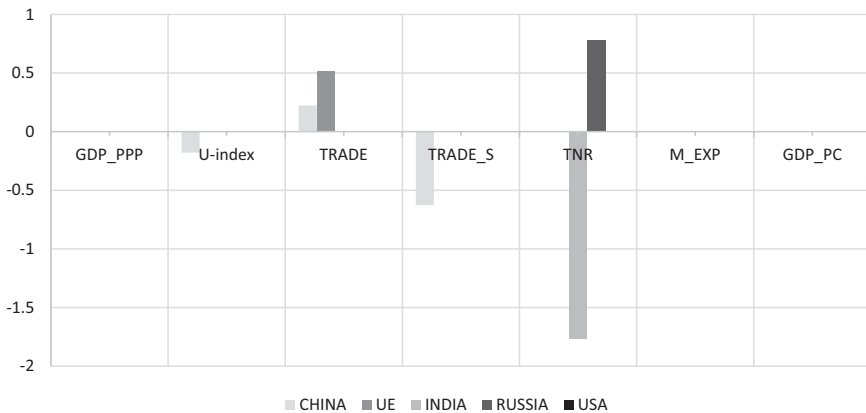


Figure 1.10 Influence of variables studied on the level of economic growth (GDP growth).

Source: Author’s own elaboration based on the World Bank database



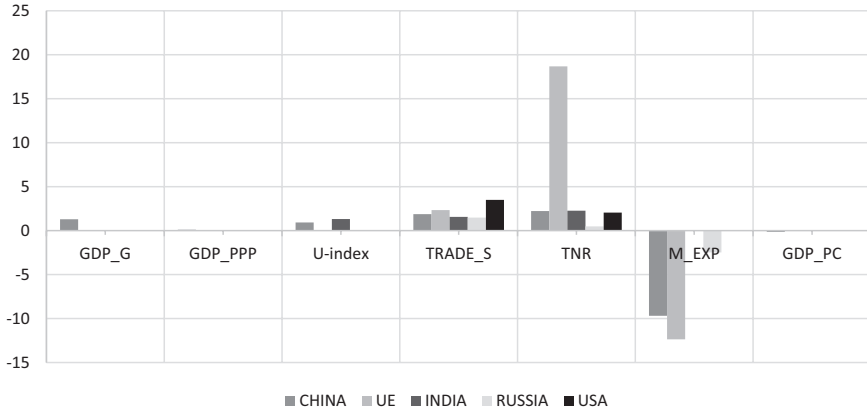


Figure 1.11 Impact of the variables studied on the trade balance (Trade).

Source: Author’s own elaboration based on the World Bank database

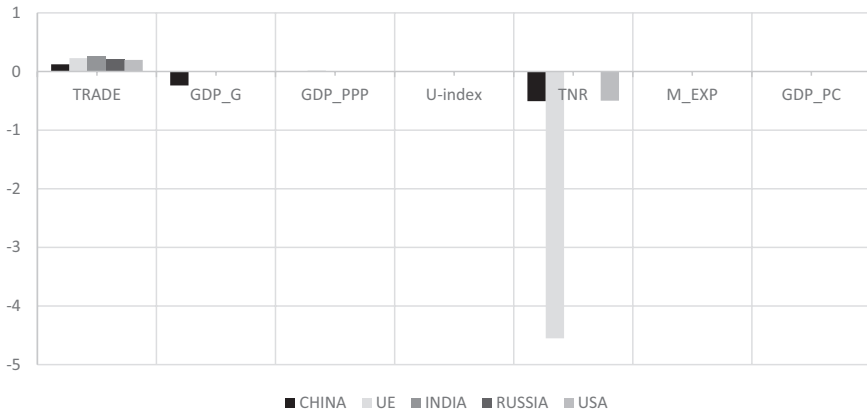


Figure 1.12 Influence of variables studied on trade in services.

Source: Author’s own elaboration based on the World Bank database

The correlations between military expenditure and total natural resources rents (TNR) in China, the United States, and the EU are strongest. As military expenditure increases, the upward pressure on natural resources exports increases (TNR: strongest impact in China and the United States). Both an increase in the uncertainty index and an increase in Trade in services reduce the level of TNR on average. The uncertainty index has the strongest impact in India. Trade in services levels are strongest in China and the United States.

In Russia, growth is significantly influenced by the growth of the trade balance (Trade) and the rate of economic growth, which shows the high dependence of the Russian economy on natural resources.

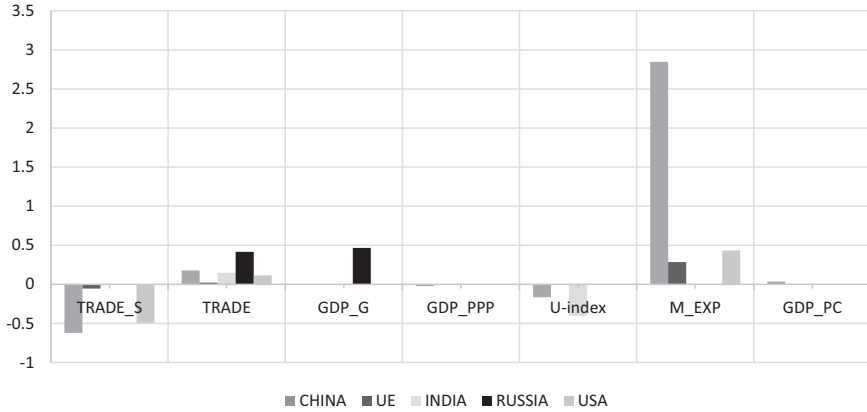


Figure 1.13 Influence of variables studied on total natural resources rents (TNR).

Source: Author’s own elaboration based on the World Bank database

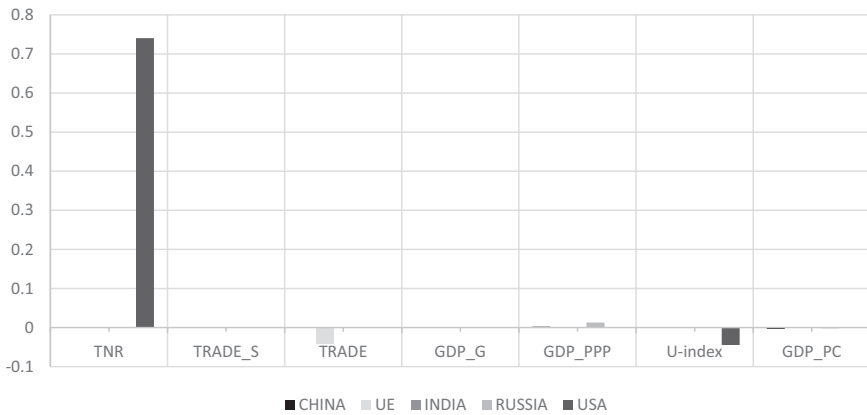


Figure 1.14 Influence of variables studied on military expenditure.

Source: Author’s own elaboration based on the World Bank database

The country with the strongest impact of macroeconomic factors on the level of military expenditure is the United States. An increase in the TNR strongly increases the level of military expenditure, while an increase in the uncertainty index reduces military expenditure (conservative US policy). In the case of the EU as a group of economically concentrated countries, an increase in the level of military expenditure and an increase in the level of the trade balance (Trade) significantly reduce military expenditure. Only in Russia does an increase in nominal GDP (GDP\_PPP) lead to the increase in the level of military expenditure.

Military expenditure in both Russia and China significantly reduces GDP per capita. In Russia, this impact is stronger than that in China (higher military

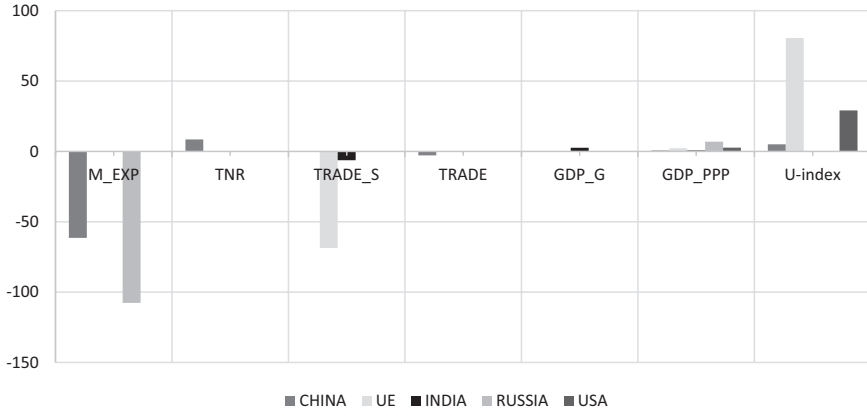


Figure 1.15 Influence of variables studied on GDP *per capita*.

Source: Author’s own elaboration based on the World Bank database

expenditure contributes to higher impoverishment dynamics). In the EU and the United States, the uncertainty index has the strongest stimulating effect. In the EU, the strongest destimulant relates to trade in services (oddly enough, trade in services causes a real decrease in GDP *per capita* and not an increase in GDP *per capita* dynamics). An increase in the uncertainty index in the EU results in a greater degree of hedging against uncertainty and more efficient financial management of households and businesses, influencing greater levels of welfare.

### Conclusion

The world is entering a new era of polycritical economic competition, and the need for unequal economic partnerships is apparent. A large group of countries will have to decide which political and economic bloc they want to belong to, mainly around the orbit of the United States and China.

One thing is for sure though: any decline of global economic ties will inevitably make each and every nation in the world poorer than it was in the world of flourishing globalization. Some countries or social groups will suffer less than others. But generally speaking, sustaining high pace of economic growth without an open global economy will hardly be feasible. This means that the world is entering an era of lower prosperity, higher instability, and prolonged uncertainty. The deeper the new divisions run, the stronger the negative effects are going to be.<sup>74</sup>

The uncertainty of economic policy in the United States is not conducive to the fragmentation of economic policy around the world as the risks of government policy and regulation for the near future are significant,<sup>75</sup> and causality fluctuates. It

is mainly due to the structural problems of the US economy, which have been built up over many years, and the degree of variable effectiveness of geoeconomics on foreign policy and international security within geopolitics.

Econometric studies of the international economic policy of the so-called superpowers, such as the EU, the United States, China, Russia, and India, show large disparities in the economic potentials of individual countries. The level of increased dynamics of military expenditure is indicative of a sense of insecurity, affecting mainly the level of the trade balance in the EU. The impact of military expenditure on the level of the trade balance is therefore destimulating and strongest in the EU and China, leading to upward pressure on natural-resource exports, mainly in China and the United States. Only in Russia does the increase in nominal GDP lead to the increase in the level of military expenditure, leading to greater impoverishment dynamics in Russia and China.

Total natural resources rents as a per cent of a country's GDP influence the level of economic growth in India and Russia, but in opposite directions, positively in Russia and negatively in India (natural resources and overexploitation of natural deposits have a destimulating effect on India's economic growth). In the EU, the level of economic growth is stimulated by trade where a one-unit increase in the trade balance affects the average economic growth rate by 0.5 units. The strength of the European Union (EU) definitely lies in its ability to trade, as evidenced by data and its position as the world leader in trade in industrial goods and services. The potential extension of the Russia-Ukraine armed conflict to European countries would weaken the EU's position as a major global trading partner, leading to an attempt by other superpowers and countries cooperating with these superpowers to take over these markets. Furthermore, ensuring a significant increase in the dynamics of military expenditure in EU countries could weaken the EU's position and trade balance. However, if a coordinated economic narrative is applied, in which military expenditure builds deterrence potential by influencing international relations and global stability, it could lead to a greater importance of the EU in global economic relations. This expenditure should be seen as an investment that protects the interests of the Community and its citizens by building a deployable deterrence force as an element of peace stimulating technological innovation that makes the entity independent.

## Notes

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