



Geopolitics and economic vulnerability

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In-depth study
Clingendael Monitor 2015



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Geopolitics and economic vulnerability

Introduction¹

For its economic prosperity the Netherlands is very dependent on its international environment, and is therefore not immune to external events and developments. As the recently published annual review of the *2015 Clingendael Monitor*, 'A world without order?', revealed today's international relations are characterised by two important trends, i.e. the changing global balance of power and mounting tensions between superpowers.² In light of the global interconnectedness of the Dutch economy, the question arises as to what these geopolitical developments (could) mean for the economic position of the Netherlands.

This study distinguishes between the economic susceptibility of the Netherlands and its economic vulnerability.³ Economic susceptibility is an inherent aspect of the extent to which the Netherlands has integrated into the European market and the global economic system. This study focuses on whether the Netherlands is economically vulnerable or in danger of becoming so as a result of such geopolitical developments: vulnerable in the sense that harmful effects occur which seriously hamper the smooth functioning of the Dutch economy and which may also have harmful political consequences due to other countries politically (mis)using economic relationships of dependence. From this point of view, economic vulnerability is closely related to the concept of economic security: the lower the level of vulnerability, the greater the economic security. The Dutch government has considered national economic security, i.e. the unhampered functioning of the Netherlands as an effective and efficient economy, to be one of the five vital interests of national security.⁴ Economic security is also one of the three strategic interests which are key to the Netherlands' international security strategy.⁵

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- 1 The authors would like to thank Anne Bakker for her contribution to this report as part of her research traineeship at the Netherlands Institute of International Relations "Clingendael" and Luc van de Goor, Ko Colijn and the co-readers at several Ministries for their valuable annotations on previous versions of the text. Finally, the authors would like to thank Peter Schregardus for editing the Dutch text.
 - 2 Jan Rood, Frans-Paul van der Putten & Minke Meijnders, *Een wereld zonder orde? (A world without order?) 2015 Clingendael Monitor*, The Hague: Netherlands Institute of International Relations "Clingendael", February 2015; see also: Jan Rood, 'Een wankle wereldorde' (*An uncertain world*), in: Jan Rood (final editing), *Een wankle wereldorde, 2014 Clingendael Strategic Monitor*, The Hague: Netherlands Institute of International Relations "Clingendael", June 2014, pp. 19-67.
 - 3 For this distinction, see: Robert O. Keohane & Joseph Nye, *Power and interdependence; World politics in transition*, Boston/Toronto: Little, Brown and Company, 1977, pp. 11-19.
 - 4 National Coordinator for Security and Counterterrorism, 'National Security', <https://www.nctv.nl/onderwerpen/nv/>
 - 5 Central government, "A secure Netherlands in a secure world - International Security Strategy", <http://www.rijksoverheid.nl/documenten-en-publicaties/rapporten/2013/06/21/veilige-wereld-veilig-nederland-internationale-veiligheidsstrategie.html>. https://www.nctv.nl/onderwerpen/prioriteiten_2015/economische_veiligheid/. In response to the report 'Between naivety and paranoia' of the Economic Security interdepartmental working group, the government has identified three priority sub-topics under the theme of economic security in 2014: foreign take-overs and investments in sectors which are classified as vital; limited access to raw materials/protection of trade routes; and (digital) espionage: <https://www.rijksoverheid.nl/documenten/kamerstukken/2014/06/11/beleidsreactie-rapportage-werkgroep-economische-veiligheid>

The basic assumption of this study is that the strong external economic dependence of the Netherlands does not necessarily imply (greater) vulnerability. This depends, *first of all*, on the nature of the relationships of dependence. If these are asymmetrical, i.e. the Netherlands is unilaterally dependent, the risk of vulnerability is greater, partly due to the (mis)use of these relationships for political purposes. However, also as a result of the greater interconnectedness, these relationships of dependence are often more complex and mutual, thereby reducing the likelihood that ill-willed parties will effectively take political advantage of them. As a result of the process of economic globalisation there is a strong tendency within the current global economic system towards production in chains, in which several countries are involved and the mutual dependencies are greater. Globalisation has brought with it a lower risk of vulnerability since there are more opportunities to diversify suppliers and markets.⁶

A *second* important factor is whether relationships of dependence are embedded in internationally agreed rules (WTO, IMF, etc.) which set limits on the conduct of States. Finally, the extent to which the Netherlands is economically vulnerable is strongly determined by its resilience and flexibility, i.e. its ability to prevent potential vulnerabilities or to redress the consequences.

The scope of this study is limited to economic vulnerability as a result of geopolitical developments. It is obvious that economic vulnerability can also result from non-geopolitical factors and events, such as serious natural, economic or financial shocks.⁷ Looking ahead to the next 5 to 10 years, this in-depth study of the *Clingendael Monitor* aims to gain a better understanding of the following two issues:

- How, in general, is the Dutch economy susceptible to international developments?
- What is the potential effect of geopolitical factors (shift in the balance of power, tensions between superpowers) on the economic susceptibility and what is the probability that these will make the Netherlands (more) economically vulnerable?

This theme has extra significance for the following three reasons. Firstly, the Netherlands has always tried to secure its interests in an open, global economic order based on market principles through multilateral agreements, procedures and regulations, particularly within the framework of the GATT/WTO and the EC/EU. However, the changes in the global playing field imply a decline in the influence of the Netherlands (and its partners) on the international rules of the game, rules moreover with which the emerging countries do not always comply.

Secondly, among the emerging powers are countries, in particular China, whose governments have a strong tendency to interfere in the markets and in the business operations of companies, with the inherent risk of political manipulation of economic relations and dependencies. Thirdly, as shown by the various editions of the *Clingendael (Strategic) Monitor*, this risk is greater in today's world characterised by mounting tensions between the superpowers, in particular the relations between Russia and the West (the European Union and the United States) and between China and the United States.

6 See i.a.: Miles Kahler, 'Economic security in an era of globalization: definition and provision', in: *The Pacific Review*, 17(2004)4, p.485-502; Stephen M. Carmel, 'Globalization, security, and economic well-being', in: *Naval War College Review*, 66(2013)1, pp. 41-55.

7 The collapse of Lehman Brothers in 2008 and the resulting serious effects on the global economic and financial system are an example of such a shock. According to some authors, the risk of such shocks, which are inherent to the global financial and economic system, has increased as a result of globalisation.

The above questions will be addressed in Sections 1 and 2 respectively. Section 1 briefly outlines the economic susceptibility of the Netherlands from different perspectives, while Section 2 explores the potential effects of geopolitical developments on this economic susceptibility. To gauge the actual effects would require considerably more data than currently available within the scope of this study. Yet, a survey of the possible effects will give a picture of the consequences of geopolitical developments for the susceptibility of the national economy over the next 5 to 10 years. Section 3 looks at how the Netherlands can boost its immune system in response to this susceptibility.

This study, the summary report 'A world without order?' and the previously published in-depth study 'Deterrence as a security concept against non-traditional threats' together constitute the *2015 Clingendael Monitor*. The Clingendael Monitor is published annually as part of the Strategic Monitor of the Netherlands government.

Integration of the Netherlands into the Global Economic and Financial System

The susceptibility of the Dutch economy to harmful effects as a result of international factors and developments is strongly determined by the level of integration of the Netherlands in the European and global economic and financial system.

This section uses several dimensions to analyse the interconnectedness and position of the Netherlands in greater detail: trade and international value chains; foreign direct investment; the international financial system; raw materials and energy; and the role of the internet in the economy.

Trade and International Value Chains

A country's economic susceptibility is to a considerable extent determined by the export dependency of its economy.⁸ For the Netherlands this dependency is relatively high; in 2013, Dutch exports accounted for over 64% of GDP⁹ while over the past few years their share in the GDP has increased significantly.¹⁰

Since the Second World War, and especially since the loss of Indonesia as a colony, the Netherlands' economic dependency has primarily focused on the European *hinterland* and the North American market, in particular as far as trade, investment and logistics are concerned. The European Union and the United States are still important partners for the Netherlands. Trade with EU partners and the United States accounts for 52% and 7% of Dutch imports, and 73% and 4% of Dutch exports respectively.¹¹ However, for a long time now, non-Western countries and regions (e.g. Russia, the Middle East and parts of Africa) have been the Netherlands's main suppliers of raw materials and energy. In addition, as a result of the changing economic relationships and the emergence of countries like China and India, non-traditional markets are becoming increasingly important for the Netherlands.

8 United Nations Development Programme, *Towards Human Resilience: Sustaining MDG progress in an age of economic uncertainty*, September 2011, p. 20.

9 CBS ('Statistics Netherlands'), *2015 Internationaliseringsmonitor: eerste kwartaal* ('Internationalisation Monitor: Q1'), The Hague/Heerlen, January 2015, p. 8.

10 Ibid.

11 Statistics Netherlands StatLine, *Internationale Handel 2014* ('International Trade 2014'); imports and exports according to the SITC classification.

The export of Dutch products to countries outside the EU has more than doubled within the space of ten years.¹² The BRICS countries jointly account for 17% of Dutch imports and 5% of Dutch exports¹³ and are thus eclipsing the United States as important trading partners. Particularly noteworthy is the increased role of China, especially given the great importance of this country as a trading partner for Germany (after the US, China is the largest market for Germany outside the EU)¹⁴ and the role which Germany in turn plays as the main economic partner for the Netherlands and as the EU's economic powerhouse.¹⁵ The Netherlands is therefore becoming increasingly interconnected with a global economic system in which an ever-growing number of (non-traditional) players and parties are adopting the role of partner and competitor.

One way to gain an understanding of the extent to which the Netherlands has become economically dependent and, in particular, susceptible to exogenous economic shocks, is by looking at what happens in case of a (sharp) drop in world trade. A model-based analysis is useful here. The Netherlands has ample macro-economic models at its disposal to estimate the effects on a national scale.¹⁶ The Netherlands Bureau for Economic Policy Analysis (Centraal Planbureau, CPB) always publishes these models in conjunction with so-called 'variant tables', which show how the economy reacts to shocks in exogenous variables. A great advantage of these models is that they show the main economic relationships for a national economy, and do so for a multiplicity of shocks. The following data for the Netherlands can be derived from the variance analysis (CPB 2011) if there were to be a 1% drop in world trade:

Cumulative difference after		1 year	2 years	4 years	8 years
GDP	%	-0.2	-0.3	-0.3	-0.2
Unemployment	%	0.1	0.2	0.2	0.1
EMU balance	% point	-0.1	-0.2	-0.2	-0.2

When we extrapolate these figures, a 10% decrease in exports comes down to a 2-3% decrease in the national product. However, according to the variance analysis, there are signs of recovery at some point, since the difference is smaller after 8 years.

These figures do not tell the whole story, however. The process of globalisation has accelerated since the middle of the 1990s and products are now increasingly manufactured in international production chains, also referred to as value chains. These chains are the result of the segmentation of production processes due to specialisation and relocation of (parts of) the production process to low-cost production locations. Consequently, products are often

12 CBS, 'CBS: Nederlands product steeds populairder buiten de EU' ('Statistics Netherlands: Dutch products increasingly popular outside the EU'), press release of 5 August 2015, <http://www.cbs.nl/nl-NL/menu/themas/internationale-handel/publicaties/artikelen/archief/2015/nederlands-product-steeds-populairder-buiten-de-eu.htm>

13 Ibid.

14 Vertretungen der Bundesrepublik Deutschland in der Volksrepublik China, 'Deutsch-chinesische Wirtschaftsbeziehungen', <http://www.china.diplo.de/Vertretung/china/de/03-wi/bilateral/2011-12-29-wirtschaft-einfuehrungstext-s.html>

15 German-Dutch Chamber of Commerce, 'Handel met Nederland' ('Trade with the Netherlands'), <http://www.dnhk.org/nl/niederlande/fakten/handel-met-nederland/>

16 Peter van Bergeijk & Marcel Mennen, 'De economische betekenis van nationale veiligheidsrisico's' ('The economic significance of national security risks'), *Tijdschrift voor Veiligheid* 13 (2014) 2, p. 46.

manufactured in more than one country and world trade increasingly consists of trade in semi-finished and intermediate products.¹⁷

Because of the growing internationalisation, less than 30% of Dutch industrial enterprises can still be regarded as 'national'.¹⁸ Although for service providers this proportion is slightly higher, it is still less than 35%.¹⁹ Hence, over 70% of the industrial enterprises and 65% of the service providers are in some way connected with the international production and value chains. Table 1 shows the share of several branches of industry in the Netherlands in terms of value added generated by export and transit.²⁰ Going by this indicator, the most vulnerable sectors are the chemical industry and the food production, tourism and transport sectors.

Table 1 Share per sector in exports on the basis of value added

Chemicals and non-metallic mineral products	18.6%
Food products, beverages and tobacco	12.3%
Wholesale and retail trade; hotels and restaurants	10.0%
Transport and storage, post and telecommunications	9.7%
Business services	6.7%
Agriculture, hunting, forestry and fishing	6.4%
Mining and quarrying	6.0%
Machinery and equipment (not elsewhere classified)	5.0%
Basic metals and fabricated metal products	5.0%
Electrical and optical equipment	4.4%
Transport equipment	3.8%
Finance and insurance	3.5%
Wood, paper, paper products, printing and publishing	3.3%
Other services	1.6%
Manufacturing (not elsewhere classified); recycling	1.2%
Textiles, textile products, leather and footwear	1.0%
Electricity, gas and water supply	0.9%
Construction	0.6%

Source: OECD-WTO Trade in Value Added (TiVA) - May 2015

17 CBS ('Statistics Netherlands'), 2015 *Internationaliseringsmonitor: eerste kwartaal* ('Internationalisation Monitor: Q1').

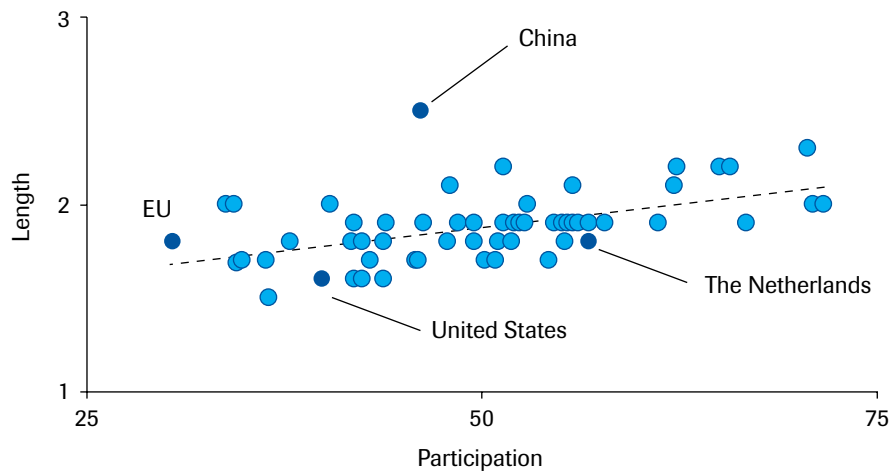
18 A national company is a company which is not foreign-owned and which is not involved in trade with foreign countries.

19 When calculating these figures, we only looked at direct relationships. These relationships are first-order relationships; we did not consider what buyers do with the products or how suppliers come by their products. If we were to do so, we would see that an even larger number of companies are indirectly connected with the rest of the world.

20 This information is more meaningful than the traditionally used export shares of sectors since it takes account of the imports needed for production.

Therefore, even if companies appear to be national, they are often part of international production and value chains. Figure 1 gives a comparative overview of the degree of intensity to which countries take part in international value chains as well as of the length of these chains. This figure shows that the degree to which Dutch companies take part in international value chains of average length is relatively intense. This creates opportunities as well as risks: if one link in the value chain were to break, this could have consequences for the entire chain.

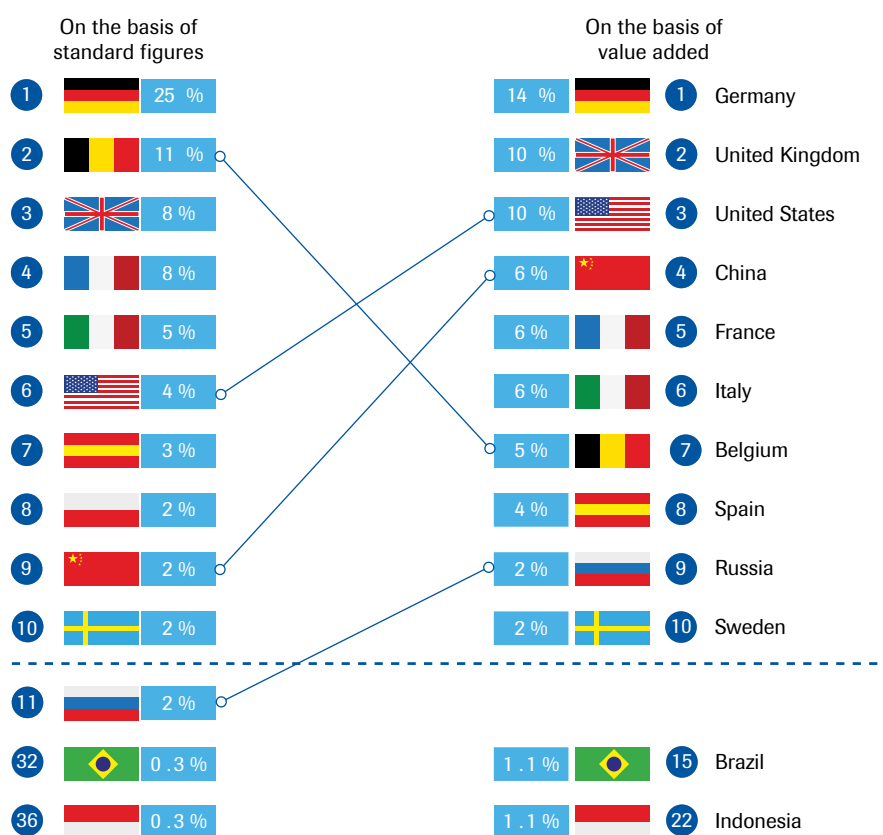
Figure 1 Length of and participation in international value chains (59 countries and regions)



Source: OECD-WTO, Trade in Value Added (TiVA) - May 2015

Because value chains have become increasingly significant, it is important that we not only examine the standard trade figures, but also the added value created in each link of an international value chain. It is, for instance, quite possible that the parts of a Chinese product originate from Malaysia and/or the United States. If we were to ascribe the entire product to China, we would exaggerate the Dutch dependence on China. Figure 2 shows the Netherlands' main trading partners, based on added value. These figures show that the large Western/European industrial countries (i.e. Germany, the United Kingdom and the United States) are still the Netherlands' most lucrative trading partners. Nevertheless, when compared with the standard trade figures, these figures give a more balanced view of the importance of these partners. Secondly, the figures clearly show that the emerging economies are more important than often thought. For instance, taking the traditional trade figures, the share of the BRICS countries is 4%, while on the basis of the added value figures it is approx. 10%. Furthermore, the importance of China as a trading partner is quite evident. Taking the standard trade figures, China ranks 9th, but taking the added value figures, it ranks as the Netherlands' 4th most important trading partner. Russia too ranks among the top ten most important trading partners, while Brazil and Indonesia are moving up the ranking.

Figure 2 Main markets for the Netherlands



Source: ING Economic Bureau, *Nederland Handelsland: Herziening ranglijst belangrijkste exportlanden voor Nederland* ('The Netherlands as a trading nation: Review of the ranking of main export countries for the Netherlands'), 6 November 2014, p. 3.

What does the above mean for the economic susceptibility of the Netherlands? The picture is twofold. On the one hand, the extension and branching out of international value chains increase economic security (thus the international value chains cushioned the drop in world trade in 2008-2009). On the other hand, new risks emerge. In the *first* place, the value creation process in the Netherlands is becoming increasingly dependent on supplies from and sales in other countries. Risk factors come into play at the lower (on the demand side) and at the higher end of the value chain (on the supply side). These risks are global and by definition more difficult to control. Quality problems of foreign suppliers are 'incorporated' into the Dutch product. These problems should be interpreted broadly; for example, they could include the working conditions under which intermediate products are manufactured. Besides, the chains are more susceptible to political risks because of their greater length, a fact which is particularly relevant in this study on the effect of geopolitical developments. These extraterritorial risks in the value chains represent increasing economic susceptibility for Dutch products.

Secondly, in an interdependent world, contamination (physical and psychological) will take place more unexpectedly and at an ever rapid pace. We need global institutions to control these risks, but these institutions are difficult to establish or often do not function properly. *Thirdly*, it will become even more difficult to maintain the Netherlands' advantage in terms

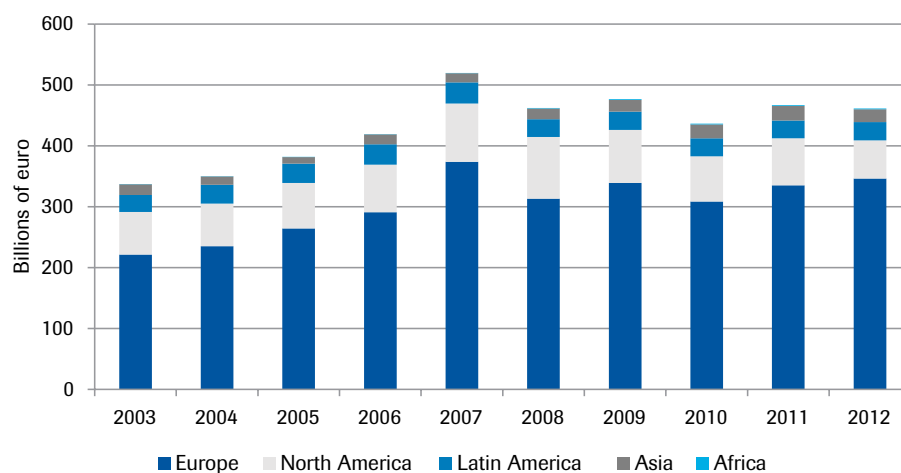
of knowledge and skills. Direct investments are increasingly geared towards acquiring knowledge about production processes and marketing. The use of new technologies has led to an increase in international (industrial) espionage, partly because ever-bigger players and vested interests are involved. It is furthermore not clear how the government should shape representing the ‘Dutch’ interests. For example, is Shell a Dutch or British company? The question arises here whether the Dutch government should take the lead in protecting these interests through economic and traditional diplomacy. Given the continuing trend of internationalisation of Dutch companies, these questions will become even more salient in the future.

Foreign Direct Investment (FDI)

In addition to trade, the Dutch economy is based on foreign direct investment (FDI). The Netherlands ranks as the 9th largest investor in the world and occupies the 16th place in the world ranking as one of the countries to receive the most FDI.²¹ Foreign investments in the Netherlands are more or less evenly distributed over goods (56%) and services (44%), but are largely concentrated in the mining/chemical industry (27%), the financial services sector and the insurance industry (16%) and the agriculture and food sectors (14%).²²

Although direct investments are very important for the Dutch economy, they also entail vulnerabilities and risks. From figure 3, showing the status of FDI *in* the Netherlands, it can be concluded that most FDI still originates from Europe and North America (United States). Although direct investments from Asia are still quite limited, this picture is likely to change in the future. For instance, a recently published report by MERICS (Mercator Institute for China Studies) and the Rhodium Group forecasts that direct investments from China in particular will grow enormously.²³

Figure 3 Foreign direct investment in the Netherlands (2003–2012)



Source: OECD International direct investment database (consulted on 14 August 2015)

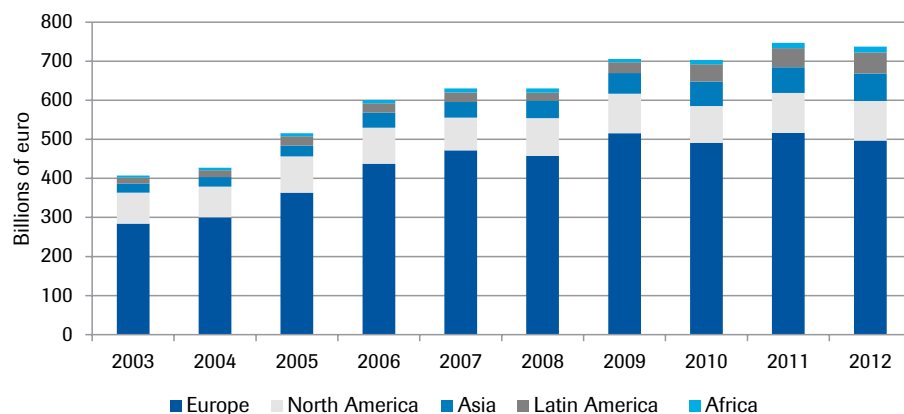
21 UNCTAD, *World Investment Report 2014*, Geneva: UNCTAD, 2014, p. xv.

22 De Nederlandsche Bank, in: Statistics Netherlands, *2013 Internationalisation Monitor*, p. 267.

23 Thilo Hanemann & Mikko Huotari, *Chinese FDI in Europe and Germany: Preparing for a New Era of Chinese Capital*, Berlin: Mercator Institute for China Studies and Rhodium Group, June 2015, p. 10.

Figure 4 shows the FDI *from* the Netherlands. Europe and North America still appear to be the main recipient regions of Dutch FDI, but the other continents are becoming increasingly important in this regard.

Figure 4 Foreign direct investment from the Netherlands (2003–2012)



Source: OECD International direct investment database (consulted on 14 August 2015)

The scale of FDI both in and by the Netherlands reflects its high level of interconnectedness with the global financial and economic system. It is expected that the proportion of direct investments from emerging economies, in particular China, will only increase in the future. This creates certain risks, since these investors gain access to the knowledge and technology of Dutch companies and can exert influence on their strategic operations. The Netherlands is especially susceptible if these investments are made in vital sectors by relatively unknown or state-led actors. It is feared that these parties do business foremost for geopolitical or ideological reasons and less for commercial ones.²⁴

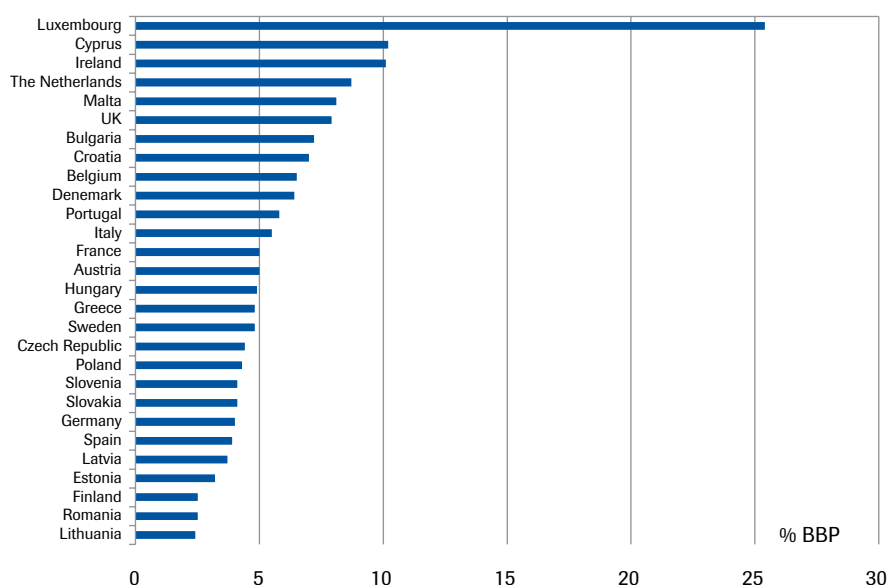
The International Financial System

The Dutch financial sector is of the utmost importance to the Dutch economy. This is evidenced by the share of the gross value added in the GDP. Although the size of the sector has decreased since the crisis, the financial sector still accounted for over 8% in 2013.²⁵ That is relatively high; Figure 5 shows that only in three EU Member States the share of the financial sector in their GDP is higher than in the Netherlands.

24 Letter from the Minister of Economic Affairs to the Lower House, dated 10 June 2014, regarding “Acquiring predominant control of a telecom company with vital telecommunications infrastructure”; letter from the Minister of Security and Justice to the Lower House, dated 10 June 2014, regarding “Policy response to the report of the Economic Security Working Group”.

25 Eurostat, ‘National Accounts and GDP’, May 2015, http://ec.europa.eu/eurostat/statistics-explained/index.php/National_accounts_and_GDP (consulted in July 2015).

Figure 5 Share of the financial sector in EU Member States, 2013



Source: Eurostat, National accounts and GDP

The Dutch economy is highly interconnected with the international financial system, both within Europe and from a global perspective. In recent decades the financial system has significantly changed in nature; it is more strongly interconnected with the economy and society. Moreover, the financial markets are now much more internationally oriented. This makes the Netherlands susceptible to instability and crises on foreign financial markets, as the recent past has clearly shown.

Moreover, as a member of the euro zone, the Netherlands is very much affected by the economies of the other euro countries. By definition, financial problems elsewhere in the euro zone also affect the Dutch economy, as the current Greek crisis has made painfully clear.

From a global perspective too there are developments in the financial and monetary system which make the Netherlands vulnerable. These are closely related to the current shift in power. In addition to markets and investment flows (see above), the stock markets, banks and currencies (e.g. the Chinese yuan) of the emerging countries will consequently play a more important role in the global financial system, making it yet more complex. Moreover, because of the level of global interdependence, instability and financial crises in the emerging countries will easily spread to other parts of the world, including countries where the financial systems are fragile. This may also affect the Netherlands. Furthermore, fluctuations on the global financial market are more difficult to control since there is a lack of adequate *governance* arrangements at this level.

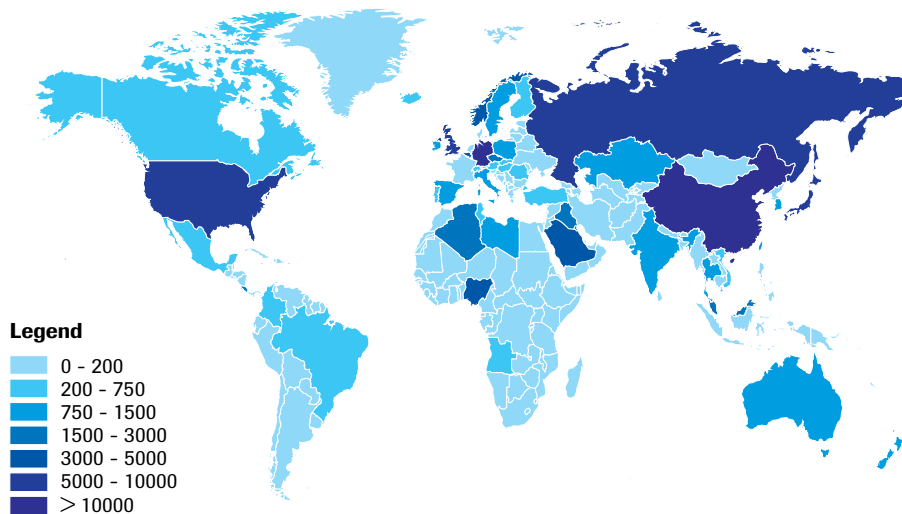
As a final point, where the Western world used to dominate this system with key roles for the US dollar and the Western financial institutions, this position has now come under pressure. The influence of the West (and the Netherlands) on the global financial and monetary system will decline as a result of the emergence of non-Western currencies (such as the Chinese yuan), the establishment of alternative financial institutions or the need to give emerging powers a say in existing institutions, such as the IMF and the World Bank.

Raw Materials and Energy

For a long time now, in particular non-Western countries and regions (e.g. Russia, the Middle East and parts of Africa) have been the main suppliers of raw materials and energy. Here the Netherlands plays a key role as an important hub in the gas and oil flows. For its oil consumption the Netherlands depends for 95% on imports;²⁶ its main suppliers of crude oil are Russia (24.5%), Norway (20.9%), the United Kingdom (12.1%), Nigeria (10.6%) and Saudi Arabia (8.6%).²⁷ As a result of the increased tensions with Russia, the share of Russian oil imports has fallen by over 8% since 2008, largely replaced by imports from Norway (+13%). The Netherlands not only runs a higher risk of economic vulnerability because of its high dependence on imports, but also since Dutch oil consumption is concentrated in specific sectors (the transport sector and the petrochemical industry), where there are few possibilities to switch to other energy sources in the short term. Gas is a different story; thanks to its gas reserves, the Netherlands is a net exporter of natural gas. However, the Netherlands still imports gas, mainly from Norway (42%), Russia (14%) and the United Kingdom (7%).²⁸

At present, the Netherlands' gas production and infrastructure ensure a high level of supply security. However, with regard to the energy issue, in the medium term the trend that the Netherlands is increasingly losing its position as a net gas exporter due to depleting gas reserves and ground instability resulting from the extraction of gas is particularly relevant.

Figure 6 Imported value in millions of euros of 22 strategic raw materials



Source: TNO, Final report critical materials in the Dutch economy - a vulnerability assessment

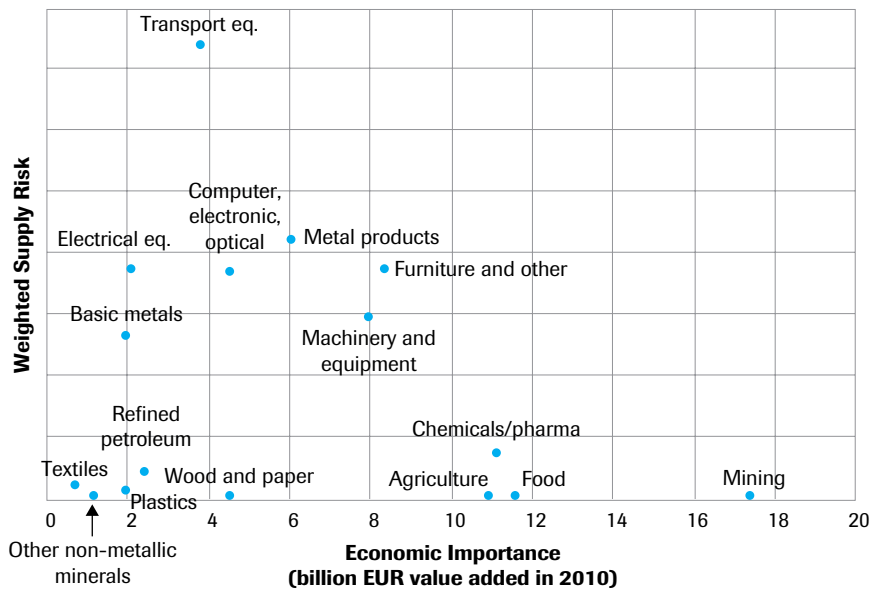
26 OECD/IAE, "Energy Supply Security 2014: The Netherlands", p. 319.

27 CBS, ('Statistics Netherlands'), 'CBS: Noorwegen passeert Rusland als belangrijkste olieleverancier' ('Statistics Netherlands: Norway surpasses Russia as top oil supplier'), 2 June 2015, <http://www.cbs.nl/nl-NL/menu/themas/internationale-handel/publicaties/artikelen/archief/2015/noorwegen-passeert-Russia-als-belangrijkste-olieleverancier.htm>

28 Based on: BP Statistical Review 2015, p. 28; Groupe International des Importateurs de Gaz Naturel Liquéfié (GIIGNL), *The LNG Industry in 2014*, p. 21-22.

Apart from energy sources, we should look at raw materials. In a recently published report on the importance of materials in the Dutch economy, TNO gives an up-to-date overview of Dutch imports of a group of 22 strategic raw materials.²⁹ The report concludes that, although phosphate and platinum-group metals are extremely important for the Dutch economy, a secure supply of rare earth metals, antimony, wolfram and indium is at particular risk.³⁰ Figure 6 shows the relative importance of the trading partners for the supply of these 22 strategic raw materials. The main suppliers are: China (16%), Germany (11%), the United States (7%), Belgium (6%), Costa Rica (6%), the United Kingdom (5%) Russia (5%) and Malaysia (4%). Figure 7 presents a sector overview for the same group of 22 strategic raw materials. The economic importance for the Dutch economy of the sector concerned has been plotted on the x-axis, the supply risk on the y-axis. Geographical concentration, recycling and substitution possibilities are examined according to these criteria. It can be concluded from figure 7 that the main product groups are subject to limited risks. The transport equipment sector is subject to the highest risks. Furniture, metal products, computers, electronic and optical equipment, electric equipment, and basic metals are subject to moderate risks. For agriculture, the food sector and the mining industry, which are important for the Netherlands, the risks are low.

Figure 7 Dutch sectors according to supply risk and importance for the economy



Source: TNO, Final report critical materials in the Dutch economy - a vulnerability assessment

29 This concerns: Antimony, Beryllium, Chromium, Cokes coal, Fluorite, Phosphate, Graphite, Indium, Cobalt, Light Rare Earth Elements, Lithium, Molybdenum, Niobium, Platinum-group Metals, Silicon, Tin, Titanium Dioxide, Vanadium, Wolfram, Silver, Zinc and Heavy Rare Earth Elements.

30 Ton Bastein, Elmer Rietveld & Stephan van Zyl, *Eindrapport Materialen in de Nederlandse Economie – een beoordeling van de kwetsbaarheid* ('Final report critical materials in the Dutch economy – a vulnerability assessment'), Delft: TNO, May 2014, p. 4.

The Internet

Another and relatively new risk has arisen from the huge importance of the Internet for the corporate sector and consumers (see Figure 8: nine out of ten Dutch nationals consult/ use the Internet every day for e-shopping, online banking, internet telephone services and for gathering and providing information). For the corporate sector high quality, high speed and reliable Internet traffic is vitally important. For example, a recent international comparative study conducted by the Netherlands Bureau for Economic Policy Analysis (CPB) examined the susceptibility of the Dutch economy to so-called 'DDoS attacks' by hackers.³¹ Such attacks block important websites unavailable and reduce the speed of data communications. According to consultancy agency Kaspersky, the Netherlands ranks among the top ten countries most affected.³² Targeted are the financial sector, private companies, the government as well as NGOs. In 2011 and 2012 it was relatively quite as far as DDoS attacks are concerned, but the Netherlands was badly hit again in 2013. In April and May 2013, the Dutch government and Dutch banks were the targets of attacks.³³ Kaspersky has estimated that the loss per DDoS attack varies from an average of >EUR 47,000 (for small and medium-sized enterprises) to an average of >EUR 400,000 (for large enterprises).³⁴ What is noteworthy is that the Netherlands is often the country of origin for these attacks (ranking third, after China and the United States), implying a risk for the image of Dutch e-providers. The CPB puts the number of DDoS attacks down to the number of users in the country where the attacks are launched (this does not necessarily have to be the country where the hackers are based) and in the country affected by the attack, as well as to the scale of international trade. This latter aspect, which pertains to the openness of the economy, is particularly relevant since it implies that global shifts of power can result in a mounting number of cyber attacks on this infrastructure, which is becoming increasingly important both socially and economically.

Dutch prosperity has traditionally been built on international trade and multinational activities – in this respect, the Netherlands has passed the point of no return. The resulting dependency on external factors is apparent on several fronts: primarily for exports, as far as access to foreign markets is concerned, but it also applies to the import of raw materials and energy, to attracting foreign investments and to the role of the Netherlands as a logistic hub. As this section shows, the level and manner of international economic dependency differs per economic sector, but generally the Netherlands is susceptible, to a greater or lesser extent (sometimes to a very great extent), to international developments and events on all fronts being discussed. As a result of the ongoing shift of power, the emergence of new players and the extension and branching out of international value chains, it may be expected that the risk of vulnerability will further increase in the years ahead. Moreover, the influence of the Netherlands in the international system will further decline, as a result of which the scope to build up resistance against these vulnerabilities (in collaboration with partners) will come under even greater pressure.

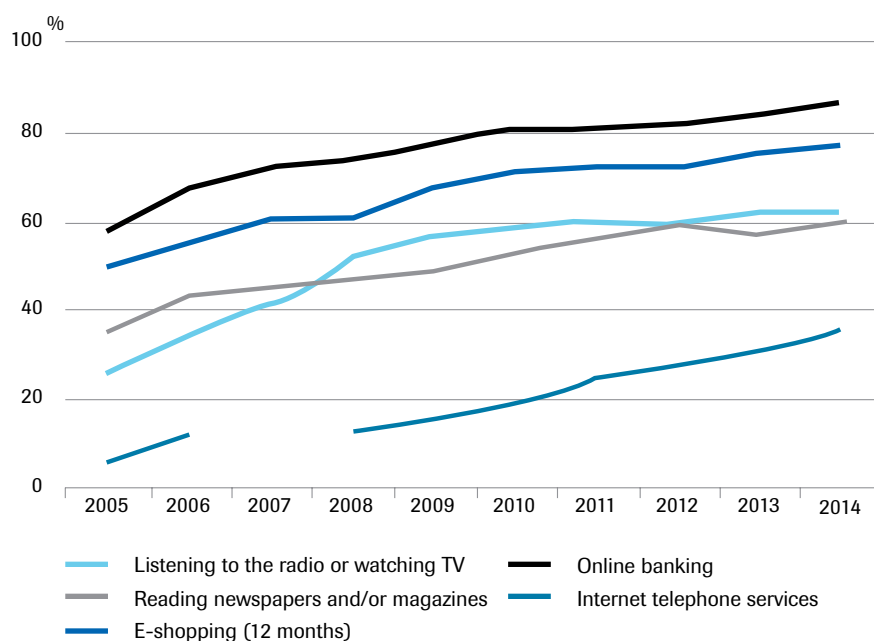
31 B. Overvest & B. Straathof, 'What drives cybercrime? Empirical evidence from DDoS attacks', *CPB Discussion Paper 306*, The Hague: Netherlands Bureau for Economic Policy Analysis (CPB), April 2015.

32 Kaspersky, 'Statistics on Botnet-assisted DDoS Attacks in Q1 2015', April 2015, p. 5.

33 National Cyber Security Centre (NCSC), *Cybersecuritybeeld Nederland: CSBN-4* ('Cyber Security Assessment of the Netherlands (CSAN-4)'), p. 32.

34 Kaspersky, 'Global IT security risks survey 2014 – distributed denial of service (DDoS) attacks', Summary Report, p. 2, <https://press.kaspersky.com/files/2014/11/B2B-International-2014-Survey-DDoS-Summary-Report.pdf>

Figure 8 Internet use in the Netherlands



Source: Statistics Netherlands

Potential Effects of Geopolitical Factors

Against the background of the general susceptibility of the Dutch economy to external influences as outlined in Section 1, this section deals with the question of how it is affected by the global shifts in power and the tensions between the superpowers. These geopolitical processes should be considered within the context of the wider range of international developments that are important for Dutch national security in the years ahead and which in the most recent editions of the *Clingendael Monitor* (2014 and 2015) have been outlined as follows:

- The shift in power resulting from the economic (and political) emergence of China and India will continue, with other countries and regions in their wake. For the years ahead, this implies a further decline in the influence of the West/theEU in a more complex global environment in terms of the number of players and diversity of interests.
- International cooperation and policy coordination will remain under pressure, partly as a result of the diffusion of power and the inability to reform the existing cooperative structures. This will be further exacerbated as a result of the establishment of new cooperative structures and initiatives in addition, or as an alternative, to the existing ones.
- International cooperation has come under further strain as a result of the increased risk of tensions and conflicts within the superpower system. This applies to the relationship between Russia and the US/EU and that between China and the US. Were these tensions to come about, it will also have an effect on the global economic system.
- There is also ongoing and possibly growing instability in regions that are important to the Netherlands and the EU, particularly regarding raw materials and energy. This applies to the MENA region and to other parts of Africa. The conflicts in these regions are not likely

to be brought to an end within the foreseeable future; this also holds true for the tensions between Russia and its neighbours and to their effect on the relationship with the EU.

- While there is still much uncertainty about the relationship with the United Kingdom and about the domestic situation of some EU Member States, including Spain, Italy and France, the EU faces the persistent risk of crises within the euro zone ('Grexit').
- In a more general sense, the Netherlands and its partners (particularly in the context of the EU) will in the years ahead have to take account of a wide range of threats (including crime, cyber (espionage), etc.) with possible economic consequences, the use of economic leverage by third parties and States manifesting themselves strongly in economic affairs, for example in the form of adopting strategic economic policies.

This summary underlines the fact that the current global system is characterised by tensions between the forces of geopolitical rivalry on the one hand and the forces of mutual dependence between parties on the other. Which forces will eventually prevail will to an important extent determine the economic vulnerability of the Netherlands: the force of interdependence and thus cooperation, or the force of geopolitical rivalry and thus conflict. Related to this is the following question: can the superpowers (including the EU) still maintain a certain order, based on shared values and principles, at a time when drastic changes in the global balance of power and the development of a more multipolar global system are taking place? These are essential questions for the Netherlands, aware as it is of its permanent dependency on the outside world.

In reply, the *2015 Clingendael Monitor* points out that the most likely scenario for the next 5 to 10 years will be a *combination* of a more multipolar world order and elements of a multilateral system.³⁵ Cooperation will depend more strongly on the relations between the superpowers – the United States and China in particular – and will increasingly take place on an *ad hoc* basis, i.e. outside the formal frameworks of the existing international organisations. In short, the world order will be characterised by a mix of rivalry and cooperation, to the extent that this cooperation serves the interests of the big players. Against this background, the question of the economic vulnerability of the Netherlands and the possibilities to reduce this vulnerability in collaboration with partners is more pressing.

This section focuses on the geopolitical elements from the above summary. The concept of geopolitics (as applied in this report) refers to the spatial dimension of the power politics of superpowers.³⁶ A geopolitical perspective on international relations therefore focuses on the relationship between political influence and geography, particularly within the context of inter-superpower rivalry. These could be regional as well as the world powers. In the current global system, geopolitics in particular manifests itself more emphatically on two fronts.

Firstly, the current shift from economic and political influence at a global level in favour of a large group of non-Western countries, of which China is the most influential, but among which India, Brazil and several regional powers are also important players, at the expense of the West and Western-oriented Japan. Russia is in a category all of its own. From a long-term perspective, Russian influence, comparable with that of the West/Japan, is on the decline.

35 Jan Rood et al., *Een wereld zonder orde?* ('A world without order?'), *2015 Clingendael Monitor*, February 2015, pp. 25-27.

36 See also http://www.exploringgeopolitics.org/publication_efferink_van_leonhardt_de_definitie_van_geopolitiek_klassieke_franse_kritische/.

However, compared with the years immediately after the demise of the Soviet Union, Russia is once again in a strong position and seeking to establish diplomatic relations with other large, non-Western countries. A consequence of this broad global trend is that, as previously indicated, the Netherlands, as part of the Western world, has less international influence, whilst the Western and standards in the global system are coming under increasing pressure.

Secondly, this concerns the increase in inter-superpower tensions. While the influence of the West (the US, the EU, Japan) is on the decline, relations between a) the US and Japan on the one hand and China on the other, and b) between the US and the EU on the one hand and Russia on the other, have become less stable. Moreover, the geopolitical rivalry between India and China is on the increase and there are latent tensions between China and Russia.³⁷ The EU and China also have conflicting interests and views, which may have a potentially disruptive effect on their relationship. In addition to the flaring up of direct inter-superpower tensions, this increasingly fierce rivalry between various superpowers has an impact on the regional stability in other parts of the world, either in the form of proxy conflicts or as a result of the inability of the international community to take action.

In the follow up to this Section, this geopolitical dimension and its potentially harmful effect on the economic vulnerability of the Netherlands will in the follow-up to this Section be analysed in greater detail from the following three angles:

1. The use of economic influence as *political leverage* in international relations, directly through sanctions or indirectly through threats or manipulation. The current conflict with Russia is an example of the use of economic sanctions by a trading party which is important for the Netherlands. However, we have also seen other examples in the past where a party has used the threat of imposing sanctions to put pressure on the Netherlands to change its behaviour. An important question in the light of the mounting geopolitical tensions and the more significant role of States in world trade is whether this risk has increased and how the Netherlands can protect itself from it.
2. Following on from this lies the vulnerability to *strategic economic policies* pursued by other countries. This is the case when States intervene in world trade to safeguard markets or raw materials in order to reduce their own vulnerability or, by means of take-overs, espionage or other instruments, try to acquire strategic knowledge or gain influence on important social and economic infrastructure. The Netherlands is vulnerable if these actions involve raw materials or suppliers of raw materials and energy vital for the Netherlands, or if this affects (knowledge) sectors and infrastructure which are important for the Dutch economy and society. The manifestation of emerging countries whose governments have a strong tendency to interfere in the economy is another reason to raise the question of vulnerability here.
3. Finally, there are the potentially negative effects of *regional instability* in regions which are important for the Netherlands from an economic point of view. In the first place, the financial and political stability of the EU/euro zone is very important in this regard. Moreover, instability in export markets outside the EU and in regions which are relevant for the Netherlands in terms of the safe supply of raw materials and energy may be

³⁷ Thomas Stephan Eder, *China-Russia Relations in Central Asia: Energy Policy, Beijing's New Assertiveness and 21st Century Geopolitics*, Springer, 2014.

harmful as well. The relationship with Russia, which has deteriorated as a result of the Ukraine crisis, and the increased instability and fragility in the MENA region, particularly in Syria and Iraq, underline the fact that there are increasing risks on this front. However, mounting tensions over the disputed islands in East Asia could also have consequences for the Dutch economic prosperity. A relevant question is how instability in these four regions (the EU, Eastern Europe/Russia, Iraq/Syria and East Asia) affects the vulnerability of the Dutch economy. Incidentally, a distinction should be made here between, on the one hand, risks to the security of supply of, amongst other things, raw materials and energy as a result of political actions (boycotts, sanctions, etc.) and on the other, the physical impossibility of supplying raw materials and energy as a result of instability and conflicts.

Economic Influence as Political Leverage

The first form of vulnerability that will be examined in greater detail in this report results from the use of economic influence as political leverage by foreign players. In international relations, economic influence for political purposes is exerted by imposing, or threatening to impose, (various forms of) sanctions. These sanctions can be directed against States, but also against specific companies or individuals (referred to as *targeted* or *smart sanctions*). Trade and investment can be affected by formal sanctions, such as a boycott, an embargo, an investment freeze or other financial sanctions. In addition to formal sanctions, States may opt for indirectly threatening to impose sanctions in order to exert pressure. Such ambiguous 'sanctions' can result in behavioural change, even if no formal sanctions were imposed. For example, Russia has made frequent use of (the threat of) sanctions in the (recent) past. However, to impose, or to openly and indirectly threaten to impose, economic sanctions is also an important means of exerting international influence for the three main economic players: the European Union, the United States and China.

At an international level, over the past ten years there has been a significant increase in the use, directly or indirectly, of economic sanctions by States and non-state actors. This trend already started in the 1990s, when the collapse of the Soviet Empire put an end to the conflict between the two superpowers; the use of UN sanctions was therefore less effected by the differences of opinion in the UN Security Council. Sanctions have been imposed more often since that time, and the affected trade flows are more extensive than in the past. Because of this trend, the Netherlands is expected to be more frequently involved in economic sanctions, also a target.

The main risks for the Netherlands as a target for sanctions arise from possible sanctions imposed by Russia and China; by Russia due to the tense relations with the EU, and by China due to its economic scale in conjunction with its foreign politics. In the case of Russia, this involves the extension and possible tightening of sanctions resulting from the relationship between Russia and the EU, which deteriorated in 2014. In response to the Russian annexation of the Crimea and interference in the civil war in the Ukraine, the EU (like the US) imposed economic sanctions on Russia in 2014. Moscow then decided on countersanctions, which also affected Dutch exports to Russia. Russia recently threatened to impose a boycott on all flowers from the Netherlands. This probably had to do with the Dutch efforts to set up an international tribunal to try those responsible for the MH17 disaster. The extension and further expansion of the Russian sanctions cannot be ruled out, especially since the EU sanctions are likely to be continued if Russia does not change its position. Moreover, in the event of renewed Russian aggression, further tightening of sanctions cannot be ruled out. Either way, it seems that the relationship between Russia and the West will remain tense in

the years ahead, partly because it is extremely unlikely that Russia will hand back the Crimea to the Ukraine.

It should be borne in mind that the effect of economic sanctions in the relations between Europe and Russia is relatively limited. As a result of globalisation and the emergence of new markets, both the EU Member States and Russia can “more easily” open up new markets and look for suppliers not directly involved in the conflict. Moreover, former Soviet States (including the Baltic States) have become less dependent on Moscow, *inter alia* because of their EU membership. As a result of both factors, the effect of a ‘cold trade war’ on world trade is limited. Although the potential effect of a ‘cold trade war’ is not insignificant, it will therefore be reduced, illustrating that it is not as significant as sometimes assumed.

At the same time, as an open and democratic society, the Netherlands is relatively more vulnerable to foreign economic pressure. By contrast, sanctions directed against autocratically governed countries (e.g. Russia and China), even if these are implemented in the framework of the EU, have a relatively smaller chance of success, in the sense that it is difficult to force behavioural change.³⁸ When assessing sanctions and the threat of them, it has to be borne in mind that, on the one hand, the Russian economy can be hit harder by the West but, on the other hand, that the economic damage resulting from sanctions also has a greater political effect in the Western democracies than in an autocracy such as Russia. Action and reaction therefore balance each other out; in some respect, the chance of success of Russian sanctions are of the same order as US and European sanctions.

In the case of China, relations with the Netherlands and the European Union are not currently strained because of a security crisis or by geopolitical rivalry similar to the conflict with Russia. As a result, and despite conflicts of interest and ideological differences, the economic and diplomatic relations are intense and of a generally positive nature. However, it is relevant to point out here that the Chinese government is not afraid to exert economic pressure on other countries if it believes that its internal security is at stake. Targets would then be the countries which actively or passively provide support to groups which the Chinese government regards as dangerous to the state (*inter alia* dissident political activists and regional activists in Xinjiang and Tibet) or which provide military or diplomatic support to Taiwan (which China regards as a renegade province).

Examples of steps which China has taken against other countries include the sanctions against the Netherlands (1981–1984) in response to the delivery of two submarines to Taiwan³⁹ and the sanctions against Norway in response to the decision of the Norwegian Nobel

38 According to a study by MERICS (Mercator Institute for China Studies) and the Rhodium Group, China is the world’s largest source of direct investments in countries with an autocratic political system. Russia and Singapore are also large investors, although not as large as China, but less autocratic. Saudi Arabia and other Gulf States are just as autocratic, but invest considerably less than China. See Thilo Hanemann & Mikko Huotari, *Chinese FDI in Europe and Germany: Preparing for a New Era of Chinese Capital*, Berlin: Mercator Institute for China Studies and Rhodium Group, June 2015, p. 41.

39 Frans Paul van der Putten, ‘Van semi-kolonie naar economische wereldmacht: China’s toepassing van diplomatieke en economische middelen in de betrekkingen met Nederland sinds het einde van de negentiende eeuw’ (‘From semi-colony to economic world power: China’s use of diplomatic and economic means in relations with the Netherlands since the end of the 19th century’), in: Thomas Lindblad & Alicia Schrikker (eds), *Het Verre Gezicht: Politieke en Culturele Relaties tussen Nederland en Azië, Afrika en Amerika. Opstellen aangeboden aan prof. dr Leonard Blusse* (‘The Far View: Political and Cultural Relations between the Netherlands and Asia, Africa and America. Essays presented to Prof. Leonard Blusse’), Franeker: Van Wijnen, 2011.

committee to award the Nobel Peace Prize to Liu Xiaobo in 2010.⁴⁰ The Chinese sanctions against Norway are still in force. Despite the generally good economic and diplomatic relations, the authoritarian nature of the Chinese political system can sometimes conflict with Dutch support for human rights and access of the Netherlands to activities by human rights activists and critical media. The dominant role of Beijing in the Chinese economy, in combination with China's expanding sphere of economic influence, means that the risk of sanctions or threats on the part of China against the Netherlands cannot be ruled out in the future.⁴¹

Besides restricting access of Dutch companies to the Chinese market, China might take steps that could harm the role of the Netherlands as a logistic hub or the extent of Chinese investments in the Netherlands. It seems that China's ambitious long-term programme for infrastructural projects in Europe, Asia and Africa, launched in 2013 under the banner *One Belt, One Road* (also referred to as the 'Silk Route initiative'), can strengthen China's ability to exert considerable influence on this last point. Furthermore, Chinese direct investments in the Netherlands are likely to increase sharply in the years ahead. According to a report by MERICS (Mercator Institute for China Studies) and the Rhodium Group, the coming years will show a significant increase in Chinese direct investment in the EU. The Netherlands is currently the 6th largest recipient country of Chinese direct investment in the EU.⁴² This means that the Netherlands' susceptibility to Chinese investments will increase.

In addition to formal sanctions imposed by States and supranational institutions, there are informal sanctions initiated by non-profit-making organisations, companies or unorganised groups of activists. Numerous international non-profit-making organisations (such as consumer, environmental, religious and political organisations) have outspoken views on the manufacturing conditions, which they translate into actions directed against companies, international trade and investment. These organisations sometimes specifically call on consumers to boycott specific products and activities (e.g. products from the Occupied Territories); they sometimes only spread information on the products concerned, leaving "the decision" up to consumers (as in the case of Greenpeace-Brent Spar). It is difficult to take countermeasures against such informal sanctions since they are usually not backed by a formal organisation. Consumer boycotts can also go hand in hand with diplomatic pressure or be initiated by governments, and therefore take the place of formal boycotts (e.g. the Chinese boycott of French products in 2008).⁴³

While formal sanctions are more likely to be directed against a country or an economic sector, informal sanctions may be directed against other sectors or against individual companies. That is why the potential threat to Dutch security is greatest in the case of State-initiated sanctions. It should be noted here that formal sanctions can also be directed against specific companies (*smart sanctions*) and that informal sanctions may also cause damage at the national level, depending on the scale, duration and the sectors affected. Consumer boycotts,

40 Benjamin David Baker, 'Soul or Salmon? Norway's Chinese Dilemma', *The Diplomat*, 9 May 2014, <http://thediplomat.com/2014/05/soul-or-salmon-norways-chinese-dilemma/>

41 Frans Paul van der Putten, 'China's randvoorwaarden' ('China's Preconditions'), *Internationale Spectator*, May 2012, pp. 229-230, <http://www.internationalespectator.nl/article/chinas-randvoorwaarden>

42 Thilo Hanemann & Mikko Huotari, *Chinese FDI in Europe and Germany*, pp. 5 and 15.

43 Frans Paul van der Putten, 'China and the Danger of Anti-Western Boycotts', *Clingendael Commentary* 3, 23 April 2008, <http://clingendael.info/cscp/publications/?id=7014>

whether they are coordinated or not, can be directed against a range of products which are considered to be Dutch.⁴⁴

Box 1 presents a few examples of sanctions directed against the Netherlands in connection with the relations between the Netherlands and the Islamic world. These examples show that sanctions against the Netherlands related to geopolitical developments are not new. As early as 1973, the Arab oil-producing countries displayed their power by imposing an oil embargo on the United States and several other countries, including the Netherlands. This oil boycott illustrated the declining power of Western oil companies and Western oil-consuming economies in favour of Saudi Arabia and other Arab oil-producing countries. Moreover, the immediate reason for the boycott was a war in the Middle East. Box 1 also shows that sanctions against the Netherlands are not always directly related to geopolitical factors, as in the cases of *Fitna* and the PVV's (Party for Freedom) sticker campaign.

Box 1 Relations with the Islamic World

In 1973, tensions between the Netherlands and the Arab world resulted in formal, inter-state sanctions against the Netherlands in the form of *inter alia* an oil boycott. The United States and several other countries were also targeted by an oil boycott.⁴⁵ These sanctions should be seen within the wider context of the strategic economic policies of the Arab oil-producing countries (OPEC) at the time. The price increases and volume restrictions also formed part of these policies.

The Arab OPEC countries used the oil boycott as a political weapon against the Netherlands because the Netherlands had provided political and military support to Israel during the 1973 October War.⁴⁶ Although the Arab countries maintained that the embargo was prompted by the Netherlands' pro-Israeli position, the question remains whether the embargo was in fact solely a reaction to Dutch Middle East policy. The boycott followed a period of mounting tensions on the international oil market, where Arab oil-producing countries increasingly opposed the dominant position of the West. With Shell and the Port of Rotterdam, the Netherlands was an important player on the oil market. As a result, the Dutch government received signals that an embargo was imminent long before the October War.⁴⁷ It is therefore likely that the embargo was partly prompted by increased tensions in the international oil sector.⁴⁸

44 It is important to establish that internationally active companies can take a position which differs from the position of the Dutch government, even if they are based in the Netherlands. In a liberal, market-oriented economy such as the Dutch economy, companies are free to take a position that is contrary to the public interest. The government can discourage such activities or try to steer them through persuasion, but real instruments are lacking.

45 In addition to the oil boycott, the sanctions against the Netherlands consisted of a boycott of KLM by Syria and Jordan and the nationalisation by Iraq of the Dutch part of Shell's shareholdings in the Iraqi *Basrah Petroleum Company*.

46 Duco Hellema, Cees Wiebes & Toby Witte, *The Netherlands and the Oil Crisis: Business as Usual*, Amsterdam: Amsterdam University Press, 2004, p. 34.

47 Ibid, p. 72.

48 Ibid.

The oil boycott threatened 40% of the total energy supply of the Netherlands.⁴⁹ Moreover, the position of the Port of Rotterdam was at stake, and it was feared that the major oil companies would pull out of the Netherlands. However, the boycott proved not very effective, largely due to the decision by oil companies to divide the scarce oil between European countries. Also, with a view to expected price increases, companies had already built up stocks before the boycott. Paradoxically, during the entire crisis the oil reserves in Rotterdam were higher than in previous years.⁵⁰ Furthermore, the embargo was not always complied with equally strictly, and the Netherlands could count on the non-Arab oil producers for oil. The supply of oil to Rotterdam therefore quickly resumed.

As part of their strategic economic policies, the Arab OPEC countries also decided to increase oil prices by 70% and reduce oil production by 5% each month. The resulting price increases did not fail to have a significant effect on the Dutch economy: the post-war years of economic growth came to an end and the increase in the oil price produced high inflation. This resulted in a period of stagflation and a decline in the Netherlands' competitive position.⁵¹

Unlike the formal, inter-state sanctions of the 1970s, the religious theme plays a prominent role in the more recent diplomatic relations with the Arab world. In addition, the range of modern means of diplomatic leverage has widened; apart from formal sanctions, also informal sanctions now constitute a threat.

The release of the film *Fitna* in 2008 by Geert Wilders, a member of the Lower House for the PVV, led to fierce reactions in the Netherlands and abroad. Several countries threatened to impose diplomatic and economic sanctions on the Netherlands. These international reactions should be seen within the wider context of anti-Islamic manifestations in the Netherlands, including the cartoons of the cartoonist Nekschot and the anti-Islamic film of Ehsan Jami (a former councillor of the municipality of Leidschendam-Voorburg). Threats to impose sanctions came from both state actors (such as Iran) and non-state actors (such as Arab clerics and the Jordanian media).

Because of the fierce international reactions, the Dutch government intensified the diplomatic talks with the Islamic countries. The Minister of Foreign Affairs Verhagen placed a notice in Arab media to "keep your head cool but keep the relations warm" and called on Islamic countries to ensure that Dutch nationals and companies would not suffer any negative effects from the film.⁵² Employers' organisation VNO-NCW and the Dutch companies Zwanenberg Food Group and Friesland Foods also distanced themselves from *Fitna* in Arab media. Partly due to these efforts, the negative consequences of *Fitna* were not as serious as expected.

49 Ibid., p. 99.

50 'Olie zat tijdens de oliecrisis' ('Plenty of oil during the oil crisis'), *De Volkskrant*, 13 November 1998, <http://www.volkskrant.nl/dossier-archief/olie-zat-tijdens-de-oliecrisis-arabische-landen-straften-met-embargo-vooral-zichzelf~a490766/>

51 CBS ('Statistics Netherlands'), *De Nederlandse Economie 2010* ('The Dutch Economy 2010'), p. 221.

52 'Verhagen bezorgd over gevolgen film Jami' ('Verhagen concerned about the effects of the Jami film'), *De Volkskrant*, 9 December 2008.

The cancellation of the state visit by the Indonesian President Yudhoyono in 2010 can also be classified as an informal sanction by a trading partner which is important for the Netherlands. Although Yudhoyono made it formally known that the cancellation was a result of interlocutory proceedings which the South Moluccan government in exile (RMS) had instituted against him in the Netherlands, it is plausible that the Rutte I government (with the PVV providing Parliamentary support from outside the governing coalition) and the anti-Islamic statements by Geert Wilders were part of the reason for the cancellation.⁵³ The Indonesian ambassador in the Netherlands, Junus Habibie, had severely criticised the views of Geert Wilders prior to the state visit. Habibie had also announced that Yudhoyono's state visit would be cancelled if the PVV were to be included in the new government. The cancellation of the state visit harmed the Netherlands since the President's meeting with representatives of the Dutch corporate sector did not take place. Furthermore, a special cooperation treaty between the Netherlands and Indonesia was not signed.

Towards the end of 2013, the Dutch-Saudi Arabian relations came under pressure as a result of another campaign by PVV leader Wilders, whereby anti-Islamic stickers were distributed. The Dutch government distanced itself from the campaign but still received signals that it could result in a boycott of Dutch companies. The Hague subsequently intensified its diplomatic talks with Saudi Arabia. The Director-General for Political Affairs of the Ministry of Foreign Affairs paid a visit to the Saudi capital of Riyadh. The Minister of Foreign Affairs Timmermans talked to his Saudi Arabian counterpart about the matter on the fringes of international conferences in London and Athens at the time.

For a long time it remained unclear whether Saudi Arabia had actually imposed a boycott. The Hague never received confirmation from the Saudi Arabian government. However, several Dutch companies, including interior designer Maas and lubricant manufacturer LubriDutch, stated they had experienced problems securing new contracts.⁵⁴ The diplomatic efforts of the Netherlands seemed to have paid off by the end of June. The employers' organisation VNO-NCW declared that Dutch companies were no longer suffering from the prospective boycott.⁵⁵

In addition to the possibility of the Netherlands becoming a direct target of economic sanctions, there is the risk that the Netherlands will be indirectly affected by sanctions between other countries. In the past, Dutch companies have been affected by American and European sanctions against countries such as Cuba, Iraq, Iran and Russia. Any prospective sanctions by the US against Chinese targets (and *vice versa*) could have far-reaching consequences for Dutch business interests. Although, given their highly significant economic

53 'Yudhoyono annuleerde om Wilders' ('Yudhoyono cancelled because of Wilders'), *Nederlands Dagblad*, 9 October 2010.

54 'Onduidelijkheid over Saoedische sancties' ('Uncertainty about Saudi sanctions'), *Het Financieel Dagblad*, 19 June 2014, <http://fd.nl/frontpage/economie-politiek/89089/onduidelijkheid-over-saoedische-sancties>.

55 'Gevaar Saoedische boycott ebt weg' ('Danger of a Saudi boycott fading away'), *Het Financieel Dagblad*, 25 June 2014, <https://fd.nl/frontpage/ondernemen/entrepreneur/wereldveroveraars/90541/gevaar-saoedische-boycott-ebt-weg>.

interdependence, the risk of economic sanctions between the US and China is limited, the risk of an unintended escalation of the mounting Sino-American tensions will increase as their geopolitical rivalry intensifies, especially in East Asia, but also in cyberspace. Hence any mutual sanctions that might be imposed between the US and China would probably be very harmful to Dutch economic interests.

Another possibility is the exchange of economic sanctions between China and Japan; these could also harm the Netherlands, although not on the same scale as Sino-American sanctions would. The recent 'cold trade war' between Russia and the US could also intensify, irrespective of whether the EU and Russia have applied sanctions. This would probably affect the Netherlands economically.

Going by recent events, the Netherlands must, over the next 5 to 10 years, take account of the greater risk of sanctions against it (particularly at EU level) or against other countries which might also affect its economic interests. In this regard the relevance of geopolitical factors mainly lies in the risk of consequential damage resulting from tensions and sanctions between superpowers. However, because of the international process of power shifting and the ensuing possibility of tensions, the risk of sanctions and countersanctions being imposed will increase; this risk also applies to the emerging economies.

Strategic Economic Policies of other States

The second form of economic vulnerability of the Netherlands concerns the potentially harmful effects of the strategic economic policies of other States. This concerns policies aimed at securing national economic interests through anticompetitive activities, such as state aid, buying up raw materials and economic espionage.⁵⁶ The likelihood that countries will opt for a strategic economic policy increases as global relationships are more controlled by geopolitical forces and there is less cooperation in multilateral frameworks aimed at free trade and a *level playing field*. The *2015 Monitor* ('A world without order?') shows that at the present time we cannot rule out a (further) progression towards a more geopolitical global system.

This largely concerns the positions and policies of the major players in the global economy, since a strategic economic policy at an individual level is not feasible for most States. They are too small to influence the global market. Small and medium-sized economies will therefore benefit from the enforceable rules within multilateral frameworks: a *rule-based system*. This does not apply to the largest countries, which can help set the conditions on the global market and are therefore able to implement a national strategic economic policy.

In the next 5 to 10 years, this concerns in particular the United States, China and the European Union. Although the BRICS countries increasingly operate as a group, they mostly do so on an *ad hoc* basis. Moreover, China is by far the largest economy in this group. The three economic superpowers (the US, China and the EU) will opt for regulations and conflict settlement through multilateral organisations if this serves their interests but, if not, they will try to safeguard their interests in other ways.

56 This also covers so-called 'beggar-thy-neighbour' policies, whereby countries try to represent their economic interests by means of, amongst other things, competitive devaluations. This type of 'strategic economic policy' will not be considered here.

One way is to create alternatives for the global multilateral system. Partly as a result of the diffusion of power and the inability of the current multilateral institutions to adapt to this situation, emerging economies increasingly opt for alternative forms of cooperation. The BRICS development bank (*New Development Bank*) is a recent example.⁵⁷ However, it would be naive to think that the multilateral system is undermined solely by the emerging economies. Also the United States sometimes pursues a policy which is not in the interest of a properly functioning global system. This may be illustrated by Washington not ratifying the new voting proportions in the International Monetary Fund or generally opting to deal with global environmental problems on a bilateral basis.

A second way is to provide targeted support to companies and to protect the domestic market. For instance, China pursues a policy whereby state aid for certain Chinese companies is combined with limited access for foreign companies to the Chinese market.⁵⁸ Given the large scale of the Chinese economy, the resulting competitive advantages for Chinese companies constitute a major challenge for Dutch and other non-Chinese companies, a challenge which is greater than in many other countries.

In this context, attempts by countries to secure access to or supply of raw materials receive a lot of attention. This attention is directed at the Chinese policy, which consists of three stages: commercial cooperation, political influence and security of supply. As an extension of its own model of development, China supports a number of special economic zones in neighbouring countries (Russia, Pakistan, Vietnam) and in countries in Africa, Asia and Latin America. The previously mentioned *One Belt, One Road* initiative also serves as an example of strategic economic policy by China. As part of this initiative, China has invested in a large number of infrastructural projects in Central Asia, South-East Asia, the Middle East, East Africa and Europe. The *One Belt, One Road* initiative provides a framework for China's long-term strategic interests, including securing access to China's export markets, access to raw materials and the ability to open up new markets.⁵⁹

This is largely prompted by the rapidly increased dependence of the Chinese economy on the import of oil and raw materials. For instance, there has been a spectacular increase in imports of oil and minerals into China. In 2013, China imported 64% of all internationally traded iron ore,⁶⁰ In comparison, the United States imported less than 2%. Moreover, in April 2015 China surpassed the United States as the biggest importer of crude oil (see Figure 9).⁶¹ Furthermore, China for many years has been the biggest importer of minerals such as aluminium, copper and zinc, although it should be pointed out that, at a more aggregated level (i.e. including processed raw materials), this level is still relatively low. Here, US demand for imports is still dominant. However, in a number of regions, China at this level is already a player on a par with Europe.

Such a strategic policy is not limited to China. A good example is the shale gas revolution in the United States. Thanks to new and innovative techniques (*fracking*), the US has gained access to large amounts of shale gas. As a result, energy prices have dropped considerably

57 NDB, 'The New Development Bank BRICS', <http://ndbbrics.org/>

58 Thilo Hanemann & Mikko Huotari, *Chinese FDI in Europe and Germany*, pp. 34-38.

59 Frans-Paul van der Putten & Minke Meijnders, 'China, Europe and the Maritime Silk Road', The Hague: Clingendael Institute, March 2015, p. 29.

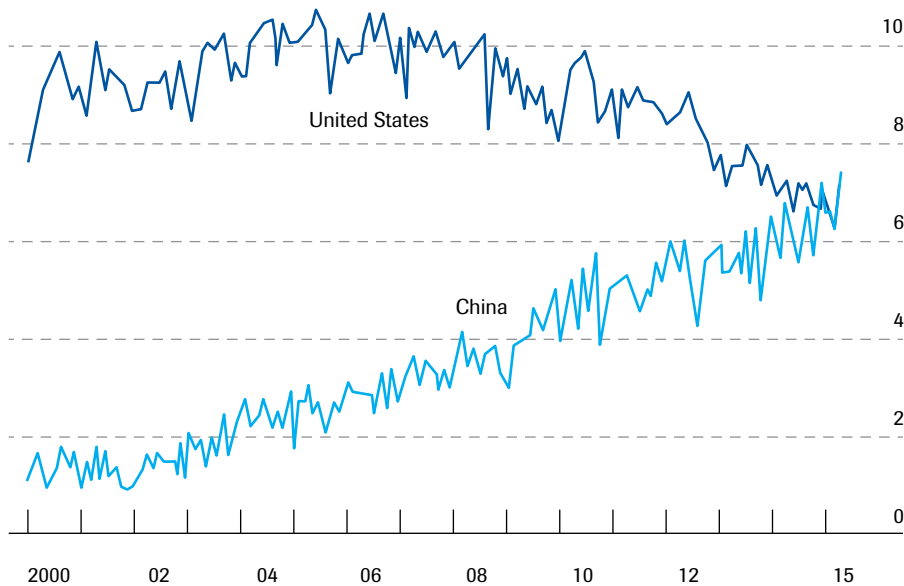
60 <http://www.statista.com/statistics/270008/top-importing-countries-of-iron-ore/>

61 <http://www.ft.com/cms/s/0/342b3a2e-f5a7-11e4-bc6d-00144feab7de.html#axzz3f3WA6bIF>

and the US is now one of the largest oil and gas producers in the world. An important driving force behind this revolution is America's wish to become independent of energy imports in the longer term. The effect of shale gas can already be seen in the level of America's dependence on oil: the import of oil has decreased from 60% in 2005 to 27% in 2014.⁶² These shifts, if they were to continue, will have geopolitical consequences for the future since the US will have less strategic interest in, for example, the Middle East. However, the EU's efforts to reduce its energy dependency on Russia, *inter alia* by making greater use of renewable energy, are also made for strategic reasons.

These examples show that, in particular with regard to energy and raw materials, a combination of dependence and scarcity in relation to geopolitics can be a catalyst for a strategic economic policy. In this field of influence, it is very important that the Netherlands secures the supply of strategic goods by diplomatic and economic means. In addition, this field of influence will to a considerable extent be conditioned by the question of whether energy and raw materials become increasingly scarce in the medium term.

Figure 9 Chinese and US oil imports



Source: Financial Times, May 2015, <http://www.ft.com/cms/s/0/342b3a2e-f5a7-11e4-bc6d-00144feab7de.html#axzz3f3WA6bIF>

This not a matter of raw materials only. In a globalising world, *knowledge* in particular has become increasingly important. Knowledge creates an important competitive advantage, albeit of a temporary nature. The temporary nature of the advantage of knowledge will increasingly constitute a vulnerability. Because of the great importance of knowledge, increasing efforts are being made to acquire knowledge, both legally and illegally (espionage).

62 U.S. Energy Information Administration, 'How dependent are we on foreign oil?', 10 May 2013, http://www.eia.gov/energy_in_brief/article/foreign_oil_dependence.cfm en U.S.; U.S. Energy Information Administration, 'How much oil consumed by the United States comes from foreign sources?', 12 March 2015, <http://www.eia.gov/tools/faqs/faq.cfm?id=32&t=6>

Many students from emerging economies go to universities in the West. Western knowledge producers are persuaded to set up expertise centres and the foreign direct investments of emerging economies in the industrialised countries are no longer driven by market access but by the desire to learn more about management, marketing, production processes and innovation. There is also an increase in illegal copycat behaviour and economic espionage.

Its status as a high-quality, knowledge-based economy makes the Netherlands an interesting target for economic espionage. In addition, the ongoing digitisation process makes the Dutch economy vulnerable to digital threats. Although traditional espionage tactics have lost none of their importance, digital espionage in particular has sharply increased over the past few years.⁶³ Because of low costs and high returns, cyber-attacks constitute an attractive alternative for traditional espionage methods. As appears from the 2014 annual report of the General Intelligence and Security Service (Algemene Inlichtingen- en Veiligheidsdienst, AIVD), States pose the biggest threat as far as digital espionage is concerned. The *2013 Cyber Security Assessment* identified China, Russia, Iran and Syria as the main actors (see Box 2). While the Iranian and Syrian intelligence services focus on disrupting and destabilising political targets, China and, increasingly, Russia are also active in the field of economic espionage. It should be pointed out here that the US too is guilty of economic espionage; for instance, both the aircraft manufacturer Airbus and the European Commission turned out to be targets of espionage by the American intelligence service NSA.

Economic espionage constitutes a threat to the economic security of the Netherlands. Although foreign intelligence services mainly focus on military technology, there is also a significant increase in espionage activities directed at the Dutch corporate sector, in particular the so-called 'top sectors' (the maritime, agriculture, high-tech, horticultural and energy) and the chemical industry.⁶⁴ In the past, Dutch companies (e.g. Philips and ASML) have fallen victim to economic espionage. The Dutch economy suffers damage from the theft of intellectual property and the undermining of its negotiating position during tendering procedures, contract negotiations, mergers and take-overs. It is difficult to assess the extent of the damage. For the Netherlands, the damage resulting from economic espionage (by state and non-state actors) is estimated at EUR 8.8b. per year.⁶⁵

Because of the power shifting process, which will result in increasing tensions, and of the manifestation of emerging countries, characterised by a high level of government interference, the risk of economic espionage is likely to remain high, and may even increase.

63 See the 2013 and 2014 Cyber Security Assessments.

64 AIVD ('General Intelligence and Security Service'), *2014 Annual Report*, p. 24.

65 'Crime kost Nederland jaarlijks 8 miljard' ('Cybercrime costs the Netherlands 8b. per year'), *De Volkskrant*, 10 June 2014, <http://www.volkskrant.nl/recensies/cybercrime-kost-nederland-jaarlijks-8-miljard-a3669671/>

Box 2 Economic Espionage⁶⁶**China**

Western media often associate China with state-level economic espionage.⁶⁷ According to a US study from 2013, *Chinese Industrial Espionage: Technology Acquisition and Military Modernisation*, China is unique in terms of the extent to which economic espionage is rooted in government policy and the frequency with which intelligence services are brought into action to spy for economic gain. This study claims that the Chinese government is not only active in the field of economic espionage, but above all also systematically encourages and facilitates companies and scientists to acquire knowledge, either legally or illegally, from foreign sources.⁶⁸

According to the General Intelligence and Security Service of the Netherlands (Algemene Inlichtingen- en Veiligheidsdienst, AIVD), China's economic espionage activities are largely focused on obtaining information on scientific and technological developments and intended investments of both the corporate sector and the government.⁶⁹ On the one hand, the high level of interconnectedness between the Chinese government and the corporate sector makes it difficult to determine the extent to which economic espionage is controlled by the government. On the other hand, this interconnectedness makes it more plausible that the Chinese government plays an important role in this. Beijing is increasingly often openly accused of economic espionage, in particular by Washington. The American intelligence services and various cyber-consultancies have traced large-scale attacks aimed at acquiring intellectual property back to the Chinese army.⁷⁰ There is even talk of "the biggest loss of intellectual property to China in world history".⁷¹ In May 2014, the American authorities charged five Chinese army officers with economic espionage by means of cyber-attacks on US-based companies.⁷²

Russia

While Russian espionage activities used to be largely focused on obtaining military strategic and political intelligence, Moscow is now increasingly active in the field of economic espionage. For instance, it was recently made known that a Russian physicist, a former employee of the Eindhoven University of Technology, is suspected

66 In contrast to espionage for political and military purposes, economic espionage concerns the collection by a State of secret information on a foreign company or individual and the passing on of this information to public or private companies. Economic espionage differs from industrial or corporate espionage, whereby private companies spy on other companies.

67 See i.a.: AIVD ('General Intelligence and Security Service'), *2011 Annual Report* and 2013, and 2014 Cyber Security Assessments.

68 William C. Hannas, James G. Mulvenon & Anna B. Puglisi, *Chinese Industrial Espionage: Technology Acquisition and Military Modernisation*, New York: Routledge, 2013, p. 14.

69 AIVD ('General Intelligence and Security Service'), *2011 Annual Report*.

70 See Mandiant, 'APT 1: Exposing One of China's Cyber Espionage Units', Mandiant Intelligence Center Report, February 2013; CrowdStrike Global Intelligence Team, *Intelligence Rapport: Putter Panda*, June 2014; and 'In Cyberspy vs. Cyberspy, China has the edge', Reuters, 14 April 2011.

71 Sam Jones, 'West eyes Dr. Strangelove tactics in cyber wars', *Financial Times*, 29 July 2015.

72 <http://www.justice.gov/opa/pr/us-charges-five-chinese-military-hackers-cyber-espionage-against-us-corporations-and-labor>.

of having spied for the Russian secret service.⁷³ Previously, the General Intelligence and Security Service reported in its *2014 Annual Report* that Russia was involved in the collection of political, military and scientific intelligence in the Netherlands.⁷⁴ Mikhail Fradkov, the director of Russia's Foreign Intelligence Service (SVR), stated that it is the role of the SVR to support Russia's technological and scientific advancement.⁷⁵ President Putin also called on the SVR "to actively protect the economic interests of [Russian] companies".⁷⁶ Economic espionage activities conducted by Russia are largely focused on the defence industry, the gas and oil industry, the banking sector and telecom companies.⁷⁷

Because Russian APT groups⁷⁸ have advanced technology at their disposal and make use of encryption, their attacks often remain undetected for a long time.⁷⁹ In 2014, the APT group *Energetic Bear* carried out the first prolonged cyber-attack, which was linked to the Russian government by cyber consultancies.⁸⁰ *Energetic Bear* largely focused on the Western energy sector, as well as production and construction companies, the IT sector, governments, research institutes, the defence industry and medical care institutions. This attack thus shows that the range of targets has widened; next to political and military strategic targets, economic targets are included. It therefore constitutes the first case of Russian economic espionage. After the *Energetic Bear* attack, other APT attacks on economic targets were also linked to the Russian government.⁸¹ The attacks are/were largely focused on the financial and strategic data of companies, enabling the APT groups to undermine the negotiating position of (Dutch) companies during mergers, take-overs and contract negotiations.

Although the SVR increasingly makes use of cyber intelligence, more traditional types of espionage are still an important source of information. Secret agents are mostly used for this purpose. Three Russian secret agents from the SVR's economic division were recently arrested in the United States for having gathered information on prospective American sanctions against Russia and on developments in the field of renewable energy.⁸²

73 'Inlichtingendiensten verdenken wetenschapper' ('Intelligence services suspect scientist'), *NRC Handelsblad*, 29 July 2015.

74 AIVD ('General Intelligence and Security Service'), *2014 Annual Report*, pp. 29-30.

75 Office of the National Counterintelligence Executive, 'Foreign Spies Stealing U.S. Economic Secrets in Cyberspace: Report to Congress on Foreign Economic Collection and Industrial Espionage, 2009-2011', October 2011.

76 Ibid.

77 *2013 Cyber Security Assessment*, p. 21.

78 APT stands for *Advanced Persistent Threat* and is used to indicate a prolonged attack (supported) by a state actor.

79 James Andrew Lewis, *Cyber Threat and Response: Combating Advanced Attacks and Cyber Espionage*, Centre for Strategic and International Studies, March 2014.

80 See CrowdStrike, *Global Threat Report: 2013 in review*; and Symantec, *Dragonfly: Western Energy Companies Under Sabotage Threat*, 30 June 2014.

81 'West accuses Russia of cyber-warfare', *IHS Jane's Intelligence Review*, 28 December 2014.

82 'Spy vs. Nonspy in Putin's Russia', *The New York Times*, 30 January 2015.

Instability in regions which are important for the Dutch economy

The *2015 Monitor* identified three *hot spots* characterised by mounting tensions or violent conflicts: East Asia, the MENA region and Eastern Europe. Instability in these three regions can affect the economy of the Netherlands in different ways.

However, the context described above which is of relevance to the Netherlands revealed that, as an economic entity, Europe (the EU/euro zone) is still the most important for the Netherlands. Since the start of the financial-economic and debt crisis, a series of measures have been taken to strengthen the euro zone in particular and to prevent a recurrence of the crisis. Nevertheless, the economic recovery is fragile and several euro countries are still plagued by major economic problems, as far as debts and budget deficits, and the failure to carry out necessary economic reforms are concerned. All this suggests that fragility in the euro zone will have to be taken into account in the years ahead. Besides the persistent risk of a 'Grexit', this largely relates to the risk that, as in Greece, the austerity and reform programmes imposed by the euro zone will also result in growing opposition to the euro in other euro countries, in particular France, Italy and Spain. This will put an even greater strain on the level of cohesion within the EU, in particular on the north-south axis. This risk is all the more acute now that national elections are about to take place in, amongst others, Spain, and Eurocritical parties in the southern Member States have gained significantly in popularity. This uncertainty about the EU's future is further increased by the referendum on British membership of the EU, which will be held in June 2017.

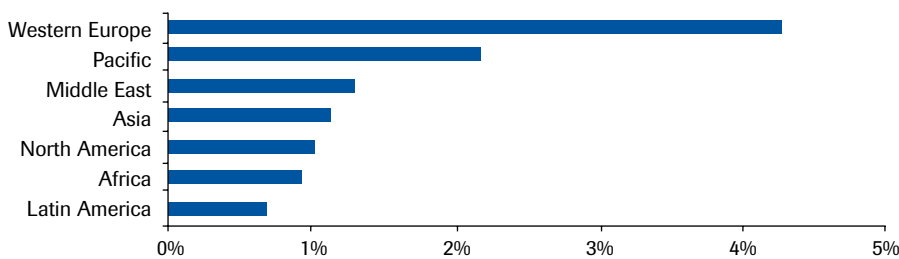
Uncertainty as to the future of the EU/euro zone will have a negative effect on the real economy and, as a result, harm the Netherlands. Moreover, as research has shown, if Britain were to leave the EU, the Netherlands would be particularly affected. It may be clear that the continuation of the problems in the EU/euro zone could also result in the further weakening of the EU's global position.

Further removed from the heart of Europe, there are two regions on its flanks, which are relevant for their own unique reasons. Economic development in the MENA region has come to a standstill and political instability there is extremely great. The conflicts are concentrated in Iraq and Syria, with a civil war (Syria) on the one hand and, with the rise of Islamic State (IS), a disintegration of existing States (Syria and Iraq) on the other. However, the political instability in Libya, Yemen, Mali and Nigeria and the attacks in Tunisia all show that large parts of the Middle East, North Africa, Sub-Saharan and West Africa have become victims of conflict, radicalisation and fragility. As a result, security of supply of important raw materials is already at risk. We have also seen extensive migration flows and there is the risk that these conflicts will *spill over* in the form of terrorism and crime. Moreover, it cannot be ruled out that the instability will spread further, partly as a result of the increasing involvement of external parties. If this were to happen, particularly if the domestic stability in Saudi Arabia and Egypt were to be threatened or the violence in Syria and Iraq were to develop into a region-wide conflict, this could have far-reaching consequences for energy supply security (Saudi Arabia and the Gulf States) and safe passage (Strait of Hormuz, Suez Canal, piracy); these are consequences which will also affect the Netherlands and its major petrochemical industry.

To the east of the EU, the deteriorating relationship with Russia plays a role. The annexation by Russia of the Crimea and the Russian-supported actions of the separatists in the Ukraine put a heavy strain on relations between the EU/US and Russia. Their economic relations in particular were intensified considerably after the Cold War, and, besides that, the energy

relationship with Russia is particularly important, not only for a number of EU Member States, but also for the Netherlands as a 'hub' for Russian gas and a transit location for Russian oil. It is feared that Russia will use Europe's energy dependency as political leverage or as a means to play EU Member States off against each other. As previously indicated, the economic effects of the current conflict, in particular the mutual economic sanctions, have been limited to date. For instance, in its August 2014 estimate, the Netherlands Bureau for Economic Policy Analysis (CPB) estimated these effects at 0.5 per cent of economic growth.⁸³ However, if the conflict were to escalate further (which cannot be ruled out), the effects will be more serious (see Figure 10). In this respect, some observers fear a return to the type of relations during the Cold War, when political tensions limited the scale of global production by 3.5 per cent.⁸⁴

Figure 10 Effect of the cold trade war scenario (trade potential in % of the GDP)



Source: P.A.G. van Bergeijk, 'The return of the Cold Trade War?', Voxeu.org, 6 November 2014

In East Asia, the playing field is largely determined by geopolitics; in particular, the risk exists of conflict in the South China Sea and East China Sea. In both cases the relationship between China and the United States plays a role. In the East China Sea there is also the risk of a conflict between China and Japan. In addition, risks exist of conflicts in the relationship between China and Taiwan and between North and South Korea. The majority of the main disputes and conflicts in East Asia results from the aftermath of the Second World War. Because of the Cold War, these issues were not resolved at the time and therefore continue to undermine the stability in the region. Moreover, increasing rivalry between the US and China as global powers manifests itself primarily in this region. It is largely through their influence in East Asia that the Americans are trying to curb and channel China's rise. In response to China's growing international influence, the US continues to exert yet more counter pressure. It seems likely that this process will continue in the years ahead. Such tensions threaten international cooperation at a global level between major economic players such as the US, China and Japan. From an economic perspective, the shipping routes through the region and the important role which Asia plays in the various links of the international value chains constitute substantial vulnerabilities for countries such as the Netherlands.

83 Paul Veenendaal, Kasia Grabska, Debby Lanser, Marco Ligthart & Joris de Wind, *Onzekerheidsvarianten bij verdere escalatie Oekraïne-conflict* ('Uncertainty variants in case of further escalation of the conflict in the Ukraine', *CPB background document*, The Hague: Netherlands Bureau for Economic Policy Analysis, 20 August 2014.

84 P.A.G. van Bergeijk, 'The return of the Cold Trade War?', Voxeu.org, 6 November 2014.

Resilience

The conclusion of the above is that the risk of economic vulnerability of the Netherlands is growing and is expected to grow further in the light of geopolitical developments discussed above. The extent to which this will actually harm the functioning of the Dutch economy depends in part on its economic resilience.⁸⁵ In response to the susceptibilities and risks already established, the resilience of the Dutch economy may be increased on several levels. Four elements are important in this respect: risk diversification, risk reduction, reduction of the direct effects of negative exogenous shocks and (credible) economic countermeasures. These instruments may be used to help boost the economy's resilience, looking at the various dimensions of susceptibility: trade and international value chains, the international financial system, direct investment, raw materials and energy, and the use of the internet.

With regard to reducing the Netherlands' vulnerability as a result of its export dependency and involvement in international value chains, diversification constitutes an important policy instrument for addressing its vulnerability to the strategic economic policies and means of economic leverage of other countries. Also with regard to access to essential raw materials and energy, this is a way to become more resilient, e.g. strong enough to deal with instability in supply countries which are important for the Netherlands. In principle, susceptibility to foreign pressure can be reduced by preventing or reducing the dependence on one or a very limited number of foreign parties, since having several suppliers and markets offers the possibility of substituting one for the other; it is thus an important policy instrument for the government and corporate sector. However, it is important here to examine the entire value chain, since on the basis of (exclusively) the direct suppliers it is not possible to gain sufficient insight into the origin(s) of various parts and, therefore, into the main dependencies.

If supplier diversification is not an option, keeping strategic stocks is; although this is ultimately not the answer, building up stocks can help to temporarily relieve the economic pressure. Furthermore, greater emphasis may be placed on waste prevention during the production and consumption process and on recycling, which decreases the intensity of use of scarce production resources in the production process and thereby reduces the level of dependency. Substitution, i.e. replacing (if possible) vulnerable materials with other means, is another way to reduce vulnerability.

With regard to the risk that direct investments will increase the economic vulnerability to political pressure or strategic economic policies, resilience can be increased by means of an assessment framework which has been tailored to similar initiatives in other EU countries. The Ministry of Economic Affairs has conducted a survey into the adequateness of the existing instruments for the telecom sector are adequate. As a follow-up to this survey, the Ministry is now preparing a legislative proposal which will provide additional instruments for assessing national security risks during take-overs ("acquiring predominant control") in vital telecommunication infrastructure.⁸⁶ The advantage of this sector-specific approach, whereby assessments are carried out *ex ante*, is that it offers the government flexibility, enabling it to

85 This in conjunction with the nature of the relationship of dependence, i.e. the degree of asymmetry in this relationship.

86 Letter from the Minister of Economic Affairs to the Lower House, dated 10 June 2014, regarding "Acquiring predominant control of a telecom company with vital telecommunications infrastructure"; letter from the Minister of Security and Justice to the Lower House, dated 10 June 2014, regarding "Policy response to the report of the Economic Security Working Group".

provide ‘tailor-made solutions’. However, it remains to be seen whether this approach will provide sufficient transparency to potential investors and whether the government will have to monitor foreign investments and their backgrounds from a central point and with a bird’s eye view. Furthermore, the possibility to strengthen coordination between EU Member States in this area also seems an important item for consideration, given the close interdependence of their economies.⁸⁷

With respect to the potential vulnerability resulting from the Netherlands’ high level of interconnectedness with the international financial system, there are various ways to increase its resilience. The Dutch financial sector would be less vulnerable to exogenous shocks if Dutch banks were better capitalised. In this respect, according to the *CPB Risk Report on the Financial Markets*, Dutch banks are on the right track to satisfy the stricter capital requirements.⁸⁸ However, the vulnerability of the financial sector lies mainly in its relative size, which is very large. A smaller financial sector would make the Dutch economy less vulnerable.⁸⁹

With regard to reducing the potential vulnerability resulting from the use of the Internet, several steps to enhance resilience may be taken, also referred to as *cyber resilience*. First of all, companies and private individuals should make themselves more aware of the risks of using the Internet. Technological steps can also be taken. This concerns, for example, investing in better defences against cyber attacks, such as multi-layered *firewalls* and advanced encryption and authentication tools. However, prevention is not enough; sufficient capacity is required to detect attacks, devise an adequate response and expose any attackers. This could, for example, also have a deterrent effect on States which systematically engage in or facilitate economic espionage as part of their strategic economic policy.⁹⁰

In a more general sense, deterrence as a countermeasure to reduce or prevent vulnerability will only be effective on specific conditions,⁹¹ and will in any event be more effective if there is a stronger mutual relationship between parties. In addition, it is a fact that, although the Netherlands can take steps independently to reduce its economic vulnerability, cooperation with partners in bilateral and multilateral frameworks (in particular EU partners) will often be required to actually increase its resilience.

Attempts have been made in the past to achieve resilience by maintaining special bilateral relations. However, intensive development cooperation with Indonesia and India, for example, has not proved to be a firm basis for good political relationships since a unilateral relation of dependence does not fit well with the growing self-awareness of these emerging economies.

87 See also in this regard as far as Chinese investments are concerned: Thilo Hanemann & Mikko Huotari, *Chinese FDI in Europe and Germany*, pp. 42-43; Maaïke Okano-Heijmans & Frans Paul van der Putten, ‘Europe Needs to Screen Chinese Investment’, *Financial Times*, 11 August 2009.

88 *CPB Risicorapportage Financiële Markten* (‘CPB Risk Report on the Financial Markets’), The Hague: Netherlands Bureau for Economic Policy Analysis (CPB), 5 June 2015, p. 17.

89 Jonathan Witteman, ‘Grote financiële sector in Nederland schaadt economie’ (‘Large financial sector in the Netherlands harms the economy’), *De Volkskrant*, 10 June 2015.

90 Frans-Paul van der Putten, Minke Meijnders & Jan Rood, *Afschrikking als veiligheidsconcept tegen niet-traditionele dreigingen: Verdiepingsstudie Clingendael Monitor 2015* (‘Deterrence as a security concept against non-traditional threats: In-depth study of the 2015 Clingendael Monitor’), The Hague: Netherlands Institute of International Relations “Clingendael”, June 2015.

91 *Ibid.*

Resilience can, however, be achieved on the basis of mutual recognition and cooperation on the basis of equality.

Yet, with a view to reducing its economic vulnerability, the Netherlands will benefit most from the existence of a well-functioning and effective multilateral global financial and economic system. Embedding a stronger, interdependent global economic system within a *rule-based order* offers the best guarantee for a *level playing field* and for peaceful conflict settlement, as well as for some protection from the unilateral actions of third parties, provided there is a wide membership. In this regard the Netherlands (just like other medium-sized European countries) is faced with a major dilemma regarding its interests. Since the Netherlands benefits from a strong multilateral system, the current challenge is to give emerging countries a say, this with a view to retaining the system. Only then will the emerging countries be prepared to abide by the rules. However, sharing power with these countries implies a declining influence of the Netherlands and its partners. If Western countries, including the Netherlands, are not prepared to make compromises, the multilateral system may be subject to further fragmentation. Initiatives by the emerging economies, such as the establishment of the BRICS Bank or the Asian Development Bank, at first glance constitute competition with institutions such as the World Bank and confirm the existing risk of a shift from a multilaterally embedded global order to a more diffuse system. From this perspective, the question arises as to whether further economic integration with North America through the so-called *Transatlantic Trade and Investment Partnership* (TTIP) is necessary and desirable. (TTIP is essentially a non-multilateral project between two economic superpowers which, because it excludes China and other emerging economies, therefore raises the question whether it will strengthen the multilateral system as the Netherlands would like). It underlines the dilemma which the Netherlands is now facing: the multilateral system can only continue if the emerging economies become co-owners.

Conclusions

From every perspective discussed in this report, the Dutch economy is highly and increasingly dependent on, and therefore susceptible to, international trends and events. This applies to trade, direct investment, financial relations, value chains, raw materials and, in the years ahead, the use of the Internet. Partly because of the extension and branching out of international value chains and the use of the Internet, this susceptibility will continue to increase. Moreover, not only is the Netherlands as far as the economy is concerned closely interconnected with countries that are ideologically compatible (EU Member States, the United States, Japan), this is also ever more the case in its relationships with countries outside this traditional circle of economic and diplomatic partners. Although in this context China stands out as the upcoming economic superpower vigorously pushing its way to the foreground, in general the economic clout of non-Western countries and regions is also steadily growing. While these countries were mainly relevant as suppliers of oil and other raw materials a few decades ago, they now as well play a major role as markets, as investors, as links in the value chain and as competitors in every possible branch of industry. The interconnectedness of the Dutch economy with the global economic system is not expected to decrease in the next 5 to 10 years; depending on the development of the global economy, this interconnectedness is more likely to increase. Moreover, it is likely that the dependence on non-traditional markets, i.e. outside the OECD region, will also increase as a result of the ongoing global shift of power.

Against this background, this report focuses on current *geopolitical* developments which are expected to still be relevant in the next 5 to 10 years as far as the economic vulnerability of the Netherlands is concerned. *First of all*, this concerns the process of the *global shift of power*, whereby the West and Japan will become less influential in comparison with the non-Western world. Of the dimensions of susceptibility discussed here, the potential impact of this process is significant as far as the harmful effects of the *strategic economic policies* of other States are concerned. The greater international influence of countries where the government intervenes in the economy more frequently and profoundly than is customary in Western economies has a long-term effect on international competitive conditions and on access to markets, capital, technology and raw materials. Depending on the particular economic sector, this may to a greater or lesser extent have an adverse effect on Dutch companies and the Dutch economy in general. An important question for a follow-up study is therefore: which economic sectors are particularly vulnerable to external factors. Incidentally, it should be pointed out here that the emergence of non-Western economies also creates opportunities for Dutch companies in the form of new markets for Dutch export products, investment opportunities, etc.

However, countries which systematically engage in or facilitate economic espionage as part of their strategic economic policy pose a potential threat as far as (cyber) espionage is concerned. Moreover, as a result of the global shift in power, the susceptibility of the Netherlands to the economic strategic policies of other States increases in two different respects. Firstly, as a result of the increasingly *close* economic contacts with countries with a centralised economy; secondly, as a result of the declining ability to promote *standards* which limit the market-distorting interventions of national governments in world trade.

The global shift in power is also relevant for the other two dimensions of economic susceptibility. With regard to the risk of the Netherlands becoming a (direct) target for *economic sanctions*, it can be concluded that the risk is limited as far as sanctions imposed by Western actors are concerned. However, as non-Western actors become more influential economically and diplomatically, the likelihood that the Netherlands will be subjected to threats of sanctions, or actual sanctions, for geopolitical, religious or ideological reasons (e.g. related to human rights) will increase. As far as the dependence of the Netherlands on *unstable regions* is concerned, the shift of the global economy's centre of gravity to Asia implies that the Dutch economy will become more susceptible to a regional crisis in that part of the world. The declining global influence of the European Union also has consequences for its ability to tackle internal financial and economic problems.

The *second* geopolitical factor concerns the increase in *tensions between the superpowers*, in particular between Russia and the EU/US and between China and the US/Japan. The potential effect of this factor is greatest when it concerns the application of economic *sanctions*. Tensions between Russia and the EU/US are already manifesting themselves in the form of mutual sanctions. As a Member State of the EU, the Netherlands is directly involved in this, but it may also indirectly suffer the consequences of, for example, a prospective tightening of American sanctions against Russia. The indirect effect of economic sanctions between China and the United States or between China and Japan could also affect Dutch economic interests. Unlike in previous instances of American sanctions against countries such as Iran, which put significant pressure on the Dutch companies involved, many Dutch companies cannot pull out of China without suffering very significant damage (and pulling out of the US is certainly not an attractive or feasible option either).

Further tensions between the superpowers could also result in stronger *strategic economic* actions by big countries. When there is growing international distrust and multilateral cooperation is difficult, big countries in particular tend to secure the competitive position of their strategic companies and access to raw materials, markets, technology and capital through government intervention. Smaller countries such as the Netherlands have limited options to reduce their economic susceptibility through such means. It should be pointed out here that an increase in inter-superpower tensions will not automatically result in less economic cooperation. As shown by the summary report of the *Clingendael Monitor*, rivalry and cooperation can exist side by side. However, if the geopolitical rivalry continues to intensify, a point may be reached where this has a negative effect on economic cooperation at bilateral and multilateral levels.

Finally, tensions between the superpowers also affect the third dimension of economic susceptibility, i.e. the dependence on *unstable regions*. In this regard, it should be pointed out that the regions surrounding the EU, in particular the MENA region, will for the time being be affected by ongoing and possibly mounting tensions and instability. In Eastern Europe and East Asia, the effect is *direct*, since the instability in these regions is an immediate result of the deteriorating inter-superpower relationships. In the Middle East and parts of Africa, the effect is more *indirect*; because of conflicting interests and mutual distrust, the superpowers seem unable to adopt a unified approach to these regional crises. At the same time, the Netherlands' economic interests in these regions are considerably less than the interests linked to China or Russia. To date, the geopolitical tensions have only had a relatively limited effect on the (in)stability within the EU. This may change, however, if Europe, partly as a result of global loss of power, were – to a greater or lesser extent – to become the playing field of rivalries between actors such as the United States, China and Russia.

One may conclude that the potentially harmful effects of geopolitical developments and events on the Dutch economy are considerable. This applies to both the global shift of power (the West becoming less dominant) and the mounting tensions between various superpowers (Russia vs. the US/EU; China vs. the US/Japan). This concerns the risk that the Netherlands will be affected directly or indirectly by sanctions, will suffer damage from the strategic economic policies of other countries and will become more vulnerable as a result of developments in unstable regions outside the EU, especially in relation to Russia and East Asia. The question as to which economic sectors are particularly vulnerable merits further investigation.

At the same time, care should be taken not to draw too alarmist conclusions. Whether, and to what extent, the Netherlands will actually become economically vulnerable will primarily depend on how global relationships develop in the future, in particular relations between the superpowers themselves. If tensions in these relations increase, resulting in international cooperation becoming more difficult, the risk of vulnerability will also increase. However, as we pointed out in the introduction, this is counterbalanced by the fact that the current global system is characterised, both financially and economically, by a high degree of interconnectedness, which can have a moderating effect. This observation is supported by the fact that, in a world where geopolitical forces seem increasingly to manifest themselves, alongside rivalry we find continuing cooperation, both within multilateral frameworks and between the superpowers. Finally, this study also shows that the Netherlands can increase its economic resilience, either independently or in collaboration with partners, but preferably within a multilateral framework.