

If You're Not Planning for World War III, Your Portfolio Is at Risk

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Today in *Exponential Investor* it's World War III – and I'm not talking metaphorically. Humanity has been at war ever since we were chimps – and there's no sign of this changing. I'm going to track down the next major conflagration – so you can invest accordingly.

Conflict exerts an enormous influence on our economies – and hence on our investments. Whether you want to profit from Britain's lead in the arms trade, or just spot the risks an emerging global conflict might cause, watching out for war is vital.

Where could World War III come from?

Major clashes tend to arise when power transfers from one global power to another – an effect known as Thucydides's Trap, named after the Athenian who discussed the inevitability of war between Athens and Sparta.

“What made war inevitable was the growth of Athenian power and the fear which this caused in Sparta.”

The transfer of power reliably leads to war – according to Harvard University's Graham Allison. In three-quarters of cases, spanning more than 500 years, a transfer of regional or global power resulted in war. In cases where peace prevailed, there were almost invariably strong bonds of culture and ethnicity, or pragmatic politics, to stand in the way.

Between weakly connected competing powers, war is all but inevitable

Apply this to the modern world, and I'm sure you know who I'm talking about. Relatively speaking, the US is on the slide. Its population is small, compared to China – the world's new superpower. This means it is at an inherent disadvantage, in any future conflict.

If you think that China's not going to be trouble, you need only look to India to find another potentially belligerent rising superpower. It is, after all, a nuclear armed state – with a rapidly expanding economy, and a huge population. Presently, India has a troubling, nationalistic, sectarian leader – with a rather murky past. This of government does not allow us to assume a future in which India settles calmly into a globalised world.

As for the US: it's almost impossible to imagine a situation in which a country that has only a fraction of the population of China can maintain its global economic and political dominance. Unlike the British Empire, which commanded 15 million troops in World War II, the Pax Americana has a relatively loose grip over its allies. Donald Trump can no more order the German army to war than he can summon fairies to fly to the moon.

While the US is indisputably the world premier military power, this situation will not last if the emergent Chinese choose to invest significantly in arms. The Chinese are already a significant nuclear state. Furthermore, they're investing in carriers – and some of the world's most advanced anti-submarine warfare (based on SQUIDS – but that's a story for another time).

The Chinese economy is set to accelerate far beyond that of the US – and its defence spending will likely follow. The US's military might has been called into question in recent years more sharply than at any time since the end of the Vietnam War. The US is mired in the consequences of its misadventures in Iraq, and unable to conclusively win in Afghanistan (its longest-ever war). Militarily, the US is looking increasingly like the crumbling Soviet Empire.

China's newly muscular approach to foreign affairs suggests a new confidence in its place in the world. China is currently buying up land, infrastructure and allies in Africa. You can read more about this growing Chinese economic influence, courtesy of our colleagues at .

Furthermore, China is also undertaking direct military expansion in its own back yard. Presently, it is engaged in low-level conflict in two key theatres:

Firstly along the border (if you could call it that) between the Indian sphere of influence and the Chinese sphere of influence. The current flashpoint is actually in Bhutan – where China has effectively annexed territory, to build a .

Secondly it's trying to militarily occupy the South China Sea – by building bases on top of formerly submerged atolls, which it

has built up into artificial islands. Notwithstanding Anglophone countries' posturing, it seems unlikely that the West will have the stomach to engage in an all-out war, for these faraway spits of land. It's exactly that kind of calculation which strengthens China's hand in its regional militarism – much to the ire of its neighbours, which have responded by rapidly arming themselves (seemingly to China's surprise).

This will end in war

In all but a handful of cases over half a millennium, a migration of the world's economic poles has resulted in catastrophic war. No saviour seems likely, according to a rigorous analysis of history. Ties of shared culture, language or ethnicity do not bind the US and China – they are chalk and cheese.

In the previous 500 years, the only example of superpowers avoiding direct conflict is the Cold War. Nevertheless, this was marked by a series of proxy wars and brinkmanship, tamped down only by the threat of nuclear-armed mutually assured destruction. Nevertheless, the enduring tinderbox of Cold War tension was almost ignited by several mistakes and malfunctions. At different times, both Soviet and American nuclear arsenals were each very nearly launched, after incoming missiles were falsely detected. The lesson of those errors is clear: even if mutually assured destruction is the main guarantor of peace, we cannot rely on its efficacy. If the Cold War technicians in the control centres had been less sceptical of their flaky warning systems, we may all be dead!

Our conclusion is simple: if you're not planning for World War III, your portfolio is vulnerable.

Please send us your thoughts in an email from your fallout shelter: andrew@southbankresearch.com.

Best,

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