

MARKET POWER POLITICS

War, Institutions, and Strategic Delay
in World Politics



Stephen E. Gent
Mark J.C. Crescenzi

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Delay in World Politics*



STEPHEN E. GENT
AND
MARK J. C. CRESCENZI

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For Nick and Anita

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Preface

CPP28

IN ITS BROADEST strokes, *Market Power Politics* is a book about politics, economics, and law in the global arena. The politics we cover here deal with peace and conflict between countries (we will call them *states* in the book). With respect to economics, we are interested primarily in trade and investment that crosses international borders. Lastly, we care here about the use of international laws and institutions that states have created to manage either the first (politics) or the second (economics) component, or both. Sometimes these three things fit together efficiently, making it easier for firms and their governments to exchange goods, services, and capital in ways that tie the world together and make it more peaceful. When that happens, the three components start to work together as a team. Legal institutions make it easier to trade goods and services or invest capital, for example, and increased wealth from trade may minimize the desire to interrupt that trade with political violence.

CPP29

Other times, however, at least one of the pieces is out of alignment with the others. When that happens, the same connectivity that brings these three dimensions of human interaction together as a team can lead to difficult or even disastrous consequences. When institutions cannot offer a legal solution to disputes, states will seek their own solutions, often at the expense of others. When those disputes are motivated by *market power*, or the ability to influence prices, supply, or demand within markets—particularly in markets that are important to governments and their leaders—then the logic of minimizing political violence in the interest of wealth can flip on its head. This is a book about the consequences of that flip. The consequences can be quite dramatic, resulting in the use of military force and even the outbreak of war. But often the consequences of market power fall in between the two extremes of prosperous peace and the catastrophic consequences of war. Instead, states sometimes opt out of cooperation with one another; but rather than jumping right into a fight, they *delay* a resolution to their dispute. They may even push one another around while they are doing it,

engaging in bellicose talk and small territorial or maritime grabs without ever boiling over into full-scale war.

CPP30

The view we take in this book is that even in these situations where the synergy of politics, economics, and law fails to materialize and market power opportunities trigger conflict, the three components still work together in important ways. By studying their interaction even when things aren't going smoothly, we believe we can identify why some states boil over into war while others seem to simmer incessantly. We illustrate our intuition by applying our theory of market power politics to three of the most important places and moments in the last fifty years: the Persian Gulf War in the 1990s, Russian conflict with its neighbors such as Georgia and Ukraine in the previous decade, and China's interactions with its neighbors in the East and South China Seas over the last thirty years.

CPP31

This already sounds complicated, so let us pause here to reassure the reader that we have designed this book to be widely accessible. Our hope is that anyone with an interest in world politics can read the book, and we have removed as much of the technical jargon as we could in pursuit of this goal. Non-academic readers may want to skim through Chapter 4, however, as we do spend a little time talking about how we chose these cases and why that matters. Even so, anyone who has taken an introductory course in international relations should have the tools to read the entire book.

CPP32

In some ways, this book represents the partnership of its two authors. Stephen Gent has long held an interest in the interactions between international institutions and peace. His expertise in the goals and structures of these institutions helped us see the cause of their failure to resolve the disputes that we examine in the second half of the book. Mark Crescenzi has studied the link between economics and conflict in world politics for a quarter of a century. When he wrote his first book on economic interdependence and conflict, and how interdependence can sometimes keep states from fighting, this flip side of the relationship nagged in the back of his mind. Both of us found that we were unable to complete our thoughts on these matters on our own. But while sitting on a bench on the balcony of the UNC Student Bookstore, we hatched a plan to work together. This book is the product of those efforts.

CPP33

Along the way we have had a tremendous amount of help. We presented nascent pieces of the research at academic conferences and meetings, gathering feedback from scholars such as Kyle Beardsley, Stephen Chaudoin, David Cunningham, Scott Gartner, Paul Hensel, Kelly Kadera, Pat McDonald, Sara Mitchell, Desiree Nilsson, Jack Paine, Michael Reese, Aisling Winston, and especially Krista Wiegand, whose work was also foundational for our own. At UNC we sought feedback and moral support from Cameron Ballard-Rosa, Navin Bapat, Graeme Robertson, and Patricia Sullivan. We simply could not ask

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CPP₃₄

Finally, Stephen would like to thank Ed and Joy Gent for providing unwavering support and encouragement over the years. He would also like to thank Michael Cain and J. P. Singh, who introduced him to the study of political science and international relations as an undergraduate at Ole Miss. Their classes undoubtedly laid the seed for many of the questions tackled in this book. Mark would like to thank Jim Crescenzi for patiently serving as an early reader, but also for a lifetime of inspiration, friendship, and encouragement. And, of course, we never would have made it to the end of the project without extraordinary support from Nick Siedentop and Anita Crescenzi. We couldn't imagine better partners as we sorted this out, and we are so thankful that they put up with us.

Abbreviations

CPP35	BIS	Bank of International Settlements
CPP36	DPR	Donetsk People's Republic
CPP37	DSB	Dispute Settlement Body (of the World Trade Organization)
CPP38	EEZ	exclusive economic zone
CPP39	EU	European Union
CPP40	FDI	foreign direct investment
CPP41	GATT	General Agreement on Tariffs and Trade
CPP42	ICJ	International Court of Justice
CPP43	INOC	Iraq National Oil Company
CPP44	ISA	International Seabed Authority
CPP45	KOC	Kuwait Oil Company
CPP46	LNG	liquified natural gas
CPP47	LPR	Luhansk People's Republic
CPP48	NATO	North Atlantic Treaty Organization
CPP49	NEE	normal economic exchange
CPP50	OPEC	Organization of the Petroleum Exporting Countries
CPP51	PCA	Permanent Court of Arbitration
CPP52	PRC	People's Republic of China
CPP53	REE	rare earth element
CPP54	TANAP	Trans-Anatolian Natural Gas Pipeline
CPP55	TAP	Trans-Adriatic Pipeline
CPP56	tcm	thousand cubic meters
CPP57	UAE	United Arab Emirates
CPP58	UN	United Nations
CPP59	UNCLOS	United Nations Convention on the Law of the Sea
CPP60	WTO	World Trade Organization

C1

I

Introduction

C1.P1

A MIDNIGHT INVASION of Iraqi troops into Kuwait in 1990 set off a chain of events that have reshaped politics in the Middle East with devastating and deadly consequences. Nearly twenty-five years later, Russia annexed the Ukrainian territory of Crimea and pushed the envelope of using military might without triggering war. Meanwhile, in the South China Sea, China has made bold moves to expand its territory island by island, triggering legal disputes from its neighbors, and yet the fear of militarized violence seems relatively low compared to Russia or Iraq. What do these crucial geopolitical moments in history have in common, besides their importance in the lives and prosperity of dozens of countries and millions of people? Could it be that all three cases are being driven by a common political-economic process? If so, what explains the variance in their outcomes? How do we know when a situation like these will become violent?

C1.P2

Answering these questions is the goal of this book. Here we develop a theory of market power politics that helps us understand why states abandon the post-World War II institutions that help states navigate territorial disputes such as these. In this analysis we identify three potential outcomes when market power politics dominate: war, cooperation, and strategic delay. Understanding the context of political institutions and economic ties that surround market power opportunities is key to knowing which outcome is likely to result when states pursue a strategy of dominating a market. In an era where we have come to expect institutions, trade, and investment to knit governments together and prevent violence, in this book we identify one source of motivation that unravels the fabric of peace and increases the risk of war.

Strategic Delay in the “Gray Zone”

C1.S1

C1.P3

The ambition of states to expand their geographic reach can create or exacerbate disputes over the control of territory or maritime areas. We refer to such disagreements as international *property rights disputes* because they involve competing claims over the sovereign control of resources. States have several strategies to choose from as they try to resolve these property rights disputes in their favor. Some, like Iraq in 1990, choose to press their claims on the battlefield. In fact, disputes over territory have historically been one of the most predominant causes of international war.¹ Alternatively, states may try to avoid a costly war and instead work toward a peaceful resolution of their dispute. Through bilateral negotiations or with the assistance of international institutions, states can reach agreements over how to divide disputed territory or maritime areas.

C1.P4

However, sometimes states choose to go down neither of these paths. Instead, they opt to pursue a policy of strategic delay. *Strategic delay* is the purposeful postponement of a violent or nonviolent settlement of a dispute with the hope of achieving a more preferable outcome in the future. The use of strategic delay is not uncommon in property rights disputes, which are often long lasting.² In some cases, these delay strategies are largely passive in nature. States may simply want to maintain the status quo because they do not expect that they would achieve a more favorable outcome through military force or negotiation.³ At other times, though, we see states taking a more proactive approach and using strategic delay as a way to further their expansionist goals. By delaying, these states have the opportunity to pursue so-called gray zone tactics that allow them to gradually shift the strategic environment in their favor over time.

C1.P5

Gray zone tactics lie somewhere in the “gray zone” between diplomacy and war. They do not involve the overt use of lethal force by a country’s military, so they fall short of what we would call strategies of war. On the other hand, they also fall outside the bounds of the behavior traditionally acceptable within international diplomacy. These gray zone activities often take the form of *salami tactics*. Like consuming an entire salami by cutting a series of small slices, salami tactics involve a country taking small steps that accumulate and achieve a larger goal over time.⁴ In property rights disputes, such a gradual approach can be very effective, as each of the individual steps is less likely to provoke an armed response

1. Holsti 1991; Vasquez 1993.

2. Wiegand 2011.

3. Fravel 2008; Huth, Croco, and Appel 2011.

4. Schelling 1966.

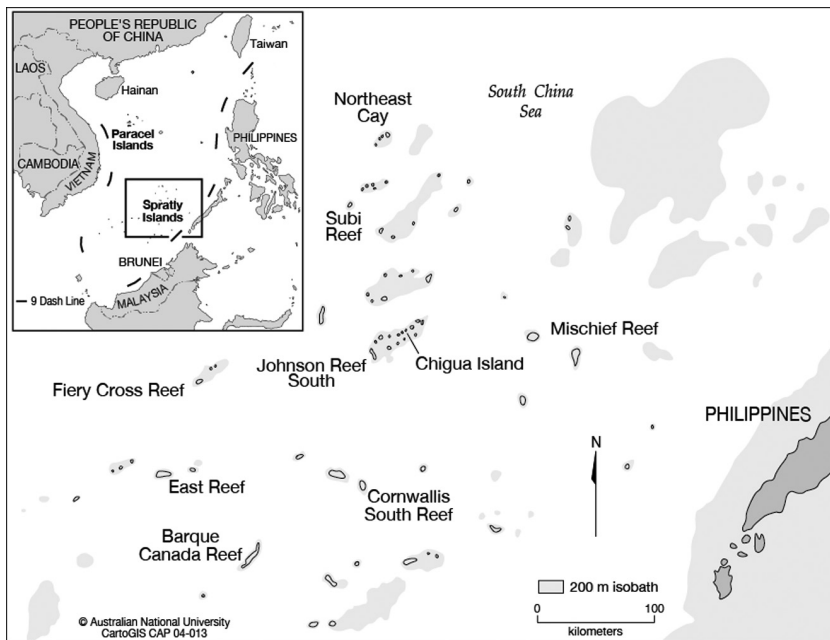
than more aggressive actions. In this way, gray zone tactics allow states to press their territorial and maritime claims while also hoping to avoid major armed conflict. To get a sense of how this combination of strategic delay and gray zone tactics plays out empirically, let us take a look at some of the expansionist activities pursued by China and Russia in recent years.

C1.S2

Mischief in the South China Sea

C1.P6

Consider, for example, the case of Mischief Reef and the ongoing dispute between China and the Philippines. Mischief Reef (Figure 1.1) is an atoll in the South China Sea, roughly 135 miles west of the Philippines. Part of the Spratly Islands, it consists of a narrow coral reef that surrounds a large lagoon. Up until a few years ago, Mischief Reef was what hydrographers and international lawyers would call a low-tide elevation, as it only rose above the level of sea during low tide. Needless to say, for most of its history, Mischief Reef has been home only to marine life and was primarily visited only by fishermen. All of that began to change in the mid-1990s, however, and today the atoll lies at the center of one of the world's



C1.F1

FIGURE 1.1. Mischief Reef in the South China Sea.

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most contentious maritime disputes. What was once a tiny slice of earth that only poked its head above water at low tide has now been launched out of obscurity and is a serious source of international tension in the Asia-Pacific region.

Ci.P7

While four countries—China, the Philippines, Taiwan, and Vietnam—make claim to Mischief Reef, China and the Philippines have taken the most active steps to assert control over the atoll.⁵ China's claim to Mischief Reef is historical. Based upon mid-twentieth-century maps that include the so-called Nine-Dash Line, China contends that it has jurisdiction over almost all of the South China Sea. Thus, despite the fact that Mischief Reef lies over 600 miles from China's Hainan Island and about 800 miles from the Chinese mainland, China claims that the reef is part of its territory. The Philippines, on the other hand, claims that Mischief Reef lies within its own exclusive economic zone (EEZ), a maritime area in which it has jurisdiction over the exploration and exploitation of marine resources.⁶ The Philippine government's claim is based upon its interpretation of the rules for drawing international maritime boundaries laid out in the United Nations Convention on the Law of the Sea (UNCLOS). Both China and the Philippines are parties to UNCLOS, which prioritizes the type of rules-based claim made by the Philippines over historical claims. However, this international institution designed to improve cooperation does not seem to be working in this case.

Ci.P8

In 1995, China established control over Mischief Reef by building four platforms on stilts that housed several bunkers equipped with a satellite dish, which it claimed were shelters for fishermen.⁷ Three years later, China expanded and fortified these structures with the support of armed military supply ships.⁸ Since then, China and the Philippines have engaged in on-and-off-again bilateral negotiations to try to resolve their competing claims over Mischief Reef, as well as other Spratly Islands and the nearby Scarborough Shoal, but they have not been able to reach an agreement on the matter. Similar attempts to resolve the many other overlapping, competing maritime claims of the seven countries that surround the South China Sea have also largely been unfruitful. Notably, China has been reluctant to turn issues of maritime control in the South China Sea over to a tribunal established under UNCLOS. In 2013, the Philippines decided to

5. Throughout the book, we will use the terms "China" and "Chinese" to refer to the People's Republic of China and the terms "Taiwan" and "Taiwanese" to refer to the Republic of China.

6. An EEZ is an area in international waters in which the state has a sovereign right to all economic resources below the surface of the sea.

7. Shenon 1995; Storey 1999.

8. Zha and Valencia 2001.

Introduction

5

take matters into its own hands and notified China that it was going to unilaterally bring its case to the Permanent Court of Arbitration (PCA). China quickly refused to participate. While the Philippine government was eager to use legal institutions to resolve this dispute, China seemed equally eager to not do so.

C1.P9

While the Philippines turned to the courts, China began to take more aggressive steps to expand its presence in the South China Sea. A significant part of China's strategy involved the construction of artificial islands on its occupied features in the Spratly Islands, including Mischief Reef. In January 2015, China began dredging sand and pumping it on top of the coral at Mischief Reef while an amphibious warship patrolled the entrance to the reef's lagoon.⁹ By June of that year, the Asia Maritime Transparency Initiative estimated that over two square miles of land had been already been reclaimed.¹⁰ Since then, Chinese development on Mischief Reef has moved apace, and it continues to construct more permanent facilities on the island. A three-kilometer-long runway was completed in 2016, along with several hangars for large aircraft. Additional construction projects on the island have included underground storage for ammunition, communications towers, and structures to house defensive weapons systems.¹¹

C1.P10

An adverse ruling by the PCA in June 2016 hardly provided a speed bump to China's expansionist plans on Mischief Reef. The Court ruled that the reef was a low-tide elevation before China's reclamation efforts and thus does not generate any entitlement to a territorial sea. Moreover, the Court found that Mischief Reef lies within the Philippines' EEZ. China, however, refused to accept the court's ruling and continued to claim sovereignty over much of the South China Sea. Rather than taking a step back, China pushed forward with its efforts to militarize the Spratly Islands, including Mischief Reef. By mid-2018, the Chinese military had quietly installed communications jamming equipment, anti-aircraft guns, anti-ship cruise missiles, and surface-to-air missile systems on its outposts in the Spratly Islands.¹²

C1.P11

The pattern of activities on Mischief Reef mirrors similar Chinese projects on other islands in the Spratly archipelago, including Fiery Cross Reef and Subi Reef. Whether or not it had initially aimed to just build structures to provide shelter for fishermen in the mid-1990s, China has clearly moved toward a slow but steady militarization of its claimed territory in the South China Sea. Rather

9. Sanger and Gladstone 2015.

10. Asia Maritime Transparency Initiative 2015.

11. Asia Maritime Transparency Initiative 2018.

12. Macias 2018.

than accepting a legal settlement or turning to military force, China has preferred a policy of strategic delay. By delaying, China has been able to pursue a campaign of gray zone activities to expand its presence in the South China Sea. In the case of Mischief Reef, China's strategy provides a textbook example of salami tactics. China first installed platforms on the reef, followed by the construction of an artificial island that could house larger structures and an airstrip. It is now moving forward with the installation of military weapons on the island. These steps have allowed China to gradually consolidate its control of Mischief Reef and other islands the South China Sea without sparking a major armed conflict.

C1.S3

Russian Expansion: A Land-Based Analogue

C1.P12

While China has been building islands to expand its reach into the South China Sea, Russia has pursued territorial ambitions of its own in the Black Sea region. South Ossetia is a landlocked breakaway region of north-central Georgia that borders Russia. It has little in the way of natural resources, and its citizens largely rely upon subsistence farming. In the wake of the breakup of the Soviet Union, South Ossetia declared independence from Georgia, sparking the first of a series of civil wars that Georgia suffered in the early 1990s. Since then, South Ossetia has often been described as being a "frozen conflict," and the region has largely remained outside the effective control of the Georgian government, relying upon the support of Russia for survival. As part of the civil war peace settlement in 1992, Russia deployed a peace-keeping force to the region that has never left. In the mid-2000s, Russia gradually increased its military capabilities in South Ossetia, and during a brief five-day war in August 2008, Russian and Ossetian troops pushed out any remaining Georgian presence in the region. Later that month, Russia officially recognized South Ossetia's independence, but very few other countries followed suit.

C1.P13

Since the 2008 conflict, Russia has continued to expand its influence in South Ossetia, as it gradually integrates the region militarily, politically, and economically with Russia. To secure the territory of South Ossetia, Russia routinely engages in a "borderization" strategy that Georgia calls a "creeping occupation." Since South Ossetia was not a formal administrative unit of Georgia, its boundaries were not clearly defined. Thus, Russian forces have taken it upon themselves to demarcate this largely unrecognized "international" border by erecting border fences and signs. As part of the strategy, on multiple occasions since 2013, Russia has literally shifted the boundary posts of the border to expand South Ossetia's territory.¹³ For example, in a land grab in July 2015, South Ossetia gained access

13. A report by the Heritage Foundation identifies ten cases of borderization from May 2013



C1.F2

FIGURE 1.2. Russia's borderization strategy in Georgia.

to a mile-long stretch of the Baku-Supsa oil pipeline and pushed the border to within 500 meters of the E60 highway connecting Azerbaijan and the Black Sea (Figure 1.2). Media reports indicate that residents have gone to bed thinking that their house was located in Georgia proper and have woken up finding themselves living in South Ossetian territory.¹⁴ Slowly but surely, these Russian encroachments into Georgian territory continue unabated, despite objections from Georgia and the West.

C1.P14

As Russia pursues its borderization strategy in Georgia, it has also utilized unconventional methods to expand its territorial reach in another neighbor, Ukraine. Crimea is a strategically located peninsula in the northern Black Sea. Home to the Russian Black Sea Fleet and a largely Russian-speaking population, Crimea had been part of Russia from 1783 to 1954, until the Soviet Union transferred control of the peninsula to Ukraine. In late February 2014, in the midst of the Euromaidan protests in Ukraine, reports of sightings of “little green men” emerged in Crimea. These men in question were Russian-speaking armed soldiers wearing green military gear without any insignia. While it was commonly understood that the men were Russian military personnel, likely including members of the 810th Marines Infantry Brigade and Russian special forces, the Kremlin

to August 2017 that resulted in additional Georgian territory falling within South Ossetian territory (Coffey 2018).

14. North 2015.

denied the presence of any Russian military forces in Crimea. Instead, Russian President Vladimir Putin claimed that they were merely members of local “self-defense groups.”¹⁵

C1.P15 These non-uniformed soldiers played a key role in Russia’s annexation of Crimea. On February 27, armed men seized the parliament building in Crimea’s capital, Simferopol, and raised the Russian flag.¹⁶ In the following days, unmarked Russian soldiers occupied and blockaded the Simferopol airport and several military bases in Crimea.¹⁷ With their help, Russia then moved arms and military equipment into Crimea and eventually took control of the peninsula. Under Russia’s guidance, Crimean officials quickly scheduled a referendum on Crimea’s political status, and within a month of the appearance of the “little green men,” Russia annexed Crimea into its own territory. Following this success in Crimea, non-uniformed Russian troops appeared in eastern Ukraine to support the pro-Russian separatist forces in Donetsk. The use of such deniable forces appears to have become a standard tactic in Russia’s strategic playbook.¹⁸

C1.P16 Like China, Russia has largely relied upon gray zone tactics to pursue its territorial ambitions in recent years. Russia’s expansion into Georgia has largely consisted of a series of salami tactics. It has gradually consolidated its power in South Ossetia over the past quarter-century and is slowly expanding its reach into Georgian territory through its borderization strategy. Moving border fences to redraw borders though a “creeping occupation” is a strategy designed to incorporate small steps that will likely not trigger a significant reaction on their own. Russia’s annexation of Crimea provides an example of a related tactic common in gray zone campaigns known as a *fait accompli*, or land grab.¹⁹ In this case, Russia seized control of the entire territory, hoping that it would not provoke an armed response from other states. Through this combination of salami tactics and *faits accomplis*, Russia has been able to strategically advance its interests without resorting to open warfare.

15. Shevchenko 2014.

16. Booth and Englund 2014.

17. Oliphant 2014.

18. Altman 2018.

19. Altman 2017; Mazarr 2015; Tarar 2016.

Two Puzzles

C1.S4

C1.P17

In many ways, the expansionist behavior of China and Russia cuts against the general trend in international relations in recent decades. For one, since the end of World War II, the international community has largely embraced a norm against the use of coercion to revise territorial borders.²⁰ Historically, major powers routinely used their military might to try to expand their territorial control, and borders often shifted as a consequence of these conflicts. However, such coercive territorial revision is no longer widely seen as acceptable behavior. Additionally, in an increasingly interdependent global environment, uncertainty about borders can have greater economic consequences. Mutually recognized boundaries clearly define property rights and jurisdictional control, facilitating economic activity and international trade.²¹ Thus, one might expect that these economic incentives would push countries to settle any outstanding disputes over territorial and maritime control. However, as China and Russia have become more integrated into the global economy in the first two decades of the twenty-first century, they have actively perpetuated these property rights disputes with the aim of expanding their territorial reach.

C1.P18

The expansionist activities of China and Russia are also notable in that they have, by and large, not escalated to major armed conflicts. The desire for territory has historically been one of the predominant causes of war between countries. However, both China and Russia have preferred to pursue tactics that remain in the gray zone between traditional diplomacy and war. Only during its brief five-day war with Georgia in 2008 has Russia engaged in significant active combat with a neighboring country, and China has largely avoided violent international military clashes to advance its claims in the South and East China Seas.²² At the same time, both countries have deferred negotiating settlements over these territorial claims. By strategically delaying the resolution of boundary disputes, China and Russia have been able to pursue salami tactics to achieve their expansionist goals over time.

C1.P19

These patterns highlight two key puzzles. First, why do China and Russia pursue policies of territorial expansion in the face of widely accepted norms of territorial integrity and their increased interconnectedness with the global economy? Second, why have China and Russia largely relied upon gray zone tactics

20. Atzili 2011; Zacher 2001.

21. Simmons 2005.

22. The two notable exceptions to this were the brief naval disputes between China and Vietnam over the Paracel Islands in 1974 and the Spratly Islands in 1988.

to pursue these goals, rather than overt military force or negotiations through international institutions? For example, why has Russia not launched a full-scale war to occupy its neighbors, as Iraq did against Kuwait in 1990? On the other hand, why has China refused to settle its maritime boundary disputes in the East and South China Seas in an international court? The goal of this book is to solve these puzzles.

C1.S5

Market Power, Economic Interdependence, and International Institutions

C1.P20

To explain the behavior of states like China and Russia, we develop a theory of market power politics. This theory helps us to solve these puzzles by identifying factors that motivate and constrain the expansionist behavior of states involved in property rights disputes. Competition for market power can motivate states to take aggressive actions to expand their territorial reach or to prevent others from doing so. At the same time, economic interdependence and international institutions can place constraints on the strategies that states take to achieve these goals. To help set up our argument, let us briefly introduce these three key pieces of the puzzle: market power, economic interdependence, and international institutions. Then we can show how they fit together to form our model of market power politics.

C1.S6

Market Power Motivation

C1.P21

Market power is the ability to generate prices that diverge from what would result from a fully clearing competitive market. In normal economic exchange environments, prices are set by supply and demand conditions in the market. Thus, for all practical purposes, buyers and sellers are price takers. However, in markets of imperfect competition—like monopolies, monopsonies, and oligopolies—opportunities emerge for firms to gain price-setting abilities. For example, when a producer controls a significant share of a market, it may be able to use its market power to raise prices above the market price. On the other hand, if a buyer sufficiently dominates a market, it may be able to benefit from below-market prices. When firms set prices in their favor, they are able to generate extra profits, which are known as *rents*. Given the value of these potential rents, firms have strong incentives to accumulate market power.

C1.P22

While the ability to set prices is clearly valuable to firms, our analysis primarily focuses on the benefits that this market power can provide to state leaders. Economically, the rents that firms generate from price setting can provide a source

of revenue for the state. Additionally, market power in key markets can promote domestic political stability and provide leaders with international bargaining leverage. These economic and political benefits will likely be greatest when states own or have significant control over firms that have the ability to set prices for a key good in the state's economy. In these cases, states have strong incentives to take steps to increase their firms' market power. At the same time, other states will be motivated to prevent these states from capitalizing on market power opportunities. As we will see, this creates a competitive international environment that can potentially lead to armed conflict.

C1.P23

We mainly focus our attention on market power competition in hard commodity markets. *Hard commodities* are natural resources that are mined or extracted, such as energy resources and metals. In Part II of the book, we will take a close look at the market power motivations of three hard commodity producers: Iraq (oil), Russia (natural gas), and China (rare earth elements). Since the production of hard commodities typically requires a state to have access to resource reserves, market power in these markets is often a function of who controls the territory where these reserves are found and the supply routes by which the commodity is transported. Thus, if a state wants to increase its firms' market power or prevent another state from doing so, it may need to expand its territorial control. If the benefits of market power are sufficiently high, the state may be motivated to take aggressive steps to do so.

C1.S7

Economic and Institutional Constraints

C1.P24

While competition over market power provides a motivation for territorial expansion, states can be constrained from taking escalatory actions in pursuit of these goals. One such constraint is *economic interdependence*. Observers of international relations often equate economic interdependence with high levels of economic interaction between states. However, interaction does not necessarily imply interdependence. Instead, economic interdependence exists when the costs of exiting an economic relationship are high. These exit costs depend upon the availability of substitutes and the costs of adaptation. For example, if a state that relies upon natural gas for home heating has only one supplier of natural gas and cannot easily access alternative sources, exiting the relationship with that supplier would be very costly. Such economic interdependence between states increases the costs and risks of using violence. If armed conflict would result in economic exit, states that are dependent on one another will face potentially destabilizing economic costs that may be sufficient to deter them from escalating property rights disputes.

C1.P25

International institutions provide another constraint on aggressive state behavior. *Institutions* are sets of rules that govern human behavior.²³ To help achieve efficient outcomes in the global political economy, states have created a variety of international institutions that promote coordination and cooperation through the reduction of transaction costs. In the context of territorial conflict, institutions reduce the need for states to turn to violence by providing an avenue for states to peacefully resolve their property rights disputes. They do this in two primary ways. First, institutions provide rules to guide states on how they should allocate property rights. For example, international law articulates principles to follow when drawing territorial borders, while UNCLOS outlines a set of rules for determining the boundaries of maritime areas. Second, institutions provide procedures to help states reach durable settlements that are in line with those rules. When states are not able to reach a negotiated settlement on their own, they have the option of turning to an international organization to mediate the dispute or an international court to lay down a legal ruling.

C1.P26

In some situations, however, the presence of institutions can discourage dispute resolution. For one, institutional rules may limit the ability of states to achieve their political goals. For example, in the South China Sea dispute, a settlement consistent with the rules laid out by UNCLOS would likely require China to give up its claim to much of the sea. This politically unacceptable outcome makes China less willing to pursue an institutionally based settlement. Additionally, the difficulty of altering legally established boundaries raises the stakes of any settlement reached in a property rights dispute. This can reduce the willingness of states to make concessions over territory or submit their claims to an international court. Thus, some of the same factors that make institutions effective dispute-resolution mechanisms can make states less willing to reach a settlement in the first place. For this reason, the ability of institutions to constrain aggressive behavior in the face of market power opportunities will vary depending upon the strategic situation.

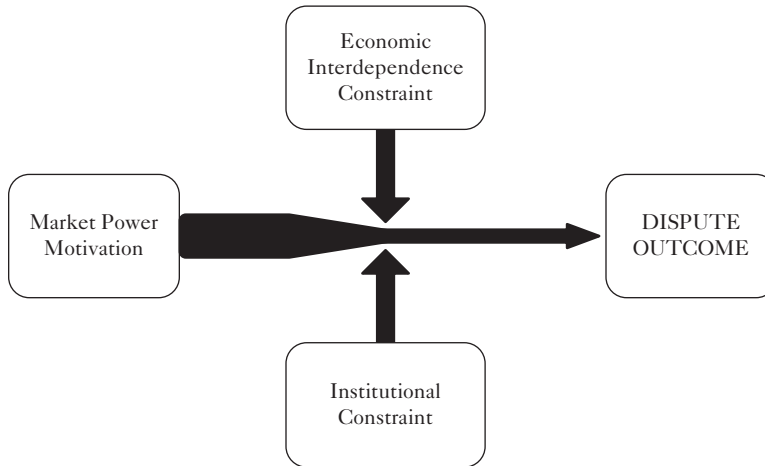
C1.S8

A Model of Market Power Politics

C1.P27

Figure 1.3 shows how these pieces fit together in our model of market power politics. When a state faces an opportunity to increase or preserve its firms' market power through the acquisition of territorial or maritime resources, it has incentives to take aggressive steps to do so. This expansionist motivation can create or exacerbate a property rights dispute between two or more states. The decision to

23. North 1990; Ostrom 1990.



C1.F3 **FIGURE 1.3.** Model of market power politics.

escalate these disputes is conditioned, however, by economic and institutional constraints. The economic constraints emerge from any interdependence that exists between the economies of the disputing states. These constraints can provide friction to slow down the dispute and limit one or more states' abilities to use force to obtain the market power opportunity. International institutional constraints work a bit differently. They can sometimes provide a similar friction if the structure of the institutional membership allows. However, their primary role is to provide more efficient, nonviolent pathways for states to resolve the dispute.

The outcome of the property rights dispute depends upon the combination of motivations and constraints that the states face. When economic and institutional constraints are low and the benefits of market power opportunities are high, states will be more willing to turn to violence. This can lead the dispute to escalate to war. Iraq's invasion of Kuwait in 1990 to gain the ability to affect oil prices provides a clear example of this path. At the other extreme, when disputants face significant constraints, they will be more willing to turn to peaceful dispute settlement. If there is a high level of economic interdependence and strong institutions can facilitate a mutually beneficial agreement, the economic benefits of resolving a property rights dispute may outweigh the potential gains from aggressively pursuing a market power opportunity. In these cases, we expect that disputants will likely agree to negotiated settlements or pursue legal dispute resolution through an international courts or arbitration panel.

In between these extremes, states with expansionist motivations may face a mix of strong and weak constraints. For example, a state may be economically dependent upon its rival but not find any of the available institutional settlements

politically acceptable. Such a state would be constrained from violence but would also be unwilling to agree to peaceful dispute settlement. In these situations, the state may instead opt to pursue strategic delay. This delay strategy could allow the state to wait until it is in a better bargaining position and take advantage of the market power opportunity at that point. Alternatively, delay could provide the state with an opportunity to gradually expand its territorial reach through gray zone tactics. Such strategic delay characterizes the activities of China in the South China Sea and Russia in Georgia and Ukraine.

C1.P30 Thus, the interplay between economics, institutions, and expansionist behavior in international relations is multifaceted. The existing academic literature largely focuses on the pacific effects of economic exchange and international institutions, but this is only part of the story. While interactions in global markets can increase the costs of fighting, the desire for increased power in these markets can motivate countries to expand their territorial reach. Similarly, strong institutions can help countries effectively resolve disputes over property rights, but they also limit the range of potential settlements and raise the stakes of any agreement that is reached. Only by taking these competing incentives into account can we understand the varying strategies countries take to pursue their economic ambitions.

C1.P31 This helps us to solve the puzzles outlined in the preceding sections. Increased economic interconnectedness and institutional developments have indeed helped to reduce the propensity of the large-scale territorial wars of previous centuries, but motivations for territorial expansion have not gone away. Among these motivations is the desire for increased power in global and regional markets, which can sometimes outweigh the economic benefits of settling disputes over international boundaries. In some cases, countries are able to resolve property rights disputes that arise from market power motivations through international institutions. However, when major powers in this economically interconnected world are constrained from using violence and cannot reach their market power goals through an institutionally prescribed settlement, they instead turn to gray zone tactics. Pursuing a strategy of delay, these countries use these tactics to try to shift the strategic environment in their favor and gradually achieve their expansionist goals over time.

C1.S9

Contributions of the Book

C1.P32

In this project, we set out to understand some emerging patterns in the conflict behavior of key players on the global stage, and we find that an important piece of the puzzle lies in disentangling the economic and institutional incentives that these countries face. For this reason, the discussion in this book cuts across many of the established research communities within the field of international relations,

from conflict and security studies to international organization to international political economy. The contemporary academic environment encourages and values specialization, and this has undoubtedly led to a great accumulation of knowledge that has pushed the study of international relations forward. As a consequence, though, these separate research communities have fewer and fewer opportunities to speak to each other. We believe that this can hinder our ability to tackle many of the pressing issues that we face in international relations today, which often requires us to take a broader perspective. For that reason, our research necessarily draws from and speaks to a wide range of literatures in the field. We briefly highlight three examples of that dialogue here, leaving a more extended discussion of the contributions and implications of this research to the book's conclusion.

C1.P33

First, we provide new insights into the relationship between economics and international conflict. Scholarship in this area has largely focused on whether trade and economic interdependence reduce the likelihood of war. Following in the footsteps of Immanuel Kant, proponents of the liberal peace argue that trade dampens the prospect of international conflict.²⁴ Others challenge this claim, arguing that the relationship between trade and war is logically indeterminate or at least more complicated than a simple negative relationship.²⁵ Here we show that a different economic incentive—the desire for market power—can be an instigator of conflict. However, we also build upon the insights of the literature on the liberal peace by integrating the constraining effects of economic interdependence into our theory to identify contexts where competition motivates conflict but interdependence constrains one or more parties from escalation to war. By exploring the market factors underlying strategies of territorial expansion, we shed light on the critical nexus between territory, trade, and war.²⁶

C1.P34

Second, we provide a unique analysis of the role of institutions in the context of territorial disputes that coincide with market power opportunities. In so doing, we reveal the pernicious incongruence between promoting efficiency and avoiding market power ambitions. The existing literature tends to focus on the ability of international institutions to help states efficiently resolve disputes.²⁷ However, we show that the development of such institutions can have

24. Polachek 1980; Russett and Oneal 2001.

25. Barbieri 1996; Chatagnier and Kavaklı 2015; Crescenzi 2005; Gowa 1995; Morrow 1999.

26. Schultz 2015.

27. In the context of property rights disputes, examples include Allee and Huth 2006; Gent and Shannon 2010; Huth, Croco, and Appel 2011; Mitchell and Hensel 2007; Powell and Wiegand 2014; Simmons 2002.

unintended consequences. In particular, institutions can constrain disputants to such an extent that they may be unable or unwilling to reach a dispute settlement. Many international institutions developed in the twentieth century were designed to add efficiency and transparency to international interactions. This focus on efficiency often comes at a price, however, if these institutions are unable to accommodate attempts to reshape markets. As a result, these institutions provide suboptimal solutions for disputing states when market power opportunities exist.

C1.P35 Third, our analysis of strategic delay in economically motivated territorial disputes provides a new understanding of the factors that lead countries to pursue gray zone strategies that lie between traditional diplomacy and war. Both experts in and practitioners of US national security policy have cited the emergence of gray zone campaigns as a critical concern in the contemporary global environment.²⁸ However, while the “gray zone” may have become a buzz word in Washington, the academic community has somewhat lagged behind in investigating these phenomena. Recently, international relations scholars have begun to put more theoretical rigor into our understanding of gray zone strategies.²⁹ Our research aims to contribute to the emerging literature on gray zone tactics by examining the economic motivations that can underlie the decision to turn to these tactics. Additionally, we show how the structure of international norms and institutions may be unexpectedly encouraging the pursuit of gray zone campaigns. Thus, our research on the strategic delay tactics pursued by Russia and China will be of interest to academics and policymakers alike.

C1.S10 *Overview of the Book*

C1.P36 The remainder of the book is primarily laid out in two parts. In Part I, consisting of Chapters 2 and 3, we lay out our theory of market power politics. Here we explain how market power motivations, in combination with economic and institutional constraints, influence countries’ strategies in territorial disputes. In Part II of the book, we explore how these factors play out in the empirical world. In these chapters, we trace how market power motivations led to armed conflict between Iraq and Kuwait, expansionist gray zone tactics by Russia in neighboring Georgia and Ukraine, and strategic delay in the maritime disputes in the East and

28. Brands 2016; Green et al. 2017; Mazarr 2015.

29. Altman 2017; Altman 2018; Cormac and Aldrich 2018; Green et al. 2017; Lanoszka 2016; Mazarr 2015; Tarar 2016; Zhang 2019.

Introduction

17

South China Seas. We then conclude with a discussion of the implications of our research for both scholars and policymakers.

C1.P37

Chapter 2 sets the stage for our theory of market power politics. Before we can analyze how the desire for market power can drive states to seek big changes in international relations, we must first map out the way things work in what we call *normal economic exchange* environments. In such environments, economic exchange takes place in perfectly competitive markets where both buyers and sellers are price takers. Whenever this characteristic holds, states have an interest in using institutions to maximize coordination and efficiency. These international institutions facilitate global commerce by reducing the transaction costs that political and economic actors face.

C1.P38

Territorial and maritime boundaries promote economic production and trade by establishing and clarifying property rights between states. International property rights disputes arise when states disagree over the sovereign control of territorial and maritime resources. Resolving these disputes can provide significant mutual economic benefits to the states involved, but it is often difficult for states to do so on their own. In normal economic exchange environments, international institutions can help resolve these territorial and maritime disputes by providing rules for allocating property rights and procedures to reach durable settlements. We illustrate the process of institutional management with a brief discussion of the resolution of the maritime boundary dispute between Romania and Ukraine.

C1.P39

In Chapter 3, we establish an argument for why property rights disputes that contain market power opportunities are particularly difficult for institutions and states to navigate, leading to interesting and important outcomes such as strategic delay and even the onset of war. To understand the emergence of war or delay in these disputes, we need to understand why states would be motivated to engage in non-cooperative behavior. One such motive is economic competition. When states are faced with an opportunity to achieve a significant increase in market power through the acquisition of territorial or maritime resources, they may have incentives to use force to seize the territory in question. This can lead these disputes to escalate to military conflict.

C1.P40

However, while states may have motives to achieve market power through violence, they are often constrained from doing so. We identify two forms of international constraints that shape decisions to pursue market power opportunities: economic interdependence and international institutions. When one state is economically dependent upon another, it is unwilling to incur the economic costs that would result from an escalation of conflict. Additionally, as we discuss in Chapter 2, institutions can help states effectively resolve disputes. However, when institutional rules and procedures prevent states from achieving market power opportunities, the same factors that make these institutions so effective

can sometimes deter states from pursuing institutional solutions in the first place. When considered in tandem, the set of constraints created by economic interdependence and incompatible international institutions can help us understand when and why states seem to wait in a holding pattern we describe as strategic delay. Such a strategy allows states to bide their time until they are able to resolve property disputes in their favor or engage in gray zone tactics that allow them to gradually achieve their market power goals.

C1.P41 Chapter 4 begins Part II and transitions the book from theory to empirical evaluation. Here we explain and justify our empirical strategy and case selection. First, we explain the motivation behind our use of qualitative cases as plausibility probes. Next, we outline the criteria that we use to select our cases. In particular, we focus our attention on hard commodity markets and limit our analysis to states that have significant control over their firms in these markets. We then introduce our three empirical foci: Iraq's invasion of Kuwait in 1990 and its desire to become a price setter in the global oil export market; Russia's territorial expansionism and contestation in Georgia and Ukraine as a result of its desire to preserve Russian market power in the regional natural gas market; and China's extended territorial expansionism in the South and East China Seas in the context of competition over seabed resources, including rare earth elements.

C1.P42 In Chapter 5, we examine how a desire for market power led to the decision of Iraq to invade Kuwait in August 1990. This case highlights the use of force to improve Iraq's position within the global oil market at a time when it desperately needed new resources. The existing institutions governing oil export revenue, such as the Organization of the Petroleum Exporting Countries (OPEC), could not provide effective solutions for Iraq's needs following a decade of war with Iran. Given the absence of normal political solutions, Saddam Hussein explored the annexation of Kuwait and its oil reserves. This opportunity to improve Iraq's oil position worked in tandem with the classic commitment problems that plague international bargaining environments, leading to conflict. Kuwait was able to fend off the attack only with the help of the world's major oil consumers, who stood to lose from Iraq's increased market power. The United States and its partners feared that Saddam Hussein's pledge to not invade Saudi Arabia was not credible, and the subsequent shift in market power for Iraq in the event of seizing Saudi oil reserves would represent a major transition for Iraq to a price setter for global oil.

C1.P43 The Coalition of the Gulf War formed and successfully expelled Iraq from Kuwait's borders. But even after Hussein learned that the United States and Operation Desert Storm would successfully compel his forces back home, he maintained his strategy of using force to revise Iraq's competitiveness in the oil market. In the wake of the initial conflict, when Iraq made a hasty withdrawal,

Hussein's army endeavored to irrevocably alter the competitiveness of Kuwait by dismantling the Kuwaiti oil infrastructure. This destruction was economic warfare by Iraq. While Hussein's first preference was to horizontally integrate this infrastructure and resources into the Iraqi economy, his second preference was to destroy it. Compared to leaving Kuwait intact, this option had the potential to improve Iraq's power in the oil market. The sanctions imposed by the international community in the wake of the war likely undid any of this advantage, but Hussein could not have predicted these costs accurately. As such, this case represents the causal path from market power opportunities to war.

Cl.P44

In Chapter 6, we explore how market power incentives in the regional natural gas market have shaped Russia's foreign policy activities since 2000. Russia is the largest exporter of natural gas in the world, and the Russian economy is largely dependent upon the production of hydrocarbons. Most of Russia's gas exports flow to Europe, and Russia would greatly benefit if it could monopolize Europe's consumption of natural gas and thus control the regional market price for gas. This would give Russia the ability to extract rents and use its price-setting capability as a lever for political gains. However, Russia's position in the European gas market is threatened by a number of factors, including the politics of transit states, the emergence of competitive suppliers, and changes to the pricing structure of European gas.

Cl.P45

In light of these challenges, Russia has pursued a multipronged strategy to maintain its market power. Part of this strategy involves moves by the Russian gas company, Gazprom, to increase its control of the supply chain through vertical integration and the construction of bypass pipelines. However, most importantly for our discussion here, Russia has also pursued a policy of territorial expansion in Georgia and Ukraine to achieve its market power goals. By increasing its presence in the breakaway regions of South Ossetia and Abkhazia and engaging in a gradual "creeping occupation" of territory in Georgia, Russia has moved to destabilize a critical transit state for gas exports from Azerbaijan. On the other hand, Russia's annexation of Crimea and intervention in eastern Ukraine have opened up additional offshore gas reserves in the Black Sea and have disrupted Ukraine's ability to increase its own domestic gas production. In these disputes, Russia has largely pursued strategic delay, which has allowed it to gradually expand its territorial reach through salami tactics. Economic interdependence constrains Russia from pursuing significant military escalation, and international institutions do not provide a viable avenue for Russia to achieve such territorial gains.

Cl.P46

In Chapter 7, we turn our attention to the ongoing property rights disputes in the South and East China Seas. Over the last half-century, China has increasingly invested in its ambitious territorial and maritime claims in both the East and South China Seas. By making and pressing these claims, China has entered

into prolonged disputes with Japan, the Philippines, Vietnam, and other states. An ability to gain exclusive rights to mine the deep seabed in the East and South China Seas would preserve China's current power in the rare earth elements market, ensuring that China will have steady and affordable access to these minerals for its downstream economies focusing on high-end electronics manufacturing and green-energy infrastructure. Preserving this market power is key to reducing risk as China pursues its "Made in China 2025" economic policy. With the International Seabed Authority's recent development of a mining code that prioritizes the environmental concerns surrounding deep seabed mining for rare earths, China is reluctant to cede authority to this international institution.

C1.P47

Yet, full throttle territorial expansion has been slow to arrive in the South China Sea, and China has shown little indication that it seeks to force the issue with Japan in the East China Sea. Asymmetric economic interdependence between China and its South China Sea rivals prevents the Philippines and Vietnam from escalating their territorial disputes militarily. Without fear of escalation, China has pursued a practice of strategic delay in which it resists conflict resolution by international regimes and slowly but determinedly moves to consolidate *de facto* control of the South China Sea through salami tactics. Similarly, in the East China Sea, both China and Japan have pursued a practice of strategic delay. As China has become emboldened in the last decade, Japan has used the combination of economic and institutional constraints to prevent the resolution of this dispute in China's favor, which could lead to a spike in Chinese market power. Japan's key role as a trading partner and contributor of foreign direct investment prevents China from escalating to more aggressive tactics, while the design of institutions such as UNCLOS makes legal dispute resolution too risky for either side.

C1.P48

In the concluding chapter, we return to our theoretical road map and the broad strokes of our empirical analysis to examine the contributions of the book and the lessons it offers for scholars, students, and practitioners of world politics. To complement our extended case studies of violence and strategic delay, we provide a brief discussion of Russia's decision to abandon strategic delay and agree to a settlement of the long-running dispute over the Caspian Sea. We also outline a set of questions for future research on market power politics. Then, to reflect upon how our research informs our understanding of international relations, we contemplate the effects of market structure on conflict behavior, the limitations of international institutions, and the future role of gray zone tactics by countries like Russia and China. We conclude the book with a discussion of some of the policy implications that follow our study of market power politics.