

Global Financial and Structural Implications of the Ukraine Crisis

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Abstract: Russia's annexation of Crimea and the subsequent bloodshed in eastern Ukraine fundamentally have altered the relations between the East and the West far more than events in the Middle East. Western levied sanctions on Russia reflect the deepest plunge in U.S.-EU-Russian relations since the Cold War. Russia neglected the West's warning and continues to undermine the peace in eastern Ukraine. Facing high tensions from the West, Russia now bids to take its business east. The emerging China-Russia economic coalition for the first time in history creates a link between very large and militarily powerful developing economies whose market power and overall productivity may well surpass that of the G7. Realist and Rationalist agree that such shifts among economically powerful entities pursuing different policy goals may cause serious confrontation, but the implications of anticipated structural paradigms differs fundamentally. Focusing on Eurasia, we estimate the likely economic and political effects in the near and more extended future for Russia. Then we analyze how sifting political alliances may affect the short-term and long-term power shifts that alter relations among great powers. Finally we summarize the effect of conflicting policy implications derived from alternate realist and rationalist power distribution paradigms.

Key words: Russia; Ukraine crisis; economic sanctions; armed conflict; economic growth; global restructuring, power dynamics; forecast

JEL codes: F01, O10, O52

1. Introduction

Following the fall and the formal dissolution of the USSR on December 26, 1991, most international observers anticipated a period of peaceful reconciliation and the emergence of new opportunities for cooperation between East and West. These expectations, never fully realized, were shattered by Russia's annexation of Crimea. This paper provides a theoretical and empirical assessment of economic and political implications of this severe downturn. We argue that the continuing crisis in East Ukraine marks a fundamental change in world politics that for the first time since the end of World War II has the potential to generate a massive confrontation among the great powers by midcentury.

We apply a rationalist and realist perspective to assess the likely political and economic implications

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expected to evolve over the coming decades. This paper is important for several reasons. First, despite resulting relatively minor number of casualties compared to the losses incurred in the continuous and severe violence that is wrecking the Middle East and for that reason dominates current news, the Ukrainian crisis is far more dangerous to global stability. The reason is that unlike conflicts in the Middle East and Africa that are regional in nature and affect relatively small portions of global commerce, output and population; the Ukrainian crisis involves Eurasia. This land mass has the largest concentration of population, trade and output. For that reason, major challenges in this area preceded previous global wars - starting with the French Napoleonic wars 1815 and ending with World War I and II. In modern history, all global wars were waged by nations that attempted to control Eurasia. We will show that the Ukraine has the potential to alter global stability that the economic consequences of the Ukraine crisis are profound and may well determine whether control of Eurasia will be determined by confrontation or cooperation.

Second, the Ukraine poses serious economic challenges to Russia. While most policy analysts concentrated on the short term military and strategic consequences of the Ukraine crisis, just as important are the hidden economic consequences. We focus first on Russia that has seemingly gained the upper hand with the invasion of Crimea, but now faces very severe economic challenges. The economic collapse and isolation from the West has long term consequences that not only affect Russia's population but motivate a major restructuring of the international system.

Finally, We focus on alliance shifts resulting from the Ukrainian crisis and on events that will follow as Russia is shifting economically and militarily from the West to the East. This tectonic shift has generated uncertainty regarding short-term and long-term alliance commitments. Russian-Chinese relations undoubtedly are entering a new stage. We will assess the consequences using the historical record.

Our argument is organized as follows. Section 2 outlines the international interactions from the competing perspective of realist and rationalist perspectives. We show that assessments provided by these competing perspectives are at seriously at odds. We then explore how the Ukraine confrontation affects political alliances, and what it might mean for the future as power shifts lead to a global restructuring. Section 3 focuses on the effects of the Ukrainian Crisis on the Russia's economic performance for 2015-2017. Our findings demonstrate that in the next two years Russia that was finally emerging from the collapse of the USSR is likely to experience a massive slowdown in economic growth. The US and the EU's are expected to maintain restrictions against Russia as the crisis migrates to other contested regions including the China Sea and the Middle East. Section 4 provides a comparative assessment based on the empirical work in the preceding section. We find that prospects of Russia joining the EU are no longer on the horizon. Instead, Russia is shifting East thus becoming more dependent on China and at the same time more dissatisfied with the workings of the international system. Section 5 uses previous deductions to show that the realist and rationalist perspectives provide contradictory answers to whether the major shifts in Eurasia will lead to war or peace. Using such arguments we outline the logical policy implications that follow.

2. Realist and Rationalist Perspectives

Our first task is to isolate the differences between power distribution realist and rationalist structural perspectives. Broad arguments from realism and rationalism are used to assess the consequences of the Ukraine crisis because these two platforms have a long theoretical and empirical record widely used by policy makers who

seemingly apply these perspectives in real time. Structural power distribution propositions share the general assumption that nations maximize net gains, but provide differing accounts of the consequences of major shifts in power distribution. Balance of Power and Power Transition arguments offer clear, logical and empirically supported propositions that provide consistent but opposing perspectives on the prerequisites for a global conflict.

Realists argue that a *balance of power* where two relatively equal groups confront each other will induce peace. Just as the Cold War remained stable a New Cold War between East and West will enhance peace as the cost of war rise and become unacceptable (Waltz, 1989; Mearsheimer, 2001). Rationalists linked to the *power transition* perspective counter that unless current trends are reversed, the emerging *power parity* will create favorable conditions for global conflict. A dissatisfied Russia-China alliance supported by many developing nations, on the one hand, is likely to confront the satisfied *status quo* US and the European Union alliance supported by the more advanced societies, satisfying the precondition for war (Organski, 1958; Organski & Kugler, 1980; Tammen et al., 2000). Let us develop these arguments a bit more.

Realist theories are built on the assumption that the international system is defined by anarchy. No higher authority sits above states. States are portrayed as self-aggrandizing players in a Hobbesian jungle that exist without a constraining rule of law (Waltz, 1979). They pursue their own interests and make decisions based on net gain assessments, as in one-shot prisoner's dilemma games. The primary motive of nations is to survive. Realists portray the interactions among states as brutal struggles for self-preservation and sovereignty. In this anarchy environment, nations act to sustain the *balance of power* that maximizes the costs of conflict and indirectly preserves peace. When the balance is achieved, states are in peace. If not, wars occur. In the absence of a central authority to punish malefactors, or institutions that can impose agreements, no individual actor can maximize its own long-term welfare by building trust and mutual relationships with others. Only high human and economic costs of the war can prevent future wars. The Realist narratives each party's decision following the Ukraine Crisis could be effectively anticipated. Russian President Vladimir Putin was not satisfied with NATO's expansion to Eastern Europe and then to the Baltic nations. The West's grand desire "to move Ukraine out of Russia's orbit and integrate it into the West" was a growing threat (Mearsheimer, 2014). Following realist anarchy arguments agreements are meaningless. Thus, fearing the menace from an expanding EU influence, Russia openly violated the 1994 Budapest Memorandum on Security Assurances that "included security assurances against the threat or use of force against Ukraine's territory or political independence" (Ashley Luer, 2014). Annexing the Crimean region was a simple cost benefit calculation made by Putin to preserve Russia's sphere of influence. The EU and NATO were thus prevented from creating a direct threat to Russian security interests'. Supporting their case, Realists note that Russia's leader Putin repeatedly emphasized that his ultimate goal was to restore the *balance of power* in Eurasia and reestablish Russia as an equal partner in world affairs¹.

A very different assessment based on the same events emerges from the Rationalist perspective. Power Transition proponents offer a different vision from the realists because they reject the assumption of anarchy. Instead, Rationalists argue that nations, while still seeking to maximize their net gains, interact with each other based primarily on their relative commitment to the status quo and the trust built among parties. The outcome is conditional anarchy where the trusted partners that agree on common norms seek to maximize joint gains while

¹ Robert Legvold wrote, "Putin believes that by annexing Crimea, he rectifies what he sees as the historical injustice of 1954, when then Soviet leader Nikita Khrushchev transferred the peninsula from Russia to Ukraine, then a Soviet republic." This is a first step to reassemble the lost USSR, available online at: <http://www.voanews.com/content/what-prompted-putins-annexation-of-crimea/1879884.html>.

distrusted antagonists that do not share common norms and distrust each other interact in anarchy. Along the status quo continuum, commitment to the *status quo* enhances trust. Actors act rationally and are aware of the potential costs of war. Allies choose the benefits of mutual cooperation when they share common norms and trust commitments. On the other hand, actors persistently dissatisfied with the status quo increasingly distrust each other, choosing war to settle disputes (Organski, 1968; Organski & Kugler, 1980; Kugler & Lemke, 1996; Werner & Kugler, 1996; Lemke, 2002; Tammen et al., 2000).

The Rationalist narrative indicates that the United States and EU were outraged by Russian actions in Ukraine and specifically the annexation of Crimea that violated Ukraine's territorial integrity secured in the 1994 Budapest Memorandum. This is particularly so because the West pressed the Ukraine to fulfill its commitments to divest of nuclear weapons and officially accede to the NPT as a non-nuclear weapon state on December 5, 1994. This step was the pre-requisite for the implementation of security guarantees required for the ratification of the START treaty that Russia and the United States agreed to. The annexation of Crimea was a historical turning point, which, followed by military actions in eastern Ukraine, and suspended the West's cooperation with Moscow. Recall that in 1998, the United States and the European Union invited Russia to join the Group of Seven (G7). This major step recognized the prominent role that Russia could play among the top industrialized and highly developed democracies despite its temporary economic decline. Relations with the West improved further in 2012, after 19 years of tortuous stop-start negotiations, when the World Trade Organization (WTO) officially welcomed the Russian Federation to join the organization as its 156th member. Russia was finally granted the right to have a say in global trade forums. All parties anticipated that admitting Russia would get the country international prestige, enhance its economic and political interactions, and adhere it more closely to the West. Following the Crimea crisis any chance of Russia joining the EU or NATO has dissipated. Instead because of the increasing dissatisfaction and shift of Russia towards a more assertive China the preconditions for a major conflict are on the rise.

3. Theoretical Structures Supporting Alternate Propositions

Here we briefly explain how global conflicts may emerge based on these contrasting perspectives. The great disparity in economic growth, population, and political developments constantly alters power relations among nations, which at times alters relative power and generates over time new balance of power and power transitions conditions among key contenders. Figure 1 contrasts the key implications of described by balance of power, and the three alternatives emerging from a power transition dynamics.

Figure 1 summarizes the logical set of power relations between major powers identifying the conditions under which nations decide to engage in conflict or preserve peace. In Figure 1 the Y axis represents relative capabilities. The X axis indicates time changes. The solid line represents nations committed to the status quo. Such actors *trust* other solid actors. The dashed line stands for nations that do not support the *status quo*. Such actors distrust all opponents. While Condition 1 alone defines the powerful and parsimonious implications of A Balance of Power, all three conditions are required to summarize the Power Transition perspective. Note that the two arguments meet at the anarchy where the *power transition coincides with the balance of power* but imply very different outcomes.

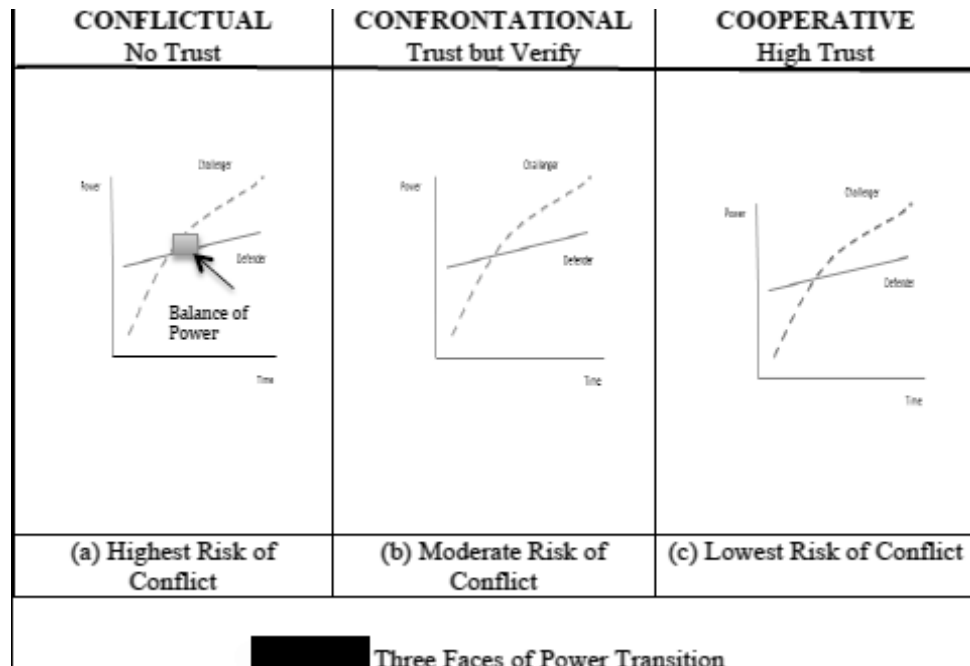


Figure 1 The Balance of Power & the Three Faces of Power Transition

From the realist perspective only Condition 1 is of interest. In anarchy, under a balance of power the costs of war are maximized and the likelihood of conflict is minimized. Simply, all actors wish to reduce their own costs. Conflict is initiated when one side or alliance is preponderant and has realistic expectations of success at relatively low cost. The current status quo has no role to play in this decision. This powerful cost benefit analysis is parsimonious and very effective. Extensions of this argument in the nuclear era are the basis of Mutual Assured Destruction (MAD) widely assumed to have prevented a global confrontation during the Cold War (Brodie, 1946; Waltz, 1980).

From the rationalist perspective Condition 1 is only one of three potential environments that account for peace or war but more importantly a balance does not lead to peace but is the precondition for war. A national commitment by contenders to the status quo determines when nations choose war or negotiations to resolve disputes. Recall that Rationalists argue that the dominant power establishes the *status quo* within a hierarchy and then persuades other satisfied nations to join the rules and norms adopted. Within each satisfied hierarchy, stable rules insure smooth economic and political transactions. Within that hierarchy, dissatisfied countries advance different norms and values and do not agree with existing rules but seek to change them. A challenger dissatisfied with the existing status quo will seek to alter norms frequently but will only confront the dominant nation as power parity is achieved. Unlike the balance of power, therefore, power transition argues that balance of power does not insure peace but is a necessary prelude to global war.

Adding satisfaction to the calculus of war produces the three extreme scenarios along this continuum. Condition 1 shows under parity and anarchy, nations will choose war not peace. At the global level bilateral dissatisfaction with the status quo consistent with anarchy is very rare and very temporary but when present should lead to conflict. Condition 2 shows the typical interactions between a dominant satisfied and dissatisfied challenger. Empirical work shows that this is the condition when conflict is used to resolve disputes half of the time but peaceful interactions are equally likely (Werner & Kugler, 1996). If the rationalist view is correct, one

reason why realists attribute peace to equality may well be that parity leads to global war when the challenger is dissatisfied. Otherwise, a balance produces peace when the status quo jointly adopted. Finally Condition 3 explicitly distinguishes rationalist from realist. When the preferences of two contending nations are aligned they will cooperate and seek to preserve the status quo. The European Union is an obvious example.

In the rest of this paper we assess the interactions anticipated by balance of power and the dynamics of power transition to estimate the likelihood of a global cooperation or conflict. This work has practical implications because the realists and rationalists, despite a shared focus on distributions of power advocate conflicting strategies to preserve peace. The realists quietly welcome the ongoing restructuring of the China-Russia coalition. They believe it may attract other developing nations and help reestablish a *balance of power and preserve peace*. On the contrary, the rationalists argue that such a shift is of a serious concern because the ongoing crisis in Ukraine for the first time since World War II set in motion the preconditions for a global war in Eurasia. Unless cooperation is reestablished among the nuclear giants, there are high chances that a *severe military conflict will take place when a balance of power (parity) once more emerges* among the major contending alliances by mid-century. Recall that the spark for the conditions of war and peace is connected to the economic performance of large nations. Russia — like Austria-Hungary prior to World War I — is not the largest among the contenders but has provided a crisis that has the potential to escalate beyond a limited confrontation between Russia and Ukraine. We thus review the economic implications of this crisis for Russia.

4. Economic Implications of the Ukraine Crisis

In this section, we will outline out possible economic scenarios for Russia for the next couple of years. As you know, at the start of 2014, Russia was already suffering from weak economic growth due to the ongoing crisis in Ukraine and Western sanctions. But a 50-percent drop in the global oil prices put even further strain on the Russian economy. Official data shows that in 2014 the real GDP grew by only 0.4 percent. Inflation hit 16.2 percent at the beginning of 2015, the highest level since 2008. The ruble has slipped to record lows against the dollar and euro, losing more than half of its value. Rising inflation forced the Russian central bank to increase the federal funds rate up to 17 percent in December 2014. Russia's embargo on food imports from Western countries boosted prices for foreign products substantially. Russia's economy faced rough times and will continue to do so. Economic estimates of Russia's show a rather bleak picture of the post Ukraine performance (For details see Tuzova & Quayum 2015).

As shown in Figure 2, the Russian economy is currently experiencing a slowdown due to the fall in the price of oil, economic sanctions, and ruble devaluation. This model predicts that the real GDP (at 2010 prices) will grow at an annual rate of 0.71 percent over the next two years. In the second quarter of 2015, the real GDP is likely to contract by 2.74 percent, as many experts suggest. We expect the real GDP to fall from 125.34 billion rubles in the first quarter of 2015 to 121.90 billion rubles in the second quarter of 2015. In the third quarter of 2015, the real GDP will continue to fall and will account for 119.42 billion rubles, which is an additional 2.04 percent decrease in real GDP compared to the previous quarter. We may see a slight boost in economic activity at the end of 2015 and 2016. The real GDP is expected to jump up by 4 percent in the fourth quarter of 2015 to 124.18 billion rubles. The year of 2016 looks more optimistic, and we predict the growth of 3.42 percent a year.



Figure 2 GDP of Russia in Constant Rubles and Dollars

The estimates of real GDP in billions of US dollars provide a far bleaker picture of Russia's economic future. Indeed, judged by external standards, Russia's economy stands approximately at the same level as immediately after the collapse of the USSR. The ability to purchase advanced equipment for the oil industry or join in cooperative international ventures with Western countries has collapsed. Even if sanctions were removed, the ability of Russians to import goods is now drastically curtailed. Analysis indicates that this is not likely to be reversed soon, particularly if Western sanctions remain in place. The ruble will continue to depreciate dropping to more than 70 rubles per US dollar.

As we mentioned earlier, the financial and trade sanctions brought by the EU, US and other countries in response to Moscow's activities in Crimea are taking a toll on the economy. In retaliation, Russia banned imports of a wide range of U.S. and European food products. Replacing foreign imports with domestic production to fill the void left by sanctions but an excessive increase in defense expenses will likely stimulate economic activity only in the short term.

The decline in the value of the Russian ruble, beginning in the second half of 2014, sparked fears of a new wave of financial crisis. As the ruble plunged at the end of last year, millions of Russian consumers made panic purchases. People rushed out to buy imported cars, refrigerators, washing machines, TV sets, and other major home appliances before they became even more expensive. Thus, we think that the growth in household consumption in the third and fourth quarters of 2015 as well as in 2016 can be explained by the carry-over effect from the stimulated increase in consumer demand at the end of 2014. As for investment, the fact that the EU froze five state-controlled banks out of its capital market made it nearly impossible to send money overseas.

The security environment continues to deteriorate. Russian president Vladimir Putin added more than 40 new intercontinental ballistic missiles to Russia's nuclear arsenal in the second quarter of 2015. However, we forecast that the relief is going to be temporary as the economy continues to grapple with serious inefficiencies in factor allocation, ruble depreciation, monetary tightening, capital flight, extinguished investment, and a heightened perception of risk (Tuzova & Qayum, 2015).

The weaker ruble and Western sanctions on food imports continue to push up inflation, causing a big decline in household consumption, personal savings, and investment. Due to a big depreciation of the ruble, we expect the prices of current imports to double. As long as the Kremlin continues its intervention in eastern Ukraine, there is no reason to anticipate that the West will ease its financial and trade sanctions against Russia. The result will be further inflation.

According to IFS, the inflation rate in Russia jumped from 7.68 percent to 9.58 percent in the last quarter of 2014, as shown in Figure 3. We predict that inflation will continue to rise in the coming years. We predict that the official inflation rate will rise to 19.6 percent in the third quarter of 2015, which will certainly be above the Russian Central Bank's 4.5 percent inflation target. We think that the Central Bank of Russia will try to keep inflation under control and slow down consumer price growth. For this reason, we predict that on average the inflation rate will be around 14 percent over the next two years.

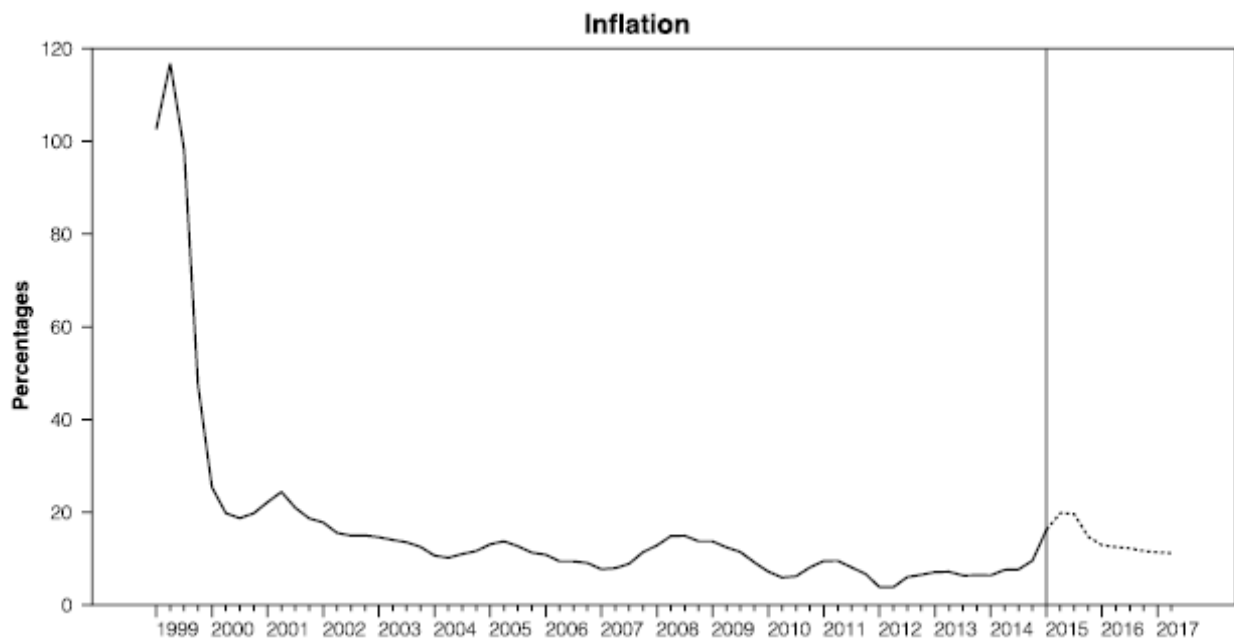


Figure 3 Inflation Rate in Russia

To earn market participants' confidence and attract investment, it is likely that Russia will lower the discount rate by switching to a floating exchange rate regime and abandoning interventions. This is exactly what happened in the beginning of 2015, when the CBR lowered the discount rate from 17 percent to 12.5 percent. None of these actions will insure a stable and welcoming environment for foreign firms to invest in the Russian economy seriously crippled by foreign capital flight.

5. Political Implications of the Ukraine Crisis

An assessment of global structures in 2000 in Figure 4 suggested following the breakdown of the USSR, Russia tittered towards neutrality and many observers anticipated or hoped for father association. Recall that in 1998 the United States and the European Union invited Russia to join the Group of Seven (G7) recognizing the prominent role that Russia could play among the top industrialized societies. Relations with the West improved further in 2012. After almost 20 years of tortuous negotiations, the World Trade Organization (WTO) officially

welcomed the Russian Federation to join the organization finally granting Russia the right to have a say in global trade forums. All parties anticipated that admitting Russia would get the country international prestige, enhance its economic and political interactions, and adhere it more closely to the West. NATO continued to consider Russia's participation as an associate member initiated at the Oslo meeting by Yeltsin and Clinton. China was building economic ties and repairing the damage that the suppression of dissent in Tiananmen Square had done to East-West relations. Figure 4 provides a short hand structural assessment of conditions in 2000.

GLOBAL STRUCTURE 2000



Figure 4 Global Interactions 2000

Assessments of satisfaction in 2000 suggested a strong link between the US and Europe as one would expect among NATO nations. The US was also overcoming strain relations with Russia during the Cold War while the latter seemed to be pushing policies that opened their constrained markets and altering the selection of leaders to a more democratic format. The large ideological gap was closing. Concurrently, relations between the United States and China, that declined after Tiananmen Square in 1989, recovered and palpable improvement could be detected in 2000.

The Ukraine crisis and the annexation of Crimea in 2014 changed these relations fundamentally. On Russia's side Putin added more than 40 new intercontinental ballistic missiles to their nuclear arsenal in the second quarter of 2015. Crimea was officially annexed to Russia in 2014 without recognition from the West while Russian troops support rebellious provinces on the eastern border continuing military pressure on East Ukraine. At the same time sanctions imposed by Europe and the US sharply limit Russia's economic performance already gravely affected by oil prices. These combined effects are driving the Russian economy into a likely depression. Military response from NATO is ongoing with military buildups, fast response contingents and deployment of anti-ballistic missiles on Russia's borders. The swift downward in the level of satisfaction among Russia and its Western neighbors is now almost at Cold War levels.

At the same time relations between China and Russia are on the rise while they deteriorate towards the United States and EU allies. In addition to the large economic agreements that secure oil exports from Russia to China, joint military exercises in the Mediterranean and the China Sea suggest a growing military coordination among these powers. Add to these recent substantive military sales agreements from Russia to China suggest growing trust and increased the level of satisfaction among these two societies. These shifts in satisfaction are taking place while China is challenging western and neutral nations in the China Sea. Relations with Japan are frail because of an unresolved conflict over a small disputed island, and China's oil exploration in the China Sea compounded by new military deployment is threatening the Philippines, Vietnam and even Taiwan. Instead of seeking internationally sanctioned accommodations, China is acting unilaterally. These events suggest that global interactions will alter as the China-Russia alliance consolidates. Below we detail likely changes in international structures that could emerge if trends persist.

FORECAST: GLOBAL STRUCTURE 2050



Figure 5 Forecast of Global Structures by Mid Century

The likely evolution depicted above will lead to substantive changes in the future. Eurasia will once more have a block that encompasses most of Western Europe and is confronted by a larger but far less developed block that covers Eastern Europe and much of Asia. The population size favors the East collation, while the output continues to favor the West with the United States until mid-century. The realists and rationalists, however disagree fundamentally about the likely consequences of such changes for the stability of the international system. Taking another view on these developments we can contrast the assessments provided by Realist and Rationalists. Figure 6 provides key elements for such analysis.

In Figure 6, along the Y axis power capabilities of the four main contenders are approximated by GDP.

Population size is measured along the X axis. The width of the bars represents the per capita output of each 14 member in these populations. Military expenditures frequently added in such comparisons are excluded because they reflect in our view response to the level of tension between these contenders and can very up and down with changes in the political climate (Kugler et. al, 2010).

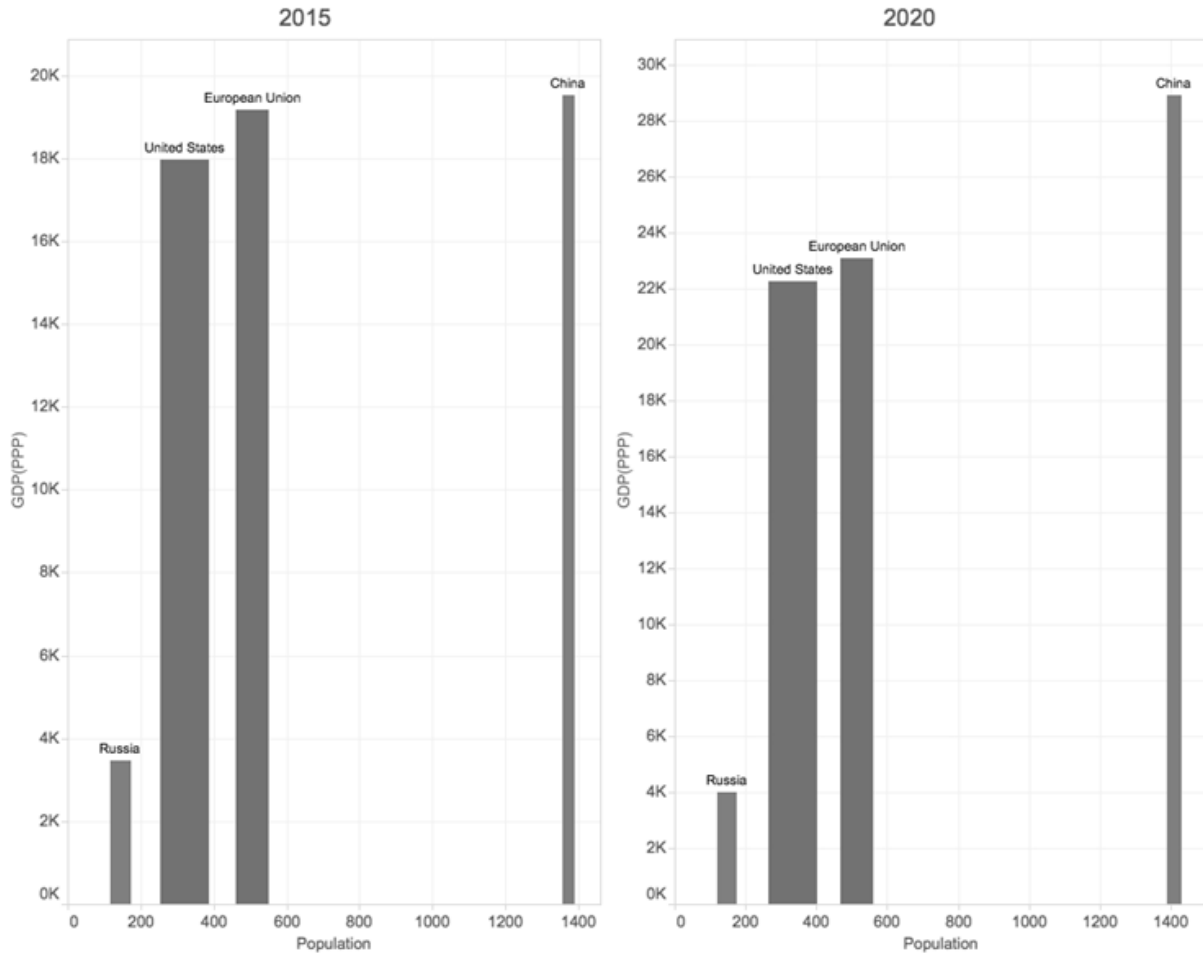


Figure 6 Contrasting East & West Contenders 2015-2020

As many observers now noted in GDP output China has overcome the United States and likely the European Union. China has and will continue to dominate all contesting entities in population. Russia is a very, very small by comparison. It is clear however if these entities are added, that China and Russia are far less capable than the United States and European Union combined to mobilize resources. Russia's shift towards China will not balance these relationships now or in 2020. A semblance of parity will emerge by midcentury but this catchup will be far different than in the past. The per capita productivity of the potential Eastern challengers is far lower than that of that of current dominant Western allies. Moreover, while China is expected to grow in relative terms over the next 15 years, Russia is expected to remain static losing ground to both the United States and the European Union.

Unless other mayor transformation take place, a balance of power in Eurasia is unlikely to occur until midcentury. Instead, the West will continue its dominance over the East. Despite arguments that a new Cold War is emerging following Russia's shift towards China it is more accurate to argue that current conditions will remain in place. Moreover if current trends persist, Russia is likely to emerge as a wassail of China — increasingly

dependent on trade, investment and the China Sea. Such events move contenders closer to anarchy and confrontation than satisfaction and cooperation.

6. Conclusions

From the realist perspective these events are encouraging. By reestablishing anarchy, China along with Russia and potentially additional relatively poor developing nations could create a collation that can catch up with the West by midcentury. While the period in between now and then is fraught with the danger of war, the reestablishment of a balance of power will reinforce stability in Eurasian and increase global security. The instability and insecurity that resulted from the emergence of the United States as the single dominant super power or as a leading partner in the western alliance with the EU will disappear. Confrontational politics in the China Sea or Ukraine are now very dangerous because the West may overreact but the underlying structural stability of the international system is strengthened by the presence of nuclear weapons. Putin's move into Crimea can in the longer term produce a far more stable environment. As the Cold War conditions reemerge the threat of conventional war will likely decline secured by Mutual Assured Destruction. In sum, while structurally the world is in peril today — the future will be far more stable than the present (Waltz, 1979; Mearsheimer, 2001; 2014).

From the rationalist perspective the most dangerous element of the Ukraine crisis is the destruction of trust between East and West. The annexation of Crimea and the continued pressure over east Ukraine have destroyed trust between Russia and Western societies, which took years to build. Western economic sanctions have set Russia on a course towards greater isolation from the West. Falling foreign investment, reduced technology transfers, and embargos on oil exports and drilling technology are likely to lead to a negative economic growth or stagnation in years to come. Such actions do not generate satisfaction and trust. The long-term political perspectives for a vibrant Russia that would join the status quo are not very attractive. Putin's actions have isolated Russia from the developed world. The chances for Russia to join the EU or even NATO discussed by Clinton and Yeltsin at the 1997 Helsinki Summit 1997 are no longer on the horizon. Recent major arms deals between Russia and China along with the joint naval exercises in the Mediterranean Sea compounded by United States increased activity in the China Sea do not reinforce stability. China and Russia are stepping up defense cooperation to offset U.S. led military primacy. The United States now has the support of the European Union concerned with stability on its borders. From a Rationalist perspective, what preserves stability is the weakness of the Challengers and forecast suggest that parity will be achieved sometime by midcentury or slightly beyond.

It is evident that realist and rationalists view similar events in a very different light. Beijing and Moscow represent a new Sino-Russian coalition highly dissatisfied with the existing status quo established by the US and EU. By midcentury parity among the contenders is likely to be approximated. If other developing countries such as India, Brazil, Argentina, Iran, Nigeria or Pakistan decide to join this coalition will overtake the stable Western group. Realist applaud the emergence of a balance of power under anarchy while rationalist view dissatisfaction and parity as the necessary prerequisites for a severe global conflict. In a nuclear world we are marching towards prolonged peace or the troubling prospect of a devastating conflict.

Given these very different perspectives on international interactions, the realist and rationalist propose almost diametrically opposed policies. The rationalists argue that the West should continue to implement sanctions against Russia in order to maintain the status quo, but should like Germany also search for an alternative, more stable solution that reignites the Russian economy and once more reduces tensions along the divide in Eurasia.

The realists, on the other hand, argue that sanctions against great powers never work. Instead, such actions lead to realignments that reestablish a *balance of power* and fortunately a cold balance of power. Nuclear weapons simply add to this stabilizing environment. Not much needs to be done.

It is up to the reader to decide which perspective should be applied to resolve the Ukraine crisis thus avoiding a future global war between east and West. The wrong choice has devastating consequences.

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