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Impact of geopolitical conflicts on countries

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Abstract:

The repercussions of the Russo-Ukrainian War, which commenced in February 2022, have prompted a resurgence of academic interest in the formulation of national strategies in the context of a conflict that has global ramifications. This paper examines post-war recovery strategies by analyzing the Russian-Ukrainian conflict, the historical precedent of World War II, and select countries' policy responses to these crises. The analysis considers both short-term measures and long-term policies, aiming to identify key factors that contribute to successful recovery and stability. Furthermore, it investigates potential strategies that governments can employ to mitigate the adverse effects of global economic downturns precipitated by volatile world situations, including disruptions in trade, energy supplies, and financial markets. This study also highlights the profound impact of interstate conflict on populations, emphasizing the need for leaders to develop comprehensive, proactive strategies that address both economic and social dimensions. By exploring these issues, the paper aims to provide actionable insights for policymakers and contribute to the broader discourse on conflict resolution and sustainable development.

Keywords: Post-war recovery; global economic stability, conflict resolution.

1. Introduction

Palestinian-Israeli conflict: The Palestinian-Israeli conflict begins on 6 October 2023.As at 1800 hours local time on 27 October 2023, Gaza: 7,326 dead, 18,967 injured, about 1,700 missing. Israel: some 1,400 dead, 5,431 injured, 229 detained. By September 12, 2024, only 17 of Gaza's 36 hospitals remained partially functional, and primary health care and community services were often disrupted due to security concerns, attacks, and repeated evacuation orders. The conflict has devastated Gaza's economy. According to a report released Thursday by the United Nations Trade and Development Organization, Gaza's gross domestic product has fallen by a staggering 81 percent [1].

Russian-Ukrainian conflict: The Russian-Ukrainian conflict commenced on February 24, 2022, and the security situation in Ukraine rapidly deteriorated in the wake of the Russian military offensive. As indicated by data from the UN News of January 10, 2024, the Office of the United Nations High Commissioner for Human Rights has verified 29,579 civilian casualties since the inception of the Russian-Ukrainian conflict. Of these casualties, 10,242 have perished, including 575 children, and more than 19,300 have sustained injuries, including 1,264 children. One month after the commencement of hostilities, the government estimated that at least $100 billion worth of infrastructure, including buildings, roads, bridges, hospitals, schools, and other physical assets, had been destroyed. The war has resulted in the complete closure of 50% of Ukrainian businesses, while the remaining half have been compelled to operate at a significantly reduced capacity. Concurrently, Ukraine will require $250 million per month to compensate for a portion of the anticipated decline in income among the 2.6 million individuals projected to experience poverty [1].

2. Impact on the Economy

About the Russian-Ukrainian conflict; as far as fiscal policy is concerned, the short-term impact of the war in Ukraine on developed economies is not significant compared with the stimulus packages during the pandemic. However, the long-term cumulative impact of the conflict is likely to be greater than most Governments have so far recognized. In Europe, for example, defense spending is likely to end up increasing by 1 percent of GDP per year or more. If that happens, the resulting costs could even exceed the ambitious €807 billion next-generation EU stimulus package during the pandemic [2]. This is not counting Europe's eventual contribution to rebuilding Ukraine, which could cost €100 billion or more [2].

Since 1989, the U.S. has reduced its military budget by 3% of GDP [2], enough to cover all of today's government spending on non-defense consumption and investment. But since the U.S. government is not proposing to invest in society by reducing defense consumption, it is safe to guess that U.S. military spending will increase at a similar rate to Europe's over the next few years.

The risk of de-globalization has also risen significantly since the Ukraine invasion. Globalization was hit as early as the outbreak of the epidemic, and as the conflict continues to escalate, Russia has become independent of the West in terms of trade. Open markets and free trade have been fundamental principles of the international order that emerged after World War II. During this period there was a broad consensus on the need to reduce the costs and prioritize the benefits of trade, which led to a deepening of the international trading system. The European Union expanded eastward and many countries joined the World Trade Organization (WTO), including Russia, the center of gravity of the former Soviet bloc. At the same time, China has shown impressive growth rates, integrated into the world market, and been recognized as a market economy through its participation in the international trading system. However, the last decade has witnessed the beginning of strong opposition to global trade integration [3].

In the short term, de-globalization will certainly have a significant negative impact on the world economy. Whether the long-term effects will be so severe is not entirely clear. Models estimate that GDP would fall by about 2-3% in the United States and possibly 3-4% in China [2]. Meanwhile the ongoing Russia-Ukraine war has had a major impact on both the stock and cryptocurrency markets. Geopolitical tensions and uncertainty surrounding the conflict have created unease among investors and increased market volatility. In terms of the equity markets, companies with significant ties to the region or heavily dependent on global trade have seen their share prices fall. In addition, disruptions to global trade flows and supply chains had an additional impact on industries, which in turn affected market performance. In the case of the cryptocurrency market, the reaction was characterized by a degree of divergence. Some investors viewed cryptocurrencies such as Bitcoin as a safe-haven asset, while others viewed them as speculative investments. However, the war and its repercussions have created more uncertainty and risk, leading to more volatility in cryptocurrency prices [4]. In conclusion, the Russia-Ukraine war has demonstrated the need to pay close attention to the geopolitical landscape and consider its potential impact on traditional and digital asset markets. It is important to recognize that the effects of war are not limited to areas of direct conflict. Disruptions to global trade and commerce can have a cascading effect on the global economy, creating additional uncertainty and volatility in financial markets. It is therefore important to recognize the impact of armed conflict on investor sentiment and to ensure that investors remain informed and prepared to deal with potential challenges that may arise during a conflict [4].

Geopolitical risks have a significant impact on investment decisions and contribute to economic growth and financial market volatility. The recent outbreak of the Israeli-Palestinian conflict in October 2023 had severe repercussions on the stock markets, global fear, and economic uncertainty. It also led to a surge in crude oil and natural gas prices due to reduced gas supplies from Israel to Europe. Gold, considered a safe-haven asset, experienced a price surge as investors shifted towards it during times of geopolitical conflict. The study found that there are substantial spillovers between oil, gas, gold, and the stock markets of Palestine and Israel, particularly in terms of volatility, skewness, and kurtosis. WTI oil and gas were identified as the main net receivers of volatility spillovers, while gold and the Palestinian stock market were the main net receivers of skewness spillovers. The Israeli stock market acted as the leading net transmitter. The study also revealed that spillover dynamics varied over time, with significant exacerbation during the COVID-19 pandemic and the Israeli-Palestinian conflict in October 2023. The findings suggest the importance of analyzing higher-order momentary risk spillovers and integrating them into portfolio construction.

World War II led to a huge increase in government spending, which was financed by debt and higher taxes. This resulted in the total debt of the United States exceeding 120% of GDP and taxes more than tripling to over 20% of GDP [5]. Although GDP grew rapidly during the war, consumption and investment fell dramatically due to government control of raw materials and supplies [5]. The war created the political will necessary to end the Great Depression by dedicating a large portion of GDP to military spending, eliminating excess capacity, and reducing unemployment [5]. However, it has been argued that similar pre-war spending on public works could have led to economic growth. The war had a significant impact on income distribution, which became more equal during the war years. The stock market initially fell but eventually rose to a higher level. Overall, financing wars can have negative macroeconomic effects, including widening budget deficits, higher taxes, and inflationary pressures. Because of the unpredictability of the outcome, duration and economic consequences of war, it is important to consider alternatives to war.

Geopolitical risks are likely to have a considerable impact on the domestic economy through a number of channels. First, during periods of high geopolitical risk, such as armed conflict, military tensions, terrorist attacks and threats of war, businesses may reduce or postpone capital expenditures. Secondly, during periods of heightened geopolitical risks, consumers may lose confidence in the economy and the government, thus reducing their desire to consume, and this reduced desire to consume will lead to a reduction in firms' revenues, and once firms' profits are reduced they will resort to ways of increasing their net profits, for example, in this case most firms will resort to cost-cutting, which is known as layoffs, and most of the leaders think that this can be a good solution to the problem, which is also the status quo of today's society, but when some people lose their jobs and lose their source of income, they naturally reduce their desire to consume, and they enter into a horrible dead end cycle, and the economic situation will only get worse and worse, so I would suggest that the government should make some actions to stop these things from happening at this time, such as the government paying to build or Repair public infrastructure such as highways, bridges, subways, which can drive a lot of industries like workers, materials. At the same time, the government can also reduce the taxes of some large companies to reduce their expenses and send people to supervise the refusal of unjustified layoffs. Third, rising geopolitical risks may erode a country's democratic credibility and investment image. During periods of military tensions, terrorist attacks and threats of war, security concerns may affect personal security, mobility and freedom of expression. This may lead to capital outflows or reduced capital inflows.

3. Policy

The next six cases can provide policy insights for governments to improve their resilience to external shocks.

Tailor policy approaches to shocks, taking into account the heterogeneous effects of war on low development countries. The size and nature of the effects vary. Evidence suggests, for example, that the impact on the total value of food consumption ranged from 0 to 6 per cent, suggesting that some countries may need to take more action than others [6]. Moreover, while some resource-intensive countries benefit from global commodity price shocks in the short term, they will be negatively affected in the long term, while non-resource-intensive countries are expected to grow faster in the medium term. In addition, countries with higher government capacity are likely to show a stronger recovery. At the same time, for some countries that are lagging behind in development, they are both vulnerable and susceptible to climate change impacts and political instability. This heterogeneity means that some countries will need to take more action than others. Like investing more of their budgets in infrastructure rehabilitation, and funding some domestic front-end companies to ensure that people's daily lives are protected, some countries will need to do more than others [6].

The objective is to facilitate the promotion of efficient domestic agricultural practices and the production of fertilizers. The implementation of measures designed to enhance agricultural productivity has the potential to mitigate the reliance on imports and the susceptibility to global commodity price fluctuations. Such measures may entail targeted initiatives, including augmented investment in agricultural and fertilizer research and development, enhanced access to contemporary and environmentally sustainable agricultural techniques and technologies, the provision of assistance to smallholder farmers, the establishment of value chains for particular agricultural products, or the implementation of comprehensive agricultural sector development strategies [6].

Concurrently, there is potential for enhancing the function of the global financial architecture in the management of economic shocks and the promotion of economic recovery. The confluence of the impacts of the Coronavirus Disease 2019 (Covid-19) pandemic and the Russo-Ukrainian conflict has constrained the availability of financial resources. Furthermore, the recent global financial crisis is leading to an increase in borrowing costs and debt servicing expenses. As of August 2023, 21 countries in Africa are at high risk of debt distress or are already in debt distress. Four countries—Chad, Ethiopia, Ghana, and Zambia—have submitted applications to join the G20 Common Framework, yet have been relatively slow to secure debt treatment. In 2020, net financing from the IMF and the World Bank represented 2.7 percent of GDP for low-income countries (LICs) and 0.6 percent of GDP for lower-middle-income countries (L&MICs). These figures fall significantly below the 2020 target of 6 percentage points and 9 percentage points of GDP growth for LICs and L&MICs, respectively.[6] This target was 6 percentage points for low- and middle-income countries (LICs) and 9 percentage points for low- and middle-income and high-income countries (L&MICs), respectively, and was thus well below the pre-Covid forecasts.[6] However, the question of direction is also of great consequence. In light of these considerations, it is pertinent to inquire as to the potential role of the IMF and the World Bank in safeguarding Africa's growth and development trajectory from the adverse effects of heightened financing requirements for targeted growth, as previously suggested in the aforementioned policy areas [6].

In the contemporary era of globalization, it is imperative for any economy to establish trade or diplomatic relations with other countries in order to ensure its survival and prosperity. However, in order to safeguard its interests in the face of unforeseen circumstances such as this war, India would be well advised to explore avenues for hedging its position. Defense supplies have constituted a significant and enduring aspect of Indo-Russian relations. Moscow has been Delhi's sole partner in the provision of sophisticated defense platforms and has even collaborated with India in the co-production of cutting-edge missiles, including the Brahmos cruise missile. Nevertheless, India has persistently expressed reservations regarding the dependability and caliber of Russian products. Prior to the outbreak of hostilities, India initiated a diversification of its defense imports, procuring defense equipment valued at approximately $30 billion from the United States since 2008. Additionally, India's trade with the U.S. has been a source of concern [6]. With regard to other trade, the relationship between India and the United States is comparable to that between India and Russia. Furthermore, the routes through Iran, Armenia, and Russia are not as reliable when attempting to expand reach to northern markets and suppliers. Consequently, New Delhi will progressively gravitate towards collaborating with nations that facilitate unimpeded access to the Pacific and linkages to the broader global network. These include the United States, Japan, Taiwan, the Gulf States, Israel, Turkey, and South Korea [6].

Concurrently, those responsible for formulating policy should give due consideration to the influence of investor attitudes on market dynamics and returns. By grasping the influence of investor sentiment, policymakers can implement measures to enhance investor confidence and attract a greater number of market participants. Investor attitudes can have a considerable impact on stock and cryptocurrency returns, particularly in periods of geopolitical instability and conflict. In such circumstances, the market value of an asset may not accurately reflect its intrinsic value due to investor sentiment, resulting in unforeseen losses for both individual investors and financial institutions. A more profound comprehension of the manner in which equity and cryptocurrency markets respond during periods of crisis is advantageous for investors. By examining the influence of volatility, investors can construct efficacious investment and hedging strategies. Furthermore, it is essential to consider the interrelationships between equities and cryptocurrencies, as well as the influence of investor behavior, when formulating portfolio adjustments to achieve risk diversification objectives. It is of the utmost importance for investors to adopt a proactive approach to risk management and diversification in order to mitigate potential losses and make informed decisions that are consistent with their investment objectives. An understanding of the impact of investor attitudes on stock and cryptocurrency returns enables investors to navigate the market with confidence and make informed decisions. Furthermore, the findings underscore the significance of incorporating macroeconomic variables and investor sentiment into the formulation of economic policies. Policymakers may wish to consider the implementation of measures designed to manage investor sentiment and thereby reduce the risks associated with market volatility. The impact of factors such as GNI, oil, CPI, and VIX on the equity and cryptocurrency markets suggests that a comprehensive range of economic indicators should be taken into account when formulating policies.

In Ukraine, policymakers have introduced a range of initiatives to encourage businesses to continue investing, including business recovery programs, subsidies for strategic industries, political risk insurance, business tax breaks, and phased improvements to digital infrastructure. Interviewees recognized the value of these initiatives, but still cited weak institutions and corruption as major obstacles. Policymakers should continue their efforts to strengthen institutions and combat corruption. On the other hand, the Ukrainian government has been very successful in its promotional campaigns and branding efforts, which have brought Ukraine to the attention of foreign stakeholders and are likely to generate support for its business community and inspire trust in its government. Our research has implications for both domestic and foreign managers. First, we find the firms we surveyed to be highly resilient. Despite the escalation of the war, continued investment suggests that infrastructure will not collapse. This is important because foreign managers are also weighing whether to continue investing. Second, interstate wars are not static events. The findings suggest the need for strategies that can adapt to the volatility of war [7]. Finally, interstate wars trigger formal and informal institutional pressures. If managers are to be able to respond to government demands on the one hand and benefit from government-supported programs on the other, they need to understand local norms and requirements. Active engagement with formal and informal institutions can help them navigate the complex regulatory and social environments that characterize countries at war [8-10].

4. Conclusion

As with other forms of government spending, military expenditure can serve as a significant source of economic demand during periods of low confidence and economic downturns. It can facilitate the advancement of new technologies, stimulate the emergence of new industries, and generate sources of demand and employment. However, there are still adverse effects, including larger budget deficits, higher taxes, and above-trend growth, which can give rise to inflationary pressures. The aforementioned effects can manifest rapidly and exert an immediate influence, or they can unfold over time through lagged effects. The macroeconomic impact of war, regardless of its financing, is typically negative. In order to gain insight into the macroeconomic impact of war, it is necessary to consider what the economic landscape would have looked like in the post-World War II era had these conflicts not occurred. In the absence of war, it is possible that taxes would have been lower, inflation would have been lower, consumption and investment would have been higher, and budget deficits would have been lower. Some wars are unavoidable, and the negative effects of not fighting them may far outweigh the costs of fighting them. However, if there are alternatives, it is prudent to exhaust them first, because once a war has begun, the outcome, duration, and economic consequences are difficult to predict.

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