FOREIGN AFFAIRS
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The Twilight of America's Financial Empire

Washington's Economic Bullying Will Erode Its Power

By Henry Farrell and Abraham Newman

When Iraqi lawmakers voted to expel U.S. forces from the country earlier this month, the Trump administration's response was swift and forceful: it refused to withdraw and, for good measure, threatened financial retaliation, saying it would freeze Iraq's accounts at the U.S. Federal Reserve.

The threat seems to have been effective. Although Iraqi officials still seethe over a U.S. drone strike that killed a top Iranian commander in Baghdad on January 3, Prime Minister Adel Abdul-Mahdi has said that his caretaker government lacks the authority to push for a U.S. withdrawal, and American troops have resumed joint operations with their Iraqi counterparts.

But that sense of normalcy is deceiving. U.S. forces were in the country at the invitation of the Iraqi government to help in the fight against the Islamic State, or ISIS. By refusing to withdraw them, the Trump administration is turning a relationship of choice into one of coercion. Just as alarming, Washington is doing so by threatening to starve its ally of critical funds, a step that could set off a financial crisis in Iraq, perhaps even economic collapse.

Washington's stranglehold over the Iraqi economy is an extreme example of a broader, worrying trend: more and more often, the United States is using its privileged role as custodian of the global financial system to coerce and punish those who object to its methods, be they friend or foe. It has slowly usurped a system intended to provide benefits to the world at large and made of it an instrument for its own geopolitical goals.

In turning financial relationships into a tool of empire, the United States follows in the footsteps of ancient Athens. The experience of this predecessor does not augur well for Washington. Athens used its financial power to abuse its allies and in doing so precipitated its own ruination. The United States risks doing the same.

THE PRICE OF ARROGANCE

Scholars of the realist school of international relations tend to think of the Athenian general and writer Thucydides as one of their own: a believer in power politics who grasped the harsh realities of statecraft. They interpret his Melian dialogue, in which Athenian conquerors tell their foes that the strong do what they will while the weak suffer as they must, as a statement of the eternal truth of international politics—great powers make war against one another to gain or to protect empires, while weak states try to survive as best they can. Yet Thucydides was not an international relations theorist—he was a historian. He was interested less in arguing that leaders had limited options to choose from than in discovering why they often chose poorly. The speeches of the victorious Athenians that he recounts should be read as a testament to the arrogance that eventually tripped the city's leaders up.

In Thucydides' telling, Athenian imperialism and hubris went hand in hand. After fending off a Persian invasion, Athens and its allies formed an association of city-states, the Delian League, to defend themselves against any Persian reprisals. To this end, each member of the league contributed funds to a shared treasury based on the island of Delos, to be administered for the common benefit. But Athens, the alliance's most influential member, did not take long to abuse its power. The Athenian statesman Pericles moved the treasury from Delos to Athens, where it was used for the city's sole benefit. The league, designed as an alliance based on shared interests, became an empire, with Athens demanding tribute from its former allies and threatening to occupy or destroy them if they failed to pay.

Athenian leaders, according to Thucydides, knew that they were alienating former allies and turning neutral states into enemies, but they saw unpopularity as the price of power. Arrogance would have its price, too. Pericles' successors, including the belligerent Cleon, faced revolt from Athens's disgruntled allies as the Peloponnesian War went on. The enemies of Athens triumphed, leading to its downfall.

WEAPONIZED FINANCE

Like Athens, the United States and its allies have created a shared treasury of sorts: the global financial system and the complex institutional arrangements that underpin it. Among them are the financial messaging network SWIFT, the dollar clearing system, and the willingness of the U.S. Federal Reserve to provide international liquidity in times of crisis. Together, these arrangements allow states to manage their wealth with unprecedented levels of coordination and safety. And like Athens in the Delian League, the United States has been the first among equals, reaping enormous benefits from its central role in global finance and from the supremacy of the dollar. Other countries, too, have benefited, including the 250 states and government financial institutions that trust the U.S. Federal Reserve to hold their money safe. The United States has provided goods for the general benefit, including a stable clearing system for financial transactions and the extraordinary "swap lines" that the U.S. Federal Reserve put in place after the global financial crisis, allowing foreign central banks to provide dollars to their weakened domestic financial institutions.

Over the last decade, however, the United States has been more and more willing to use its vast power in the global financial system for its own ends. No longer does Washington try to coerce its adversaries simply by cutting off access to U.S. firms and markets; instead, it often imposes so-called secondary sanctions, which cut off access to the global financial system itself. International banks cannot do their job without access to the dollar clearing system, which the United States controls. As a result, they are terrified of displeasing U.S. regulators, who can fine them billions of dollars or effectively shut them down. That has allowed the United States to press financial institutions around the world into service as proxy regulators who will refuse to deal with individuals, businesses, or even states that have been designated by U.S. sanctions. Weaponizing global finance in this way has become the tool of choice for the U.S. government in pursuing goals as diverse as nonproliferation, human rights, and regime change. Adversaries such as Iran have seen their economies crippled. But even European firms perceived to have flouted U.S. sanctions have had to pay billions of dollars in penalties to U.S. authorities to avoid becoming untouchable pariahs in the world economy.

In the early stages of building this financial empire, the United States at least consulted with its allies and gave them the chance to speak out against measures that affected their firms. Under the administration of U.S. President Donald Trump, however, Washington has been unwilling even to pretend to defer to allies, who receive little if any advance warning of coming sanctions that might hurt their companies or stymie their foreign policy objectives. In a growing number of cases, U.S. allies are actually the objects of U.S. economic coercion. High-ranking U.S. officials have, for instance, warned U.S. allies in Europe that they may face secondary sanctions if they try to salvage the 2015 Iran nuclear deal.

Now the Trump administration is using the same tactic to hold Iraq's economy hostage. Should Baghdad force U.S. troops to withdraw, Trump has warned, Washington will retaliate with "sanctions like they've never seen before ever. It'll make Iranian sanctions look somewhat tame." A supposed ally is quite explicitly being turned into a vassal.

THE REAL THUCYDIDES TRAP

The Trump administration believes that countries the likes of Iraq have no choice but to bend to its will: the all-important role of the dollar means that the United States is strong while others are weak. Of course, the weak will complain—that is what they always do—but the complaints of the powerless are irrelevant.

Yet Washington's arrogant belief in the inevitability of its power may end up creating the conditions for that power to crumble. Much of the United States' economic and political influence rests on the trust of foreign states and firms in the global financial architecture that it dominates. If the country is clearly not administering that system in the interests of all nations, and instead uses it as a straightforward tool of coercion, its influence will wilt away.

In fact, that process has already begun. Turkey—a NATO member and U.S. ally that in recent years has come to fear the sting of American sanctions—is working with Russia to build payment channels that allow international trade flows to circumvent the U.S. financial system. The European Union's new executive is coldly and carefully considering how best to protect the continent from both U.S. and Chinese economic aggression. Even close allies, such as the United Kingdom, are considering rejecting the U.S. demand that they block the Chinese tech behemoth Huawei from building their telecommunications networks. The dollar clearing system is unlikely to collapse, but states and nonstate actors may dig alternative tunnels of exchange that could gradually undermine and replace it. The more domineering the United States becomes, the more incentives its allies will have to resist its domination or defect just when they are needed most. And as the trust of U.S. allies erodes, so will Washington's ability to project power around the world.

U.S. financial coercion is vastly milder than the terror inflicted by Athens, which massacred and enslaved the populations of cities that rebelled against it. But Washington's methods become far more problematic if they serve to impose a de facto military occupation, as they now do in Iraq. Friction with host governments, in Iraq and elsewhere, may force the United States to deploy more troops in order to protect those already on the ground. Even for a superpower, power projection on such a scale will be too expensive to sustain.

Powerful states can build extraordinary collective goods that benefit their allies and themselves: a jointly funded defense league in the eastern Mediterranean, in Athens's case, or the vast network of relationships that underpins the U.S.-led global financial system today. Great powers also face the pitfall of hubris. They are prone to assuming that their power is a given and that they can therefore treat lesser states with contempt. As these states become more secure and arrogant in their supremacy, subtle forms of imperialism can turn into cruder ones. The missteps of a Pericles can open the way for gross and dangerous demagogues like Cleon, whose recklessness led Athens into disaster. Recent U.S. administrations built far-reaching tools for economic coercion. They never imagined a president who would use those tools to threaten to destroy the economy of a NATO ally or who would revel in how the "tremendous economic power" of sanctions allows him to do far more than "playing around with having a few soldiers shooting each other at the border."

The chronicler of Athens's downfall has given his name to the "Thucydides trap"—the idea, popularized in recent years by the political scientist Graham Allison, that war is likely whenever a rising power confronts an established one. Such was the fate that befell Athens and Sparta, Allison has argued, and it may play out today between China and the United States. But the real Thucydides trap facing Washington is less about the inevitability of great-power conflict than about the persistent temptation of imperial power. Athens's decision to turn a common treasury into a system of tribute and subjugation alienated its former allies and precipitated its fall from power. The United States may be starting to recapitulate this dismal history