

# The new age of economic warfare – and why America is playing with fire

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Moghadam Family Professor of Finance Matteo Maggiori of Stanford University is among the world's leading authorities on the international monetary system, dollar dominance and the architecture of global financial power. He says the more aggressively a hegemon wields economic coercion, the faster it erodes the foundations of its own power. PHOTO: NAZRI KAMURI

Nations have long weaponised trade and finance to get what they want. What's new is the scale, the speed and the risk of blowback.



The US national debt now stands at close to US\$39 trillion, or roughly 123 percent of GDP. Professor Maggiori says if the fiscal trajectory continues to deteriorate at this rate, the dollar dominance question will inevitably come up. While dollar dominance has historically been extraordinarily durable, it is not eternal, he says. PHOTO: AFP



Vikram Khanna

Over the past decade, economic coercion has become the foreign policy tool of choice for the world's great powers. The US has weaponised the dollar and the SWIFT financial messaging system to bend Iran to its will and cripple Russia's war machine. It has imposed sweeping semiconductor export controls on China to slow its rise as a technological power. Since 2025, it has slapped tariffs on much of

the world in pursuit of favourable trade deals. China, in turn, spent three years throttling Australia's commodity exports after Canberra called for an independent investigation into the origins of Covid-19. For years before its invasion of Ukraine, Russia held Europe hostage with its control of natural gas supplies, periodically cutting – or threatening to cut – the flow. Such behaviour has revived a

field of study that mainstream economics had allowed to atrophy: geoeconomics, the discipline that examines how hegemonic countries leverage financial and trade relationships to achieve geopolitical ends. Few people are thinking harder about these questions than Mr Matteo Maggiori, the Moghadam Family Professor of Finance at Stanford University. Winner of the Fischer Black Prize – awarded

to an outstanding financial economist under 40 – Professor Maggiori is among the world's leading authorities on the international monetary system, dollar dominance and the architecture of global financial power. "In modern economics, power is too often reduced to mean only 'market power,'" he said in a lecture at last week's meeting of the Asian Bureau of Finance and

Economic Research in Singapore. "But a sovereign or large firm is powerful in a broader sense."

In a subsequent interview with me, he was blunter about the stakes. "It's clear to everybody that for the next 20 years, we're going to live in a world where large countries like the US and China exert a lot of influence abroad. Such issues are already shaping the world. To me as an economist, this is an enormously important field."

#### HISTORY'S LONG SHADOW

What looks like a new phenomenon is, in fact, an old story. Prof Maggiori points out that economic coercion by hegemony stretches back centuries. In the 15th century, the Medici banking family of Florence exercised leverage over Renaissance Europe by controlling credit, currency exchange and financial infrastructure – the equivalent, in their day, of controlling SWIFT or the dollar system. In the 19th century, Britain used its naval superiority to force the opium trade on China and ultimately to extract the island of Hong Kong.

The post-war decades looked different – and deliberately so. After World War II, the US deployed its economic statecraft largely in a constructive way. The Marshall Plan rebuilt Europe, turning it into a massive market and a bedrock ally. Washington also designed the architecture of the world trading system around a calculated offer to other nations: join my sphere of influence and I will tie my own hands, committing to rules that limit coercion.

"Our research shows that a hegemon can benefit by unilaterally tying its own hands," Prof Maggiori explains. "If you and I have a relationship and I use my power to simply bully you, the relationship has no value to you – so you move away, and I have no power left. What I should do instead is say: come into my sphere of influence. Yes, there might be some coercion, but the deal will still be good for you."

Those rules served not only the rest of the world, but America itself.

The years from roughly 1990 to 2010 now look, in retrospect, like an anomaly. With the Cold War over, Russia diminished, and China still an emerging market, the United States was in a position of unchallenged dominance – but chose not to use all of its tools. "It's a period that looks abnormal from a historical perspective," says Prof Maggiori. "But I wouldn't think of it as the absence of geoeconomics, rather as a particular incarnation of it."

The mistake came later, when Americans began to misread their own history. Institutions like the World Trade Organization came to be framed – politically, and then popularly – as gifts to the rest of the world, rather than pillars of American power. "The US public came to believe that if it's good for others, it's not good for them," Prof Maggiori observes.

CONTINUED ON PAGE B2

## Nations already reducing dependence on US systems

FROM B1

That misreading has had consequences.

#### THE PARADOX OF POWER

Now that competition with China has intensified, the usual instruments of statecraft are back. But Prof Maggiori warns that their use comes with a paradox: the more aggressively a hegemon wields economic coercion, the faster it erodes the foundations of its own power.

"In the short run, a country might think the world is dependent on it and so it has a lot of power," he says. "But arbitrary threats and coercion dilute that power. Eventually, other countries move away." The evidence is already visible – in Europe's accelerating push for strategic autonomy, both economically and through NATO; and across Asia, where dependence on American systems is being quietly reduced.

Nowhere is this dynamic more consequential than in payments. China has built an alternative to SWIFT called the Cross-Border Interbank Payment System (CIPS). Unlike SWIFT, which is purely a messaging network, CIPS combines messaging and

settlement in a single system – which makes it more up-to-date than its Western counterpart.

"The reasons why China is putting it together are pure geoeconomics," says Prof Maggiori. "On the defensive side, they want to ensure that if they ever face the threat of being disconnected from the Western system – like Russia was – they can still sustain trade. On the offensive side, they can offer their system to other countries, allowing them to transact away from the US. This is hugely important."

Here is where Prof Maggiori's research introduces a finding that should unsettle policymakers in Washington. China currently accounts for around 2-3 per cent of global payments. Suppose that share grows to 10 per cent over the next five years. The instinctive American response might be: fine, we still control 60-70 percent. That response, Prof Maggiori argues, would be dangerously wrong.

"We argue in our work that power is non-linear. The first 10 per cent you lose in market share causes a disproportionate loss to your power compared to the next 10 per cent." The reason is threshold effects. When China

controls 3 per cent of global payments, it cannot provide enough liquidity to sustain an economy the size of Russia transacting outside the US system. But when China controls 10 per cent, it can. At that point, the ability of the US to impose meaningful financial sanctions on a country like Russia declines substantially. "This is not commonly understood in policy circles," Prof Maggiori says. "And I think China is well aware of it."

#### MANUFACTURING VS FINANCE: WHO HOLDS THE EDGE?

China is now a powerhouse in manufacturing, accounting for close to 30 per cent of global industrial output. So which form of economic power carries more global leverage: China's manufacturing muscle, or America's financial dominance?

On this question, Prof Maggiori is clear. US financial power, rooted in the dollar and the depth and liquidity of American bond markets, is very difficult to dislodge. Any country seeking to build an alternative system would need an open capital account, a credible commitment not to stop foreigners withdrawing capital in a crisis, no risk of expropriation, no threat of default and no runaway inflation. "Those are very hard conditions to match," he says.

China's manufacturing strength, by contrast, is more substitutable than it appears. Most of what China produces – with the

exception of critical inputs like rare earths – can increasingly be sourced from Vietnam, Mexico, India, and other rising industrial economies.

On semiconductors, the picture is more complicated. Prof Maggiori is sceptical of the long-term effectiveness of chip export controls. The industry is geographically dispersed across South Korea, Taiwan, China, Singapore and Malaysia, making total supply-chain control far harder than controlling a financial system. And the technology is moving fast. "The difference between a super-advanced chip and one just below it is unclear," he notes. "Are we really sure we can't do the same things with a chip that's just below the frontier? The DeepSeek shock was part of that question." So, while the US is globally dominant in AI software and information services, hardware is more contestable.

#### AMERICA'S TICKING CLOCK

Perhaps the most sobering part of Prof Maggiori's analysis concerns America's fiscal trajectory – and what it could mean for dollar hegemony itself.

The US national debt now stands at close to US\$39 trillion, or roughly 123 percent of GDP. "The fiscal trajectory has deteriorated much faster than I expected 10 years ago," he says. "It used to be a curiosity. Now it's a conversation. If it goes on like this, it's going to become an

urgent conversation." Both political parties, he notes, disagree on what to spend money on – but agree it should be debt-financed. "Nobody seems to want to run on a platform of bringing down the debt. That's not a good trajectory."

Dollar dominance has historically been extraordinarily durable – but it is not eternal. Britain lost its reserve currency status in the 1920s when it abandoned the gold standard. Other financial centres have risen and fallen before. "This is not a privilege any country gets forever," Prof Maggiori says.

**America still holds the strongest hand in the global economic order. Its financial system remains without peer, its dollar without a credible rival. But the window to reinforce that advantage – through fiscal discipline, innovation in financial infrastructure and the rule-bound multilateralism that made the US indispensable in the first place – is not unlimited.**

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The particular danger of reserve currency crises is that they arrive without warning. They are crises of confidence – sudden, non-linear, and by their nature invisible until they are already upon you. "We model them as bank runs," Prof Maggiori explains.

"Everything looks fine until it doesn't. I wish there were market signals, because they give you time to get your house in order. But sometimes that's not what happens, or it's too late." He invokes the image of a car hurtling at 100km an hour: safe, if you brake gradually; catastrophic, if you have to stop in the next ten seconds.

It is a fitting moment to recall what Rudiger Dornbusch, the great MIT economist, once wrote: "A crisis takes a much longer time coming than you think, and then it happens much faster than you would have thought."

America still holds the strongest hand in the global economic order. Its financial system remains without peer, its dollar without a credible rival. But the window to reinforce that advantage – through fiscal discipline, innovation in financial infrastructure and the rule-bound multilateralism that made the US indispensable in the first place – is not unlimited.

America's car is still racing ahead. The question is whether anyone in Washington is watching the speedometer.

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