

Geopolitics in 2022: Turbulence Ahead?

The threat of great-power competition will merge with the worsening climate crisis to produce a world of heightened national-security risks.

In my view, 2022 will present one of the most complex, unpredictable, and potentially dangerous geopolitical backdrops in decades.

Several factors drive this elevated risk, starting with structural changes in the geopolitical environment that include a more competitive world order, rising economic inequality, and political dysfunction globally. We are also witnessing the growing national-security implications of climate change.

I believe that COVID-19 will still have a lingering impact. As we saw in 2021, the pandemic tends to accelerate geopolitical shifts and help shape events in new and surprising ways by contributing to diverging macro effects, ongoing supply-chain disruptions, cyclical and structural changes in labor markets, and varying inflation outlooks. Expect all this macroeconomic uncertainty to influence, once again, domestic policies and elections.

US-China Policy: Great-Power Competition, Writ Large

Given the stakes for the global economy and for investors, the US-China relationship will arguably remain the most important geopolitical dynamic in 2022.

While both governments will likely prioritize domestic matters—COVID-19 management, the Winter Olympics in Beijing, the Chinese Communist Party's 20th National Party Congress, US mid-term elections—we can expect intensifying great-power competition to dominate the geopolitical landscape in 2022 and for years to come.

I anticipate that the US will look to deepen multilateral-security approaches in the Indo-Pacific, such as the Quad security alliance with Japan, Australia, and India. This new foreign-policy direction also includes Australia's plans to acquire advanced US nuclear-submarine technology under the emerging AUKUS security alliance, as Canberra effectively joins the US special relationship with the UK.

These significant security developments in the Indo-Pacific come amid US intelligence reports that China is rapidly upgrading its nuclear-weapons arsenal and hypersonic-missile capabilities.

I also think that the great-power competition will trigger new legislative initiatives on Capitol Hill in 2022, as US lawmakers seek new tools to counter China's military and economic rise.

Here, we should look for more US government support and attention for strategic industries, including semiconductors, space technologies, next-generation communications, robotics, biotech, rare-earth minerals, artificial intelligence, and quantum computing.

Beijing, meanwhile, is likely to continue to advance its own expanding military, economic, and diplomatic capacities in 2022, as China seeks greater regional and global influence.

Insight from sub-adviser, Wellington Management



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Key Points

- The US-China relationship will arguably remain the most important geopolitical dynamic in 2022, with competition likely to trigger US policy counter-moves and greater support for strategic industries.
- Climate change is increasingly viewed as a worldwide national-security threat that will feature resource conflicts, food and energy shortages, rising extremism, and forced migrations.
- Investment themes are likely to include demand tailwinds for traditional defense applications. Companies with solutions for helping societies adapt to climate change may also find favor.

With geopolitical rivalry forecast to grow in importance in 2022, both countries will remain keen to decouple strategic sectors in a managed fashion, while also seeking opportunities for limited bilateral cooperation in areas of mutual interest, including trade, climate, and the global pandemic.

Key Geopolitical Risks: What Could Go Wrong?

Several geopolitical risks could derail my base case of a structurally challenged but more manageable US-China relationship in 2022. In a worst-case scenario, any one of these could lead to a sudden rupture in bilateral relations.

Taiwan tops this list, given its strategic and domestic political importance to Beijing, and the emphasis on human rights and democracy in the Biden administration's foreign policy.

It is probable, therefore, that tensions will stay elevated in and around the Taiwan Strait, with a higher tempo of military activity on all sides presenting a low but real risk of accidental military conflict.

Driven by territorial disputes and increased military activity, geopolitical risk is also likely to remain pronounced in the South and East China Seas, while North Korea's accelerating nuclear weapons program could produce additional opportunities for crisis and conflict in 2022.

Elsewhere, I see Iran as another crucial geopolitical risk to monitor—particularly if ongoing diplomatic efforts to resuscitate the Joint Comprehensive Plan of Action fail, and Tehran resumes its nuclear program.

Meanwhile, cyber risks may intensify in 2022 for both government and corporates, as this highly effective (and highly disruptive) "shadow war" tool becomes the new normal in a more competitive global order.

As for Europe, Russia's role in the great-power competition will continue to be the chief concern of the US and its allies, particularly as Moscow advances its hypersonic and nuclear weapons capabilities. I also expect more Russia-linked cyber operations aimed at US and Western companies as part of the new normal of geopolitical risk.

On the Horizon: Climate Change as Geopolitical Risk

Finally, I expect climate change to become a bigger defense priority in 2022.

Natural disasters around the world have underscored the Pentagon's long-standing concerns about the national-security implications of climate change, which it views as a "complex catastrophe" that will act as a threat multiplier across many dimensions.

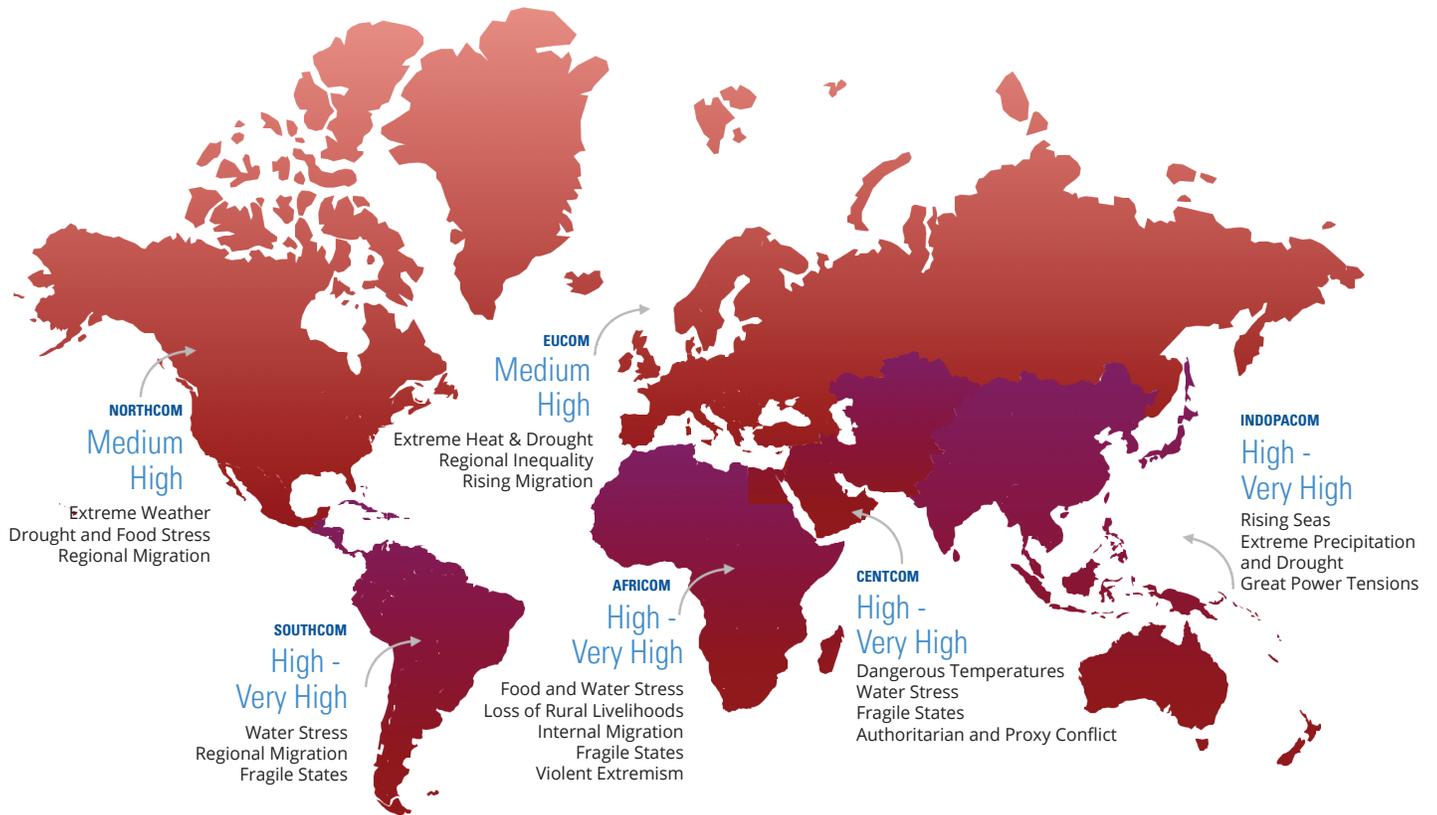
These coming climate risks will be centered on equatorial regions and in the tropics—home to some of the world's most challenging geopolitical hotspots as illustrated in **FIGURE 1**. Principal threats include increased climate migration, resource conflicts, food and energy shortages, rising extremism, and expanding opportunities for disease vectors.

A higher tempo of military activity in and around the Taiwan Strait could present a threat of accidental military conflict.

FIGURE 1

US National Security and Military Leaders See Climate Change as “Catastrophic”

The Center for Climate and Security’s “Climate Security Threat” Profile, near-term scenario (1-2°C+ warming)



Source: Guy, Kate et al. “A Security Threat Assessment of Global Climate Change: How Likely Warming Scenarios Indicate a Catastrophic Security Future.” Product of the National Security, Military, and Intelligence Panel on Climate Change. Edited by Femia, Francesco and Werrell, Caitlin. The Center for Climate and Security, an institute of the Council on Strategic Risks. Washington, DC. February 2020.

At the same time, climate change is likely to continue to pressure US military capacity in 2022, just as it is likely to further destabilize the geopolitical landscape.

As it stands, more than two-thirds of US military facilities have already been hit by climate-related events such as wildfires, heat waves, hurricanes, and flooding. This includes the critical US national-security assets of Norfolk Naval Station in Virginia (also home to more than 30 other military installations), Marine Corps Base Camp Lejeune in North Carolina, and Tyndall Air Force Base in Florida.

The Pentagon has also reported a 60% increase in heat-related illnesses among troops over the past decade, adding to heightening national-security concerns.

I expect that this climate-as-national-security argument will continue to shape the US climate-policy narrative in 2022—and for years to come—as it merges with the long-term trend of great-power competition.

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Investment Implications: Adapt, Adapt, Adapt

Great-power competition and climate-change issues that intensify in 2022 may present significant long-term investment opportunities as governments, businesses, and individuals across society seek to adapt to these structural geopolitical shifts.

Major investment themes related to great-power competition include strong demand tailwinds for traditional defense applications, with a particular focus on emerging dual-use technologies that have both civil and military applications, as these are now at the heart of shifting military doctrines in the US, China, and globally.

On the climate side, I view adaptation as the most direct way to invest through the geopolitical lens, as helping societies better cope with rising temperatures, food and water scarcity, flooding, storms, and other climate-related issues may be the best insurance policy against these coming national-security challenges.

Talk to your financial professional to help you navigate the headwinds of tomorrow's geopolitical challenges.

Important Risks: Investing involves risk, including the possible loss of principal.

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