

China's Role in the World – The New Normal

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Focus & Question: Economic and financial integration of China into the world economy and what it means for the West. I like to answer this question in three parts: (i) By explaining the starting points of China's internationalisation from a historical point of view; (ii) By focusing on the most important current developments of China's economic and financial internationalisation; and last but not least (iii) by trying to answer the question what this could mean for the West.

Three important starting points of the international of China's economy and financial sector:

1978: Deng Xiao Ping's policy of 'Reform and Opening Up' with a strong stress on both: moving China's economy towards a market economy and towards the world. Invite foreign companies to invest in China und educate the Chinese society to learn from the West especially in terms how to run a market economy. The goal of the opening policy was clearly to use the best of the West in order to leverage China's economy and society and hence the welfare of its people.

I think I should remind you that Deng's statement was not self-evident given the complicated history of China with foreign powers in the 20 century, starting with the colonialization during the Ching Dynasty by Western countries at the beginning of the century and continued with the invasion of Japan during the II. World War.

The current president of China, Xi Jinping, has adjusted the opening policy towards a more prominent role of China in the world in economic as well as in political terms. He called for the 'renaissance of the China dream', remembering the world of the great history of China before the industrial revolution. In fact, China is on its way becoming the second superpower of the world.

2001: The WTO-entry of China was the second big step of China's new role in the world. It marks the starting point of a strong increase in international economic and financial activities like, for example, more trade, higher direct investments, and stronger cross-border capital flows. This

phenomenon is known today as so-called 'hyperglobalisation' and ends with the outbreak of the global financial crisis triggered by the collapse of Lehman Brothers in the year 2008. In fact what happened was a heavily indebted West – especially the United States but also European countries - financed by international capital flows provided by China and other surplus countries like, for instance, the oil producing countries. This imbalance burst in 2008 and thanks to the strong and fast reactions of central banks and governments around the globe a new Great Depression like 1929 was eventually avoided although we still suffering from the impact of this crisis.

2008: Actually, the outbreak of the financial crisis marks the third and perhaps strongest wave of China's rise in the world especially in financial terms. It was the starting point of the internationalisation of the Chinese currency, the Renminbi, which was later integrated in the SDR of IMF. The Renminbi is nowadays already the 5th largest trading currency after the US-Dollar, the €, the British Pound, and the Japanese Yen. Since this March even RMB-denominated oil price futures can be traded in Shanghai. To develop Shanghai into an international financial centre was a decision taken by China's central government in 2009 in the middle of the financial crisis. This was some years later topped with the implementation of an international trade zone in Shanghai in which international trade of currencies and capital can take place in the same way than under the regime of free capital flows and flexible currencies in the West. Furthermore, Hong Kong has been developed as a leading off-shore market for the RMB also following the rules of free markets. You may know that Frankfurt is an off-shore centre for the RMB as well.

The importance of China rose also in international institution. I mentioned already the integration of the RMB into the SDR of IMF. Furthermore, China's capital share in IMF, which is relevant for the voting power, has been increased to the third largest after the USA and Japan. And China in meantime has also become a member of the Basle Committee for Banking Regulation and the Financial Stability Board of IFM for macro prudential supervision.

After this short historical excursion of China's internationalisation in economic and financial terms I like to turn to **current situation**. What is the **situation today with regards to China's role in the world**? I see mainly four important developments: (1) The rising importance of China's economy, (2) China's overseas direct investments, (3) China's Africa strategy, and last but not least (4) the so-called Belt & Road Initiative.

(1) **Economic Importance**: Let's start with numbers. Measured in terms of the size of its GDP, China is the second largest economy of the world behind the USA. However, measured in purchasing power parities – i.e.: what people can buy for their income – China is already the largest one. But also in nominal terms: China's GDP will take over that of the USA in around 5 years and it is expected that in 2050 China's economy will be double as large as that of the USA. In terms of GDP-growth, China's economic growth contributes almost 40 % to the world growth rate.

However, size and growth is not everything. In terms of GDP-per-capita and therefore the living standard of the people, China is still only no. 89 in the world with a GDP-per-capita of only around 20 % of the level of the USA. That means, it is still a long way to go for China to reach the same living standard than the West.

(II) This leads me to the second development, **China's overseas direct investments**: In order to increase the living standard towards the level of the West, China has launched the so-called 'China 2025' – strategy three years ago. The strategy intends to develop the country into a leading international technology hub. It is in this context that Chinese company's investment more and more in Western companies with a focus on high-tech companies of key industries like AI, robotics, E-cars, Industry 4.0 and so forth. Especially German companies with its high industrial standards are a target of these investments and take-overs if we, for example, think of the recent cases of Daimler and Kuka. The goal of these investments is clear: Closing the technology gap to the West and overcome the status as a cheap labour economy.

(III) China's **Africa strategy** - that is already under way since some years - is another good example of the strategic approach of China

with regards to its internationalisation. It involves, in fact, different stakeholders of the country like China's government, China's SOE, but also private Chinese companies. And in this case again the interests of China are well defined: To ensure a steady flow of raw materials to China by supporting the economic development of the African continent. And, indeed, the approach works well: Africa's economic development has picked-up and China faces no shortage of raw material.

(IV) Last but not least we have to talk about the so-called **Belt & Road – Initiative** launched by China's President in the year 2013. This initiative is the largest and most comprehensive global economic activity of our times. It consists on a land as well as a sea channel that covers more than 60 countries, around 65 % of the world population, one-third of world's GDP, and about 25 % of global trade. Currently, the investment required is estimated with 20 trillion USD roughly $\frac{1}{4}$ of world's overall GDP. One important funding source of the project is the Asian Infrastructure and Development Bank (AIIB) set up by China in the beginning of 2016 with the support of 57 countries – including a variety of European countries. Further funding through Public-Private-Partnerships and the so-called 'Silk Road Fund' is under way.

I just published a working paper together with an MBA graduate of our school on the topic and as a result it turned out that in most of the 7 economic corridors, in which the project is disaggregated, the success of the project is 'likely' or even 'highly likely' although a variety of risks is involved as well like, like, for instance, low standards of administration and inefficient bureaucracies, political risks including corruption, rivalry between countries, and last but not least, of course, a lack of funding.

Nevertheless, the Belt & Road Initiative is up and running and helps China economically to reduce its domestic overcapacities by exporting it to the involved countries and to internationalise the RMB further on. Moreover, the project promotes the ongoing rise of the country in international affairs by exporting the China development model to the involved countries that in turn benefit for their own economic development.

Finally, let me conclude by trying to answering the questions: What all these developments **mean for the West?**

I think the following:

Firstly: As a matter of fact, China is underway to become the second superpower beside of the USA especially in economic and political terms but still not so much in military terms.

Secondly: China is both an economic opportunity as well as an economic threat for the West.

What are the **opportunities?**

- Investments of Chinese companies in Western companies help employment and growth in Western economies.
- China imports a lot of goods and services produced in Western countries, whereas their exports to the West helps to keep the inflation rate low in our countries due to the lower prices of these goods and services.
- Last but not least, the great hope for China and the world is the rise of the middle class in China with a strong consumption power. This is good for business of foreign companies in China and for companies in the West given the rising flow of Chinese people traveling and buying in Western countries. China's rising middle class will become a great promoter of income growth worldwide.

Let's turn to the **threats** now.

- China's rise means more competition for Western countries and companies. China wants to avoid the so-called 'middle-income' trap and is therefore keen using advanced technology that was until yet the competitive advantage of the West. However, instead of blocking these investments, Western companies and Western countries should take this challenge and competition by developing their own technologies even faster. Indeed, there is still a strong gap between the technology level playing field of China and the West. China is moving forward but the West as well.

- A second threat for the West is the business of Western companies in China. I think this is more important for the West than the investment of China in Western economies because business of foreigners in China is still much more restricted than for Chinese companies in the West. I suggest the West should follow a tit-for-tat-strategy in this case: The approval of important and significant investments of Chinese in Western companies should be combined with a more opening up of business for Western companies in China as well.

However: opportunity or threat. It doesn't matter too much. The rise of China as the second superpower is a reality – the new normal. We in the West should accept this instead of complaining about it and regret the old times of the unrivalled power of the West. Let's be more moderate as well as competitive, which not mean to give up the own interest. Actually, I am not afraid of the West because of the rise of China. I think we have something to offer in economic, financial, as well as in political terms and we can benefit from China's success.

However, the pre-eminence of the West since Christopher Columbus discovered America more than 500 years that was even levered by the industrial revolution, is actually a historical coincidence and not written for all times. I very much agree with the judgement of Warren Buffet some years ago that the 21st century will be the Chinese century as the 20th century was the century of the USA and the 19th that of the United Kingdom. Actually, we are moving from a Western-dominated past to a post-Western future. And we have to do the best of it!

With regards to China this means that we are looking for an essential partner in ensuring a reasonable co-operative, stable, prosperous, and peaceful world.

Thanks you for your attention!