The harmonious superpower?
China’s role in a multi-polar world
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* With the support of Deutsche Bank Research
The views expressed in the articles of this reader are solely those of the authors and do not represent the views of the conveners of the Foresight project.
The harmonious superpower? China's role in a multi-polar world
Foreword

Thomas Matussek

“China to overtake US by 2016”, read recent headlines in newspapers in many different parts of the world, citing a report by the OECD. While such forecasts are contentious, they serve to underscore the dramatic transformations that have taken place in China over the last three decades. The country’s economic growth has occurred in the context of globalisation, and been accompanied by increased interaction and engagement with the outside world. The rapid rate of growth in China’s economy and its external influence has found both outside observers and internal strategists struggling to keep pace and make sense of its implications. However, it is not only the scale of the Chinese economy or the size of its population that makes China significant for world affairs, but also the country’s civilisational heritage, unique socio-cultural systems and distinct ways of thinking. It is these ways of thinking that the Foresight China reader aims to explore and compare with different perspectives from other countries.

It forms part of the Foresight initiative, which arises out of a concern with how to better govern an increasingly interdependent and multi-polar world. Economic and technological interconnectedness have brought development and prosperity to many parts of the world. Yet they have also led to problems travelling quickly across borders, which no longer serve as a guarantee of protection against threats. From economic crises to pandemics to cybercrime, no single country is in a position to address these challenges on its own. Further, deeper, and more structured international cooperation are an absolute necessity in today’s world.

At the same time, the process of international cooperation is made more complicated by the fact that each country approaches global issues in a way shaped by its own historical experience, cultural context, socio-economic model and political realities. As the relative constellation of global power shifts and diffuses, both among countries and to non-state actors, no single state is in a position to dictate its vision and solutions to others. It has therefore become even more important to understand the perspectives of other countries, a process that the Foresight initiative seeks to facilitate.

To the outside world, China’s rise inspires both awe and fear. While there are myriad proclamations of ‘China as the next superpower’, there is little understanding about the preferences and priorities of the country. We aim to help fill this gap with this publication. Following the legacy of Herrhausen, we at the Alfred Herrhausen Society seek to identify relevant dynamics and currents in developments to seek traces of the future in the present. In this endeavour, we are grateful to our partners, the China Institute for Innovation and Development Strategy and the China Institute of International Studies for their invaluable support and many fruitful discussions.

China is at a momentous juncture in its development, and at the same time, the world order is undergoing a significant transition. Both processes will affect each other - the way in which the interaction between China and the rest of the world plays out will have a bearing both on China’s own internal development and on the evolution of the global order. The country’s new leaders face both enormous opportunities and significant challenges as they chart China’s path over the coming years. The diverse themes analysed in this publication, from both Chinese and international viewpoints, highlight that there are important choices to be made that will affect our interrelated futures in a multi-polar world.

We hope that we can spur some discussion and look forward to your comments and critiques from different perspectives.

THOMAS MATUSSEK is Managing Director of the Alfred Herrhausen Society, the International Forum of Deutsche Bank.
The harmonious superpower? China’s role in a multi-polar world
Introduction

Priya Shankar with Claudia K. Huber and Ronja Scheler

*A changing China has long been a mirror in which visitors can see their expectations and their own character reflected.*

This metaphor reflects the variety of views that China’s rise generates amongst the outside world. Some welcome the country’s success in lifting hundreds of millions out of poverty and building a unique development model, while others point to its vulnerabilities and fragility. Some see great potential for China contributing to a more equitable and balanced world order, while others see potential for conflict and instability. However, China is much more than an elusive mirror in which to see different perspectives reflected. The country is home to the world’s largest population and its second largest economy. It also has the fourth largest area and the second largest defence-spending budget in the world. But it is not only China’s enormous scale and size that make it important to delve beyond the reflections and come to grips with the realities of the country. It is also the fact that China is at a moment of transition, and the way this evolves will have implications for the wider world.

The country’s new leadership inherits remarkable successes and great opportunities, but also significant challenges. The way it navigates these challenges will have a bearing beyond its borders. Soon after being appointed General Secretary of the Communist Party of China, President Xi Jinping spoke of China’s contribution to the world. He said “Our responsibility is to unite and lead people…while accepting the baton of history and continuing to work for realising the great revival of the Chinese nation in order to let the Chinese nation stand more firmly and powerfully among all nations around the world and make a greater contribution to mankind.” While it seems apparent that China will have a greater role in world affairs, the shape and form that this role will take is not yet clear, neither within China nor internationally.

This Foresight reader examines China’s rise and role in an interdependent and multi-polar world by examining different perspectives on three policy issues that are of critical importance in China but also have broader international relevance: economic development, resource security and regional order. The issues were determined in preparation for the Foresight China symposium through a series of conversations with a range of Chinese experts who outlined their views on the most important challenges facing China. We are grateful for their insights and perspectives.

In this publication, each of these challenges is explored in a separate section by Chinese and non-Chinese authors, with the aim of relating ‘insider’ and ‘outsider’ perspectives on the major issues at stake. These sections also contain key data and facts that indicate some of the recent trends in each field. The overarching theme running throughout the publication – the role of China in a changing world order – is explored most explicitly in the last section.

**Furthering economic development**

Further poverty reduction and employment generation continue to be top priorities for China. While there is much regional diversity within the country and debate on the existence of a ‘Chinese

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1 ‘The power of China: Toasting the world (or not)’, The Economist, 23 March, 2013
2 Speech at the Politburo Standing Committee Members’ meeting with the press at the Great Hall of the People, Beijing, 15 November 2012, retrieved from BBC news website on 30 March 2013
economic model’, it is clear that the country’s economic policies have resulted in spectacular growth over the last three decades. However, there also appears to be a sense that the economic path and strategies that followed the 1978 reforms, while having achieved remarkable successes, have now reached their zenith. A recent joint report by the World Bank and the Development Research Center of the State Council of China called for further economic reforms.3

Indeed, the country faces several bottlenecks to its growth. Declining international demand has coincided with domestic challenges such as rising wages and an ageing labour force. It appears that China can no longer go on simply being the ‘workshop of the world’. Anna Jaguaribe emphasises the role of innovation and technology in moving China up the value chain. She suggests that China’s state-led initiatives in this field are unique and may offer opportunities for other emerging economies.

Along with China’s growing economy, its global financial presence has also increased manifold. However, the formal institutions and mechanisms that govern the global financial system are still largely dominated by the United States and Europe. With its large international reserves, China has already been lending to other countries and financing many international projects. Recent discussions around the launching of a Brics development bank, in which China is likely to play a key role, raise further questions about a multi-institutional international landscape. As Yao Yang argues, China has so far largely been a passive participant in the global financial system but this is now changing. He asserts that reform at home will be as critical as reform abroad in this process of change.

Ensuring resource security

President Xi Jinping’s first international visits as head of state, to Russia and Africa, and the host of accompanying agreements, indicate how important natural resources are for China. Indeed, China is now the world’s biggest energy consumer, although its per capita consumption still remains low. As China’s economy grows and its living standards improve, this is likely to increase. In recent years, a rising world population and changing patterns of consumption have led many to talk about impending resource scarcity. In this context, China’s purchases and development of equity oil and gas, mines and even agricultural land, have sometimes caused international debate.

Shi Ze, in his article on China’s energy security, emphasises the importance of securing adequate hydrocarbon supplies and speaks of the benefits of China’s international activism in this field. However, as a recent article by Lamido Sanusi, Governor of Nigeria’s Central Bank, indicates, China’s initiatives to secure resources internationally have attracted mixed responses including concerns about the exploitative potential of economic relations.4 Indeed, Fyodor Lukyanov highlights that the changing international landscape also presents challenges for resource producers and suppliers. He calls for an international energy organisation that reflects the interests and needs of consumers, producers and vulnerable countries. While this seems an apt suggestion, it will not be easy to agree on the practicalities of how such an organisation should function, especially at a time of a changing balance of global power.

As each of the contributors to this section point out, possible scarcity, at least in the field of energy resources, may no longer be such a strong concern. First, the current shale gas ‘revolution’ and the development of renewables open up new sources. Second, the development of technologies that enable greater energy efficiency will also help reduce the threat of scarcity. As a result, Zha Daojiong calls for a paradigm shift in the conception of resource security towards the issue of efficiency, both in terms of energy and food. He argues that Chinese and international efforts should focus on improving

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3 China 2030: Building a Modern, Harmonious and Creative Society, World Bank, 2013
efficiency and reducing wastage in patterns of production and consumption.

Building regional order
The complexities presented by a changing balance of power are clearly visible in Asia. With strong nationalist sentiments, historical rivalries and rising powers, many had predicted that East Asia was a region ripe for conflict. Yet, so far, the region has defied scaremongers and remained largely peaceful, partially due to the web of associations and institutions that bind different countries together. In recent years, however, tensions have been rising, including over disputed territories and maritime routes. China, which borders fourteen countries in different parts of Asia will be critical in any exercise to build a stronger regional order.

Pang Zhongying stresses the urgent need to politically imagine an Asian community. He argues that China has been contributing to building regional communities but that the United States’ ‘rebalance’ to Asia may prevent this from going further. On the other hand, Jonathan Pollack asserts that many Asian countries have welcomed the US ‘rebalance’, in part, due to their concerns about China’s intentions in the region. He also suggests that although the task of building regional order is critical, it is also very difficult in an increasingly complex landscape. It will be important to avoid getting locked into cycles of conflict.

China rising
A connecting thread between each of the distinct themes outlined above is that they all demonstrate patterns of both conflict and cooperation. Wu Jianmin and Rosemary Foot both emphasise these patterns in their contributions. Wu characterises them as the “two mega-trends of our times” and Foot speaks of the “duality of global order”. However, Wu highlights China’s cooperative tendencies while Foot suggests that there are likely to be a complex series of negotiations across different issues. Another important theme that emerges throughout the contributions is the notion whether economic interdependence will be enough to ensure that conflict is avoided – the power of economics to guide politics as it were.

It appears that as China rises, both China and other countries will confront important political choices in navigating this rise. The way in which the interaction between China and the world plays out will have a significant bearing, both on the country’s own internal development as well as on the evolution of the global order. It is important that this interaction is shaped by realities and mutual understanding. In part, the contradictory perceptions of China are driven by the fact that the country has been rather opaque in its policies and strategies. But, in part it is also because outsiders have not adequately attempted to see the country from within and understand its dynamics.

It is inevitable that different countries will have different, and sometimes even conflicting, perspectives. An underlying premise of the Foresight initiative is that economic interests and interdependence, on their own, will not be enough to overcome these conflicts. In an increasingly multi-polar world, it is becoming more and more crucial to have an understanding of the context shaping those differing and multiple perspectives. Understanding the reasons behind different viewpoints is the first step in any attempt to bridge the gap between them. It is this process that this publication and the associated Foresight China symposium seek to facilitate.

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The harmonious superpower? China's role in a multi-polar world
Section one: Furthering economic development
The harmonious superpower? China's role in a multi-polar world
The present international context of slower economic growth and transition in international power relations, poses new development challenges for emerging economies. There are increasing difficulties in competing for a growth edge in the global economy while catching up with new technology frontiers. A new and growing debate is now taking place on the role of public policy in managing the relationships between finance, government and markets. In this scenario, industrial and technology policy, long kept-out of the public eye by the belief in the capacity of the market to govern demand, have once again come to the fore. Brazil and China are good examples of contrasts in this new challenging development debate.

From the 1990s, changes in international finance, geographies of production and distribution of research, altered the way in which goods and services are produced and demand regulated. Increase in international liquidity brought new players into the international finance market, looking for good returns. International liquidity, deregulation of financial flows, increase in foreign direct investment and in financial instruments available for credit helped to decouple development targets from national ‘external constraints’.

In the realm of production, the fragmentation of manufacturing through the creation of regional/global value chains, the centralisation of retail into few powerful global groups and the relocation of research and development (R&D) away from original production sites created a new geography of production and innovation. Goods are being produced in different places, through different methods with direct consequences to the creation of value added and the capacity to innovate.

China is the success case in the new world of fragmented production and global value chains. Its manufacturing and technological achievements changed global terms of trade but, more importantly, altered competition in all global markets. The first effect of this new sinocentric world of production in Latin America and in particular in Brazil, was to alter the parameters through which North/South divisions in trade were understood and growth strategies conceived. The South, now represented by China, became the principal market for commodities, but also for the production and exports of information technology (IT) goods, leading the race for secondary innovations in information and telecommunications sectors.

Crisis and indeterminacy: difficulties ahead

The crisis of 2008 and the relatively slower growth of China are altering this economic scenario. In contrast to previous crises, the present moment does not seem to outline clear exits. The technologies that had underlined the alternative in production patterns in the 1970s (the essence of the great divide) are still unfolding. The great energy challenges, which will condition the long-term options for technology and production in the near future, have numerous possible outcomes. There is a lack of clear-cut economic stimuli for changing energy scenarios and many of the financial instruments, which spurred the information revolution such as venture capital, are poorly shaped to deal with radical changes and low economic returns. Classical state instruments...
In a global scenario of uncertainty regarding economic opportunities and power relations, innovation gains particular relevance to spur innovation such as military spending and or government procurement (the military-industrial dimension) also seem to be under revision, with very interesting implications for the logic of the industrial security establishment.

Giovanni Arrighi argued that China could be opening up a new bifurcation in the road that tied war to economic expansion, starting a new parenthesis for a ‘mercantilist’ approach to international relations. It could be said that in guaranteeing large public investments in technology, China is opening up a new approach towards radical innovation, alternative to the defence-sponsored innovation drive.2

In a global scenario of uncertainty regarding economic opportunities and power relations, innovation gains particular relevance but competition is also more pressing. Key factors that characterised the boom years of globalisation are changing, such as trans-border financial flows, international liquidity and the high propensity for consumption of the American economy.

In more complex markets, the struggle to gain shares and advantages through incremental product innovation is immense. The costs and risks also increase in the absence of a clear-cut line between product and process. As pointed out by Breznitz,3 incremental innovation is like the running of the red queen in Alice in Wonderland, much effort has to be employed to stay in the race. National growth opportunities through exports of low cost products are also different as cheap wages and abundance of labour are diminishing in China.

Over thirty years of constant growth have created imbalances in the Chinese economy. Adjustments must be made in the fiscal and financial system, cyclical real estate bubbles corrected, and growing inequality and inefficiencies in government services also need to be dealt with. For countries such as Brazil the capacity to maintain an economy with almost full employment with low investments, increasing wages and high consumption is clearly diminishing.

Betting on technology and industrial policy
It is in the context of this international scenario that the 12th Chinese Development Plan, calling for a reorientation of the Chinese growth model, acquires particular relevance. The plan has important reform targets: welfare, fiscal and financial policies. But more importantly, it has major transformational goals: turning China into an innovation economy through the development of strategic industries (SEI).

Scientific and technological modernisation has been a consensus in China since the early days of reform. Technology policy has also been coherent with educational objectives and market reforms. Furthermore, Chinese economy policy has always used foreign direct investment (FDI) as a tool for integration of the national economy in the global market. Access to the Chinese market has since the very start been contingent on technology policy, and FDI has been utilised as a constant tool for technological advancement.

The Innovation Surveys of Booz and McKinsey indicate that at present, most multinationals carry out R&D activities in China and use it as a global platform. Yet, it is not an easy task to transform the Chinese economy from a global manufacturing hub into an economy operating at the technological frontier.4

There are various challenges. New policy ground is being experimented with, beyond the more tested grounds of catching-up policies. It is not easy to bridge innovation with the commercial aspects of

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2 Giovanni Arrighi, Adam Smith in Beijing, Boitempo 2008
3 Dan Breznitz, Run of the Red Queen, Yale University Press 2011
industrial policies or to strike a good balance between long and short term interests. There are competing causes for public investment and the consolidation of a Chinese welfare system, which is sustainable in the long-term, is the major one.

For many western observers the policy instruments developed for the reform and opening-up period—the Deng Legacy—is reaching its limits. For orthodox economists a complex market society such as China today needs a more flexible and open financing system, with differentiated credit instruments, less dependent on state investments. There are ample indications that institutional reforms will follow a different and more heterodox direction and the main contours of new economic institutions are already in place. There is an increase in state investments in key sectors, more commercial emphasis on innovation, and institutional flexibility in implementing new programmes.

The reorganisation of the economic and industry ministries in a more horizontal manner, the creation of the National Development and Reform Commission, and the disassociation of state-owned enterprises from sector ministries have contributed to the creation of technical elites committed to industrial development. These are elites that combine an academic trajectory with bureaucratic expertise and ensure quality and continuity in the planning exercise. The in-depth research of Naughton and Chen on Chinese industrial policy indicates that as of 2003, technology policy in China became more structured, sector specific and systematic, giving rise to a new techno-industrial policy paradigm. Policy-making is routinised, with agreed-upon rules, which avoid a zero sum war amongst bureaucracies. The policy process is open at different levels to outside consultations and ideas but also organised to facilitate top-down decision-making.

Opportunities to engage in change

The twelfth plan is couched on a vision that emphasises scientific and technological innovation as both achievement and necessity. The strategic industries’ programme is unique in scope, funding and attempts to forge new relations between the planning process and a complex market economy. There are probably no precedents for this policy effort and no prior models which address the question of entering an innovation economy on such different terms.

The project commercialises and organises the demand for new industries, which have also been part of the megaprojects in key sectors. There is a special effort in enhancing coordination between different institutions, guaranteeing coherence between economic and industrial policies and choice of technological paradigms. While clearly a top-down decision-making process, the planning and project selection process involves many programming and implementing agencies and has competing enterprises as executing agencies. Outside of the military-industrial procurement system there are no precedents for such a vast long-term resource programme and such a trial-and-error technological environment.

Will the Chinese programme succeed? Will it be effective in providing the distinguishing edge for future growth? Does it open up spaces for cooperation in a global development agenda? The historical process of development in China is in itself unique, but the new programme unveils perspectives for public policy that have significant implications for other emerging economies.

Brazil’s recent development efforts have been concentrated on sustaining inclusion. But inclusion is also putting pressure on growth and as a consequence there is a new emphasis on industrial and technology policy. Many different issues are being addressed: from faulty links between research and industry to

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5 Joseph Y.S. Cheng, A New Stage of Development for an Emerging Superpower, City University of Hong Kong Press 2012
7 Barry Naughton and Chen Lin, The Emergence of Chinese Techno-Industrial Policy, SPIDER WEB Conference paper, BNDES, Rio 2013
interconnections with global systems of innovation. A large and varied technology and science programme is just now being put into place.

It is not a simple task to stimulate innovation in an open market economy with the characteristics of Brazil. The industrial sector is older and more fragmented than in China and competition for rents most often prevents ‘structured policy consensus’ from being achieved. The region has remained outside the last wave of changes in fragmented IT production and there are feeble regional linkages to high value manufacturing chains.

The Chinese new techno-industrial paradigm is clearly conceived as an instrument for policies that are part of a Chinese strategic vision of its role in the global economy. The SEI programme will bring about an inward orientation for industry and economy. While the programme draws on the global technology frontier, its priority is on indigenous innovation and firms. How regional and global links will be developed remains to be seen. There is a tremendous potential in the idea of indigenous innovation but also a danger of it being captured in a global competition for standards and brands and as such become more of a commercial than a development strategy. It is, in part, a top-down exercise in a world of bottom-up creativity and it always runs the risk of encasing the innovation effort by closing in new knowledge fields. It is too early to see whether it will engage industry and create technologies, which will produce social transformations.

The task is different in Brazil both in scope and nature. The new technology programmes are not an all an intensive effort to reach technological frontiers on multiple fronts, but a new push for an economy which was stalling in its innovation spirit. Success in social inclusion policies, abundance in natural resources, technological expertise in food production, mining and energy as well as a clean energy matrix should constitute advantages for Brazil in the challenges ahead.

For China and Brazil, their new technology policies are conditioned by each country’s vision of challenges and opportunities in the global economy. But the programmes open opportunities for cooperation that go beyond comparative strategic advantages. There is a real chance to build a cooperation agenda, which engages both countries into drafting a more transformative development agenda for the future.

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China is a passive participant in the current international financial system. This system, centred on the dominant role of the US dollar, was established by the United States after the Second World War. Today, it is still dominated by the United States and European countries. To a large extent, China has benefited from this system by adopting and following its rules. However, the system also poses risks to China.

The most significant risk is created by the dominance of the US dollar. China is now the largest trading country in the world. About sixty per cent of its trade is denominated in US dollars. Due to the so-called ‘Penn effect’, a country’s currency will appreciate against the dollar when its per capita income gap with the United States narrows. Because China is catching up with the United States in terms of per capita income, the Chinese yuan is on a long-term trend of appreciation. This trend has been reinforced by the US Federal Reserve’s quantitative easing (QE) policy. The Fed has conducted three rounds of QE since the global financial crisis began in 2008. Those QEs have created excessive dollar liquidities in the market, which inevitably drive down the value of the dollar. As a result, Chinese exporters have to face the risks of the dollar’s devaluation.

China faces a dollar trap
As China’s economy integrates into the world economy, China’s monetary authorities have to increasingly take into account the consequences of their monetary policy towards China’s external economic parameters, especially the exchange rate. This is quite different from the case of the Fed that usually does not have that concern because America’s trade is denominated in its own currency. These risks are accentuated by the value of China’s official foreign reserves. The amount of China’s official foreign reserves has been growing by staggering rates in most years since 2004. Standing at 3.2 trillion dollars today, the reserves lose value if the dollar devalues.

In a sense, China is in a dollar trap. Because the majority of its trade is denominated in the US dollar, China has lost the flexibility to diversify the risks posed by a weakening dollar. For example, to maintain the value of China’s foreign reserves, it is better to distribute the holding into different currencies. However, whenever China begins to sell a significant part of its dollar holdings and to buy another currency, the value of the dollar declines and the value of the other currency increases. As a result, China ends up with losing in the process. This is the reason that large quantities of China’s foreign reserves are used to buy US treasury bonds and other dollar-denominated assets.

Steps to internationalise the yuan
The internationalisation of the yuan is a way to help China escape from this dollar trap. It comprises of two processes: to make the yuan a settlement currency for trade (starting with China’s own trade with other countries) and to make the yuan an intermediary for international value storage. Since 2009, China has taken several steps on both fronts.

The first step is to allow companies to settle their trade in the yuan. Before 2009, there was virtually no trade settled in the yuan; now close to ten per cent of China’s trade is settled in the yuan. The second step is to provide yuan liquidities to other countries. This includes currency swaps with other countries, mostly China’s neighbouring countries, and issuing...
yuan-denominated overseas loans. Before 2011, the amount of such loans was very small, only dwelling at about 20 billion yuan per month. In January 2011, it shot up to 140 billion yuan. Since then it has increased steadily to 183 billion yuan in January 2013.

The third step is to build off-shore yuan settlement centres. Hong Kong is expected to become the largest one. Ten years ago, there was virtually no yuan deposit in Hong Kong. Since 2009, the amount has increased sharply. Today, it lingers at about 550 billion yuan. These yuan deposits have been brought to Hong Kong by mainland tourists, companies, and inter-bank borrowings. Starting in 2007, companies have been allowed to issue yuan-denominated bonds. As a result, the yuan has begun to assume the role of providing the value of storage in overseas markets.

Necessity for internal reforms

Despite the above steps, the road to the yuan’s internationalisation is going to be a long one. It is unlikely that the yuan will become a major international currency in the next ten years. The impediments come from inside China rather than from the outside. In China’s neighbouring countries, the yuan has a good reputation and has long been used for daily transactions in the tourist sector. As long as China continues to narrow its gap with the United States in terms of per capita GDP, the yuan will continue to face upward revaluation pressures. Therefore people in other countries will be willing to hold the yuan. Domestically, however, China needs to seriously deal with the following obstacles in order to accelerate the yuan’s pace of internationalisation.

First, China has to liberalise its capital account and make the yuan fully convertible. Currently, off-shore yuan can only flow back to China when they have been used for exports from China. In addition, because the yuan is not fully convertible, people lose the flexibility of being able to quickly convert it into other currencies. This reduces the value of the yuan as an intermediary of value storage and seriously limits people’s willingness to hold the yuan.

Second, together with capital account liberalisation, China needs to adopt a floating exchange rate regime. This is driven by both a theoretical imperative and a practical necessity. By the ‘Mondell trilogy of impossibility’, a country can only obtain two of the three macroeconomic objectives, namely, free capital flows, fixed exchange rate and independent monetary policy. China is a large country, so maintaining its monetary policy independence is imperative. Therefore, China would have to give up the fixed exchange rate if it were to liberalise its capital account. In practice, the existence of the off-shore yuan markets means that it is possible that multiple exchange rates could exist for the yuan. As a result, cross-border arbitrage would become profitable. China’s capital control cannot completely fence off cross-border capital flows; people and companies do have ways of bringing money into China without official permission. These cross-border flows have an impact on China’s official exchange rate. For example, in early 2012 the yuan depreciated against the dollar because people in Hong Kong sold the yuan in large quantities (the yuan deposit dropped by 100 billion in a matter of three months).

Third, China’s monetary authorities need to strengthen their regulatory capacities in order to effectively manage the monetary system. When China opens up its capital account, its monetary authorities will need to be in a position to face fluid short-term capital flows. Most of those flows are likely to be for speculative purposes and could cause serious instabilities in the real economy as well as to the financial system. The lack of regulatory capacities may well be China’s biggest constraint, both in terms of fully opening its capital account and in terms of internationalising the yuan.

The nature of change in China

It seems, though, that the Chinese leadership is quite determined to push forward the yuan’s internationalisation. If that is the case, the imperative...
to internationalise the yuan will serve as a sort of commitment device to push China to move forward to reform its capital account, exchange rate regime and the financial system in general. China’s reform history shows that this kind of daobi, or ‘reverse pushing’, mechanism has been critical in pushing forward reforms in the past. For example, the privatisation of most state-owned enterprises was pushed through as a result of local governments’ drive for fiscal sustainability. Similarly, China’s almost hasty agreement to the American conditions set for China’s accession to the WTO came about due to China’s desire to obtain most-favoured-nation (MFN) status at the WTO. Although financial reforms in China are likely to take a long time, the wheels of change have already been set in motion.

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Section one data: economic development*

China’s economy has exhibited breathtaking growth since the country’s introduction of reforms in 1978. At the same time, its poverty rate has also declined dramatically. Trade has had an important role to play in this growth as can be seen in changes in the country’s trade to GDP ratio. Although given its large population, per capita income levels still remain low and there is significant regional variation within the country. At the international level, its share of world trade, foreign direct investment and international reserves have been rising rapidly. Yet it, along with other emerging economies, remains underrepresented in international institutions.

* With the support of Deutsche Bank Research
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Section one data: economic development

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<th>Guangdong</th>
<th>Sichuan</th>
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<tr>
<td>GDP per capita</td>
<td>53,868.2 RMB</td>
<td>29,531.0 RMB</td>
<td>21,920.8 RMB</td>
</tr>
<tr>
<td>Economic structure</td>
<td>5.0 %</td>
<td>13.8 %</td>
<td>13.8 %</td>
</tr>
<tr>
<td></td>
<td>48.8 %</td>
<td>52.8 %</td>
<td>46.0 %</td>
</tr>
<tr>
<td></td>
<td>46.2 %</td>
<td>33.4 %</td>
<td>40.2 %</td>
</tr>
</tbody>
</table>

Source: DB Research, China Statistical Yearbook

Note: Provinces were chosen as examples for different levels of development in China. The figures in the table are from 2012.
The harmonious superpower? China’s role in a multi-polar world

Population and Population Growth Rate in China

Source: World Bank

Life Expectancy in China

Source: World Bank

Age Structure in China

Source: US Census Bureau
Note: Numbers from 2020 onwards are based on forecast data

Section one data: economic development
The harmonious superpower? China’s role in a multi-polar world

Section one data: economic development

GDP and Percentage Change in GDP

Source: IMF
Note: GDP is on PPP basis; percentage change in GDP measures the overall percentage change in GDP from 2000-2011

Share of World Trade: 2011

Source: UNCTAD
Note: This only measures merchandise trade. EU-15 in 2000, EU-27 in 2011
The harmonious superpower? China’s role in a multi-polar world

Section one data: economic development

Share of Global FDI: 2000

Change in Share of Global FDI: 2000 – 2011

Source: OECD
Note: EU figures include intra-EU investment. EU-15 in 2000, EU-27 in 2011

International Reserves

Source: IMF
Note: This includes international reserves minus gold
The harmonious superpower? China’s role in a multi-polar world

Section one data: economic development

International Monetary Fund: Status of Reforms

- IMF quotas are meant to be based on GDP, openness, economic variability and international reserves
- Quotas determine a member country's voting power, financial obligations and access to financing
- The 14th General Review of Quotas agreed to a reform package that would:
  - Double existing quotas
  - Shift six per cent of quota shares to emerging market and developing countries
  - Re-align quota shares so that China becomes the third largest member country and other emerging economies also have greater shares
- Although agreed in 2010, this reform package has still not yet been implemented

Composition of International Reserves

Allocated and unallocated reserves

2000

- Allocated reserves: 78%
- Unallocated reserves: 22%

2011

- Allocated reserves: 55%
- Unallocated reserves: 45%

Currency composition of allocated reserves

2000

- US$: 3%
- EUR: 2%
- YEN: 15%
- GBP: 6%
- Other: 6%

2011

- US$: 74%
- EUR: 4%
- YEN: 25%
- GBP: 4%
- Other: 5%

Source: IMF
Note: Unallocated reserves include the total reserves of countries not reporting to the IMF
The harmonious superpower? China’s role in a multi-polar world
Section two:
Ensuring resource security
In recent years, China’s development has been an important factor in improving the global economic situation. At a time of widespread recession in other parts of the world, China’s growth has fostered economic recovery. Countries all over the world can benefit from the opportunities that accompany China’s rapid growth. China is the world’s largest developing country and its population accounts for one-fifth of the global total. Therefore, the country’s sustainable development and improvement of living standards are not only of domestic importance, but also relevant for global prosperity and stability. China’s development is dependent on its energy supply and as a result, the country’s energy path also has global implications. There are mutual and shared responsibilities among China and the world to ensure energy security, both for China and internationally. This article outlines China’s energy security challenges and the strategies the country is adopting in order to meet them.

Challenges facing China
The search for energy is becoming increasingly important for the development of China’s economy. The country faces many challenges in ensuring its energy security. First, there is a widening gap between supply and demand. Over the past thirty years, the Chinese economy has grown rapidly and consequently, energy consumption has also grown at an average pace of over five per cent. In 2012, China’s energy consumption reached 3.62 billion tonnes of coal equivalent (btce), an increase of 3.9 per cent from the previous year. In 2011, China’s energy output was only 3.18 btce, leaving a demand gap of 300 million tonnes of coal equivalent (mtce). Indeed, China appears all set to overtake the United States as the world’s biggest total energy consumer. At the same time, China’s per capita energy consumption remains low, and much lower than in developed parts of the world such as the United States, the European Union and Japan. Over the next ten years, China is likely to enter into a later stage of industrialisation with the acceleration of urbanisation. The country’s GDP is likely to double by 2020 and this will lead to much better living standards. Therefore, demand for energy is likely to continue to rise, leading to a widening gap between supply and demand.

Second, the country also faces severe environmental problems. Since the beginning of this year, smoggy weather in eastern China has caused widespread public concern. The goal of building a ‘Beautiful China’ was formulated in the 18th Congress of the Communist Party of China but the country’s current ecological environment is far from this goal. Pollution is largely due to growing energy consumption as China’s energy mix is primarily coal-based. In 2012, coal consumption accounted for 66.4 per cent of China’s energy consumption. On the other hand, non-fossil fuels accounted for only 9.2 per cent. Therefore, China faces the dilemma of minimising environmental costs of energy consumption, while at the same time guaranteeing adequate energy supply.

Third, China is heavily reliant on imported fossil fuels. Even though China is the largest energy producer in the world and its energy supply is primarily based on domestic production, the country still needs to import coal, petroleum and gas. China’s foreign dependency in terms of coal, oil and natural gas has been increasing. It is estimated that China’s dependence on oil imports will reach 60 per cent of total oil consumption this year. Domestic production...
in China is likely to remain stable in the short term, and therefore, China’s reliance on other countries will continue to increase.

Fourth, the uncertainties of the changing global energy landscape will be difficult to manoeuvre. International energy production and market dynamics are changing. The Iranian nuclear issue and Syria’s civil war have dragged the Middle East into turmoil, leading to uncertainties and risks for oil and gas producing countries in the region. This has become an important factor that influences international market supply and drives up oil prices. At the same time, America’s energy independence strategy and its breakthrough in shale gas drilling have had significant impacts on the world energy market. Meanwhile, the economies of Europe, the US, Japan and other developed countries are growing slowly and their demand for energy resources is starting to decline. The centre of energy consumption is shifting to the Asia-Pacific, as the demand for energy from the emerging economies continues to grow. China has, therefore, adopted a number of domestic and international policies to help ensure energy security.

Energy policy priorities

At home, China will adhere to the principle of primarily relying on domestic production to meet energy needs. China is the largest energy producer across the world, and its energy self-sufficiency rate has been maintained above 90 per cent. Despite the growth in energy consumption, the 12th five-year plan has reaffirmed that energy self-sufficiency is a priority and should be maintained at a rate of 85 per cent by 2015. China will pursue energy savings and seek to limit total consumption to four btce per annum. China will attempt to change its energy consumption structure away from coal, with the aim that natural gas will account for over ten per cent, and non-fossil fuel forms of energy for about 15 per cent of China’s energy consumption by 2020. The country will rely on innovations in science and technology to achieve this aim. It will increase its investment in technological development, especially for clean coal, non-fossil fuel forms of energy, and non-conventional sources of energy. It also aims to increase energy efficiency and reduce greenhouse gas emission. The Chinese government commits that by 2015, energy consumption per unit of GDP will reduce by 16 per cent and carbon dioxide emissions per unit of GDP will reduce by 17 per cent as compared to 2010.

Internationally, China seeks to build a diversified energy supply system. Although China faces many energy challenges, the essence of China’s energy security is to guarantee sufficient, secure and stable supplies of oil and gas, which are urgently needed for economic development. At the moment, the issue of China’s oil supply is the centre of debate. With rising dependency on foreign oil, the country’s energy security is becoming increasingly influenced by international oil supply and price fluctuations. In the long-term, a disruption of China’s oil imports due to a shortage in the world’s oil resources is unlikely. Global oil trade and international oil markets should be stable enough to meet China’s energy needs. However, there are several short-term risks. These include abrupt political and military events in the oil-producing regions as well as supply and demand imbalances in the international market. These could lead to soaring oil prices and may even cause a shortage, or perhaps even suspension, of China’s oil imports. Such risks are exacerbated by the fact that China’s oil imports come mainly from the Middle East and Africa, which are regions with much political and social turbulence. There are concerns, not only
about the sources of supply, but also about means of transportation. Transportation via sea is the major supply route for China’s energy imports and could easily be affected by piracy as well as geopolitical factors.

Therefore, in recent years, China has pursued international action to secure energy supply. Following the principles of equality, reciprocity, mutual benefit and win-win, Chinese energy enterprises participate in international energy cooperation. This includes foreign investment and overseas infrastructure creation. Such cooperation increases global energy market supply and also promotes the diversification of China’s oil and gas sources. In the building of transport corridors, China has enhanced its cooperation with neighbouring countries. Amongst other projects, it has finished construction of the China-Kazakhstan oil pipeline, the China-Russia oil pipeline, the China-Central Asia natural gas pipeline, the China-Myanmar oil and gas pipelines. Through these means, it has improved energy security.

China’s need for energy security presents dilemmas. On the one hand, China should secure reliable energy supply for its economic and social development. On the other hand, it should shoulder the joint responsibility of securing global energy supply. It should meet the demand of energy consumption for development. But it should also take responsibility for protecting the environment and tackling global climate change. Therefore, China must take both internal and external measures simultaneously. In the future, China needs to coordinate both domestic and international energy development in order to take a global view. It needs to base its actions on present needs but also take a long-term perspective. And it should continue emphasising the principles of mutual benefit and cooperation to promote diversified development of energy sources. It is only by taking action at both home and abroad, that China will be able to guarantee its energy security in the long-term.
Beyond geopolitics: building a global approach on resources

Fyodor Lukyanov

There is a phrase in Russian political discourse that has been used for many years and that is attributed to an American politician: ‘Siberia is too important for the world to let Russians govern it on their own’. Initially, these words were attributed to Madeleine Albright, and if you search for this phrase on the Russian-language version of the internet, you will find many references to her saying it. This quote is presented as evidence of America’s expansionist nature and of the need for Russia to build up its defences. Other voices on the internet attribute the quote to Condoleezza Rice and Hillary Clinton. Any attempts to find the original quote in English fail, as it exists only in Russian ‘translation’. The myth around this phrase serves to highlight how sensitive resource-rich countries can be about outside interference. A legend about enemies who are dreaming of seizing someone else’s wealth is typical of all countries rich in natural resources. It would be unfair to explain and characterise this only as paranoia.

Although resources have always been a significant issue in global politics, recent developments indicate that world energy patterns are on the cusp of a dramatic change. The rise in consumption in the emerging countries, the shift in the United States towards energy self-sufficiency, and the drive for green energy are likely to radically alter the dynamics of global energy markets. Given these changes and the potential for turbulence, this article argues that we need a global approach on resources to ensure a smooth process of transition that takes into account the interests of both producers and consumers.

Basis of geopolitics or exaggerated threat?
Global geopolitics has always been based on the idea that countries need resources for development, and that the struggle for them is the basis of international relations. The Cold War era was an exception to the usual course of international history, as the confrontation in those years often had ideological rather than material implications. And the two rival superpowers simply sought to sideline each other wherever possible. However, after the collapse of communism, the threat of resource-based conflicts re-emerged. Although military campaigns were never explained by resource motives, their shadow was always present, especially when the focus of military operations increasingly shifted towards the Middle East, which is a global hydrocarbon reservoir.

This is not surprising, considering that the issue of resources has become a major topic of international debate. This started in the 1970s with the publication of a Club of Rome report, which raised considerable public attention on resource scarcity. Today, in the early 21st century, as consumption in developing countries has soared, more and more people have begun to talk about a looming scarcity of resources and associated political threats.

At the same time, it is risky (if not pointless) to try to forecast developments, especially in the modern world where ‘black swans’ are frequent visitors. If

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1 Donella Meadows et al., The Limits to Growth, Universe Books, 1972
we do try to think about future lines of conflict, it may turn out that they arise in areas other than expected. Moreover, the scarcity of resources may not have as significant an impact on global stability as used to be feared. Paradoxically, suppliers, the owners of resources, may encounter as many problems in the future as consumers.

Changing patterns of international demand
If one is to believe forecasts of the International Energy Agency (IEA) published in late 2012, within twenty years the United States will not only achieve energy self-sufficiency, but will also become the world’s largest energy exporter. The explanation is the shale gas revolution that is taking place in America. The IEA forecast is only one of several possible scenarios, and during the forecast period until 2035, there may arise many factors that can change the situation. Still, the forecast is sufficiently founded to make one think about consequences. The greatest changes are expected in the Middle East. If America has no more demand for Middle East oil, it will change the nature of its foreign policy. The US will no longer feel the need to be deeply involved in the intricate processes taking place in the Arab world, or to influence the formation of political regimes in key oil-producing countries. This process of US withdrawal from the Middle East is likely to be exacerbated by the fact that external players are now unable to keep up with the processes unfolding there. As the political forces coming to power in Middle Eastern countries become more democratic, they are often opposed to the West.

For Europe, the Middle East is undoubtedly much more important as an energy supplier and neighbouring region. However, consistent efforts by the EU to improve energy efficiency can also gradually reduce its dependence on external suppliers. The emergence of other factors, such as energy surplus in the US, the EU’s own shale gas resources, and its efforts in the field of renewables will broaden the range of energy sources available to Europe.

An interesting situation may emerge where some of the key energy consumers, the US and the EU, will be able to stop using the services of suppliers, or to begin to dictate their own terms to energy supplying countries. The latter is already partly happening (in a mild form) in the relations between the European Union and Russia as the situation in the gas market is gradually changing. Russia’s natural gas giant, Gazprom, which not long ago refused to discuss any revision of the terms of its contracts with western consumers, has now had to enter into negotiations on these issues. If oil-producing countries in the Middle East find themselves in a similar situation, their reaction may be quite unexpected. The growing demand in the rising economies of Asia can compensate for falling demand elsewhere as long as the United States does not get locked in a bitter competition with China and does not try to restrict China’s access to surplus gas resources.

Competition over conflict
Even if there are tensions and escalating lines of conflict, a big world war like those that took place in the 20th century is, in all probability, impossible in the 21st century – because of the ‘nuclear weapons factor’. The presence of nuclear weapons in the arsenals of the great powers, which waged large-scale wars – including for resources – with each other in the past, raises the risks and costs of a hypothetical combat scenario to a level so high that it negates the incentives for war. Although there has been much discussion about the total destructive capacity of nuclear weapons, their existence actually serves as a guarantor of stability in relations between the great powers. This means that the great global competition that will take shape in the coming decades will mainly unfold in the field of economic and technological capacity. Such competition will require resources as will the demands of the growing middle classes in developing countries that seek a more comfortable existence and better quality of life.
Restructuring for green growth

At the same time, there is increasing evidence that the desire to develop an environmentally friendly, green economy and to improve energy efficiency is becoming an engine of economic growth and a catalyst for new technologies. At a time of global recession, when all countries are seeking resources to reset their economies, this area of green growth presents huge untapped potential.

The efficiency of resource usage is becoming a criterion for economic success and a guarantee of strong positions in global competition. In a sense, it replaces the military-industrial complex, which has traditionally served as the engine of technological development. Countries, even those rich in mineral resources that fail to fit into this new wave will increasingly lag behind leaders that have managed to quickly adapt to the new reality. Paradoxically, if the world commodity market is reorganised, the sources of destabilisation may be unexpected. Consumers are usually interested in changing the status quo, primarily defined by resource producers, to achieve better conditions. Resource producers, on the other hand, have usually tended to want to preserve the status quo, as they had dictated the terms. However, the shift to green technologies alters this dynamic.

The need for a global approach

It is important to note that only comparatively rich and growing countries will be able to make the green shift. On the other hand, the scarcity of resources will especially hit the poorest and most troubled countries that are unable to reorganise their economies. Some of these countries will also be affected by the consequences of climate change. This is the reason that a global approach, intended to counter the expected scarcity of resources in the world, should be based on two pillars. First, it is important to achieve a balance between suppliers and consumers in the energy market, which will be restructured as demand and supply change. It is necessary to ensure that the interests of not only consumers (energy security is now interpreted primarily in this way) but also suppliers, for whom the loss of the market will be a major challenge, are taken into account. Second, there should be an international programme of assistance for the most vulnerable countries that are unable to cope with resource scarcity on their own.

All this work can be done within the framework of an organisation that would be similar to the International Energy Agency. However, it should not be established in the framework of the OECD (as the IEA), which mainly reflects the interests of consumer countries. The United Nations would be the most appropriate framework for such an organisation. In addition to its universal legitimacy, the UN has a unique experience in harmonising different approaches. In addition, the G-20, which unites countries with different types of economies, including both consumers and producers of resources, could serve as a natural forum for discussing this issue. Energy and other non-renewable resources are almost never discussed within the G-20. Russia’s attempt during Dmitry Medvedev’s presidency to propose this issue for discussion within the G-20 did not lead anywhere. However, sooner or later, resources will need to be discussed and dealt with internationally in order to ensure that the interests of producers, consumers and vulnerable countries are balanced and taken into account in a truly global approach.

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Anxiety over resources is universal. Also in China, there is much discussion about the country’s resource vulnerabilities with energy and food being two of the most significant areas of concern. The idea of security through self-sufficiency is highly attractive. However, this simple concept can sometimes disguise much more complex realities. Dramatising risks connected to the use of sources outside the country is easy. This article analyses China’s approaches to energy and food security to argue that it is important to recognise and utilise the inter-linkages between resource security and resource efficiency. While the international dimension of resource security often attracts more discussion, the bulk of China’s challenges in these areas continue to be on the domestic front.

In recent years, resource security has become an increasingly significant public policy issue in China. Indeed, there has been so much debate that it is difficult to identify one single Chinese perspective on this issue. While there is widespread concern over challenges in meeting the consumption needs of the country, there is a great diversity of views on potential solutions. In the field of energy, for example, industrialists think that low costs are as important as the security of supply, entrepreneurs see rationalisation of investment flows as key, technophiles argue that engineering is the path to pursue, and environmentalists try to reduce extraction and consumption. Also, there are many different interests involved. Foreign policy experts weigh the costs and benefits associated with the country’s dependence on foreign sources of oil, and individual consumers resist fluctuation of energy prices. This leaves politicians with the complex task of finding the best solutions and at the same time trying to satisfy as many interests as possible in the formulation and implementation of national policies in this field.

The evolution of China’s approach to energy resources

For much of contemporary history, China treated energy resources as just another set of ordinary commodities. When the country made the decision to re-join the world economy, it sought international participation in the exploration and production of oil and gas in its offshore areas. It started the first round of bidding in 1982 and the terms in a standard contract were modelled after a meticulous study of Western European and American norms. Indeed, until the mid-1990s, oil, coal, minerals, grain and other raw materials accounted for over half of China’s total exports. At that stage, the central government even prioritised increasing production for export in exchange for both hard currency and technical equipment for resource extraction.

International commentators were much faster than the Chinese themselves in raising alarm about China’s shift from a net exporter to a net importer of oil in the early 1990s. Throughout the 1980s and 1990s, only one article in Chinese language professional journals ever raised questions whether it is reasonable to trade oil as an ordinary commodity without thinking about its strategic importance. Energy security, in terms of overall policy conceptualisation, was synonymous with safety.

During the past few years, China’s approach has changed. The issue of security (defined to be reliance on supply from abroad) is increasingly significant and has become central to the debate. Geologists agree that domestic production is unlikely to increase...
significantly and China cannot expect to become a net exporter of oil or gas in the foreseeable future. Consequently, the emphasis today is on attracting foreign capital, technology and services to China for the development of its domestic energy sector, especially in the field of natural gas, shale gas, coal-bed methane and renewable forms of energy. There is still much space for further international collaboration in these areas, as well as to help increase the recovery records of existing fossil fuel fields.

**China’s international commitments**

In addition to developing its domestic energy production, reaching out to the rest of the world to supply fossil fuels is another part of China’s strategy to secure energy sources. Over sixty per cent of China’s imported crude oil comes from the Middle East and Africa. There is therefore growing debate about whether China is likely to take a more proactive diplomatic (and even military) stance in these regions in order to safeguard its largest foreign source of supply.

Such discussions and speculation are currently increasing because of the rise in domestic energy production in the United States, which will lead to a reduction of US dependency on the Middle East. Of course, there is no dearth of Chinese arguments that indicate an interest in foreign policy and even military activism in the Middle East and Africa. But such sentiments are not likely to be translated into policy action for a number of reasons.

In part, this is because the outbreak of the Middle East oil crisis in the early 1970s did not have a strong impact on China. The military and economic arrangements between the major energy producing states in the Middle East, Africa and Nato member countries weave a web of forces that help to stabilise the region. Those networks have well served China’s need in accessing Middle Eastern and North African oil and gas deposits. Regardless of the destination of fossil fuels produced in the region, the existent political and military arrangements are unlikely to undergo a fundamental change. After all, fossil fuels were only one of many factors justifying those arrangements.

Another reason is that market forces are likely to keep global energy trade stable. For the past decades, there have been continuous concerns about volatilities in the Middle East and Africa and their implication for Chinese access to energy resources. But global market forces helped maintain a constant outflow of fossil fuels from those regions. Today, the prospect of the United States becoming more energy self-sufficient, among other factors, further reduces the impulse in other parts of the world to deliberately disrupt fossil fuel production and outflow. After all, security of demand for an exporter is just as powerful as security of supply for an importer.

Therefore, a chance for China to function as an external power to restore order in those regions continues to be too remote to contemplate. Also, there is no intellectual or ideological sense of urgency in China to ‘get the Middle East right’ as in the West. China has not had a military presence in those regions in the past and, there is no credible justification for a change in security policy in the future.

**The pollution problem**

The month of January 2013 saw major cities across China under such heavy smog that meters installed to monitor urban air quality went off scale. This latest episode is a reminder that the country’s overwhelming reliance on coal as the primary source of energy supply presents very urgent challenges
for energy policy. China’s dependence on coal leads to enormous associated costs on air, water, health and quality of life. Such incidents remind us that the pursuit of resource security – conventionally defined to exclusively refer to meeting the demand for supply – is self-damaging if not enough attention is paid to efficiency and safety in resource utilisation.

At the same time, measures taken to upgrade levels of resource efficiency and safety can help alleviate growing worries about adequacy of supply.

Events such as the blackening of Beijing in early 2013 have added momentum to efforts to curtail domestic consumption. For the first time in China’s energy policy planning, a few days after the outbreak of smog, the State Council formally adopted capping total energy consumption to four billion tonnes of coal equivalent (btce) by the end of 2015. In 2012 China’s total energy consumption stood at 3.62 btce, an eleven per cent increase from 2011. To reach this target, drastic action will be required.

Hopefully, the latest initiative will lead to the streamlining of energy prices that will enable conservation efforts. However, the announced cap requires action over all forms of energy, rather than coal alone. Because coal is so fundamental in affecting domestic pricing of all forms of energy, without a targeted campaign on coal consumption, the cap risks becoming little more than a numerical exercise.

The biggest challenge for China’s energy policy continues to be domestic: how to maximise domestic and international efforts to reduce growth in fossil fuel use. China needs to focus on improving efficiency in energy consumption and give greater weight to protecting the environment. In the past, the overall goal of China’s energy policy was to ensure a secure supply of energy at reasonable prices for its economic development. Environmental protection was a simultaneous policy goal, but only a secondary priority after economic growth. A paradigm shift in Chinese energy security thinking is required. China has successfully transformed itself from a society plagued by energy poverty to one that thrives in spite of various constraints in energy supply. A focus on ensuring faster deliverables in energy efficiency is now more feasible than ever before.

Food self-sufficiency in China

The question of how China factors in the evolution of world food security dynamics has received consistent attention. For the past thirty years, China’s performance in food production repeatedly demonstrated that pessimistic predictions of scarcity were false alarms.

At the same time, Chinese government policies prioritise food security over energy security. In the context of the global rise in biofuel production, China adopted an official policy that biofuel development (including ethanol and biodiesel) should not come at the cost of crops intended for human consumption; and that land for producing food crops should not be used for fuel crop production.

In the past decade (except for in 2004) China has been a net exporter of grain. The country has achieved the government’s target of ninety-five per cent self-sufficiency. China has a significant role in the world grain trade market, which is sensitive during times of global financial volatility. In recent years, around one per cent of China’s grain has been imported from international markets. But prospects of a rise in Chinese imports cause widespread international concern, given the limited amount of stocks available for global trade. It is, therefore, desirable for China’s import levels of grain to shift only in minor and predictable ways.

Efforts to minimise the level of food imports are likely to continue, as the domestic governance framework is already in place to support this approach. In 1993, China initiated a system of provincial governors taking responsibility for the ‘rice bag’ (grain supply) programme and city mayors taking responsibility for the ‘vegetable basket’ (non-grain food supply) programme. Given China’s large size and complex and difficult terrains for domestic
transportation, food production and consumption is handled locally first, before moving onto the regional and national levels.

**Domestic agricultural challenges**

However, China faces real and long-term challenges in the field of agriculture in order to maintain food security. There is a need for continuous policy attention, financial investment, and technological advancement. The agricultural challenges facing China include: loss of cultivated land from degradation and urbanisation; uneven distribution of water resources; frequent natural disasters; impacts of climate change; vulnerable ecosystems; increased demand from population growth and improved standards of living; a small-scale agricultural economy; and an ageing agricultural infrastructure. In particular, two domestic challenges are most significant.

The first is food availability at the household level. Chronic food shortages and malnutrition in poverty-stricken provinces in the western regions are well known. But even in better-off provinces, many rural households still face challenges in affording and accessing food that is available. This means government poverty relief policies are likely to continue. The process of addressing rural poverty is a long-term task. But the same process can also help alleviate pressure on aggregate food supply security by enabling reuse of farmland abandoned for economic reasons. In other words, the urbanisation process does not necessarily have to result in a massive loss of agricultural production, as is sometimes feared.

The second major challenge is farmer motivation. Farming in much of China continues to be labour-intensive. The motivation of farmers is particularly crucial in China because rural households continue to be the bulk of the workforce in agricultural production. Average farm size is small and paddies in hilly parts of the country are unsuitable for mechanisation. Labour-intensive industrial jobs in the urban areas and other employment opportunities compete with agriculture for labour input. These and other factors make farmer motivation key in ensuring continuity and stability of grain production.

China seeks to ensure a smooth path to development and urbanisation. The emphasis on prioritising domestic sources of food grain supply is part of this overall development strategy. Developing agriculture can help ensure social stability and achieve sufficiently high levels of employment amongst the rural work force. This implies that agriculture will remain an economic policy priority. China will continue to be a reliable producer and trading partner in grain and food products.

**Seeking greater efficiency**

The biggest priority for China’s resource security remains at home. Over geostrategic questions, such as how China may relate to regions such as the Middle East and North America in the future, it is wise to contain and avoid impulses of competition for the sake of competition.

In the field of energy, ‘coal as the basic source of energy supply’ has been the motto of Chinese energy policy in the past. But this has often served as a political excuse for inaction when it comes to answering the call for improving efficiency. The good news is that the de-facto ‘grow first and clean up later’ framework is starting to change. The past approach to policy-making has reached its limit. It is time for a paradigm shift within China.

In terms of food security, China is set to continue maximising its domestic resources to meet supply needs. Numerous challenges remain, particularly as urbanisation transforms the population’s demand for total amounts as well as varieties of food supply. Despite climate change concerns, the seasonal cycle of grain production in China suggests that it is unlikely that China will experience drastic drops in domestic supply. Meanwhile, China must devote more resources to ensure greater efficiency in the use of agricultural inputs. It can reduce loss of food produced through enhancing post-harvest...
management and reduce food waste after final consumption.

Also in terms of international collaboration for resource security, the biggest priority for China should be maximising efficiency in consumption. This will help spur innovation and new technologies for resource use. Sound policy in search of resource security begins with greater efforts towards improving efficiency. For both China and the rest of the world, it will be most beneficial to utilise resource security concerns as a constant impetus for strengthening cooperation in promoting efficiency in resource consumption.

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Section two data: resource security

Although consumption levels in the emerging economies are rising, per capita consumption still largely remains low compared to the advanced economies. In terms of energy, the share of different sources varies significantly across countries, with China heavily reliant on coal. With regards to water, China’s water footprint has been comparatively low but it appears that the region may face increasing scarcity in the future. Given the importance of resources, international collaboration in this field is increasingly being recognised as a necessity with a number of recent declarations and initiatives.

**Food Consumption Per Capita: 2009**

- **Source:** Food and Agricultural Organisation

**Energy Consumption Per Capita: 2010**

- **Source:** US Energy Information Administration
Recent declarations on key resources

**UN Initiative on Sustainable Energy for All, 2012**
- Ensure universal access to modern energy services
- Double the global rate of improvement in energy efficiency
- Double the share of renewable energy in the global energy mix
- Seeks to achieve these aims by 2030. UN General Assembly declared 2014-2024 as the decade of sustainable energy for all

**G8 New Alliance for Food Security and Nutrition, 2012**
- Accelerate flow of private capital to under-developed agriculture
- Scale new technologies and innovations to increase sustainable agricultural productivity
- Reduce risk borne by vulnerable economies and communities
- In partnership with the African Union and other actors

**Istanbul Declaration of Heads of State on Water, 2009**
- Generate a global vision and framework to develop and manage water resources in a sustainable manner
- Guarantee access to safe water and sanitation for all
- Prioritise investments to increase capacity for managing water resources
- Develop new water management strategies with the effective contribution of local stakeholders, financial mechanisms, technology and innovation
The harmonious superpower? China’s role in a multi-polar world

Section two data: resource security

Water footprint definition

The “water footprint” of a country is defined as the volume of water needed for the production of goods and services consumed by the inhabitants of the country.


Water Footprint Map: 2001

Water Scarcity Forecast Map

Section three: Building regional order
Section three: Building regional order
Forging an Asian community: prospects and dilemmas

Pang Zhongying

Accompanying its domestic development, China’s foreign policy is also in the midst of a significant transformation. As part of this change, its attitude towards regional associations in Asia has evolved since the 1990s, with increasing activism and involvement in the Asian regional architecture. There is still no unified multilateral framework of coordination or control within the region. At the same time, the configuration of regional architecture remains a major issue of debate. Not only for big powers like China, Japan and the US, but also for many smaller nations in the area and for the wider world, the stakes are high about whether Asia, and more broadly the whole Asia-Pacific, can operate cooperatively as a region. This article explores China’s role in the region as well as the prospects of Asian regional cooperation.

The nature of Asian regional architecture
In order to analyse China’s role in the region, it is important to have an understanding of the nature of Asian regional architecture. Although there is a multiplicity of organisations and associations in the area, these can be characterised into two key types. The first are Asian/East Asian institutions, such as the Association of South East Asian Nations (Asean), and the second are Asia-Pacific (trans-Pacific) institutions, such as the Asia-Pacific Economic Community (Apec). During the Cold War, there were no truly regional institutions in Asia; Asean was a sub-regional exception. The United States developed and led a hub-and-spokes system of alliances with the US itself at the centre of the wheel. However, since the end of the Cold War, various diverse economic and regional institutions have been emerging in Asia.

These institutions pursue a number of aims including trade and investment liberalisation; economic development and technology cooperation; managing transnational challenges; strengthening regional peace and security; and, in some cases, attempting to build regional communities. They are characterised by three distinguishing features. The first is diversity, with multiple groupings and forums often addressing similar issues and sometimes with overlapping responsibilities. The second is informality, with most of these associations not having legally binding rules and regulations but rather serving as mechanisms for bringing groups together to discuss issues and promote agendas. The third is networking, with many of these institutions interconnected with each other and also with more specific policy issue networks across countries, such as on railways or higher education.

Each regional institution has its own mission and enjoys its own legitimacy. There is little likelihood that they would be amalgamated into one overarching framework for the region as whole. In fact, these various institutions reflect the diversity and complexity of the region.

China’s regional role
China attaches great importance to regional institutions, and has sought actively to promote regional cooperation in Asia. Asia is the only region in which all dimensions of China’s national interests, both economic and strategic, are present. To secure its regional interests and integrate with the region after the Cold War, China has been developing a regional policy and seeks comprehensive engagement in the region. Its growing faith in regionalism has been part of a broader embrace...
of multilateralism as an effective way to promote China’s interests and avoid confrontation with other powers. Given the significant geopolitical changes in Asia, China realises that regional arrangements may be an effective platform to accommodate the rise of new powers. In fact, China hopes that an integrated Asian region could serve as a foothold on its path to become a global power.

China’s role in the region in different institutions can be characterised in three key ways. The first is as a participant and supporter, a role it performs with Asean and the forums that it leads. Asean as a regional institution is a bridge to other regional institutions for China. China provided financial and policy support to Asean countries during the financial crisis of 1997-98, and relations between China and Asean have developed rapidly since. China and Asean have a free trade agreement and China was the first Asean dialogue partner to sign the Treaty of Amity and Cooperation in Southeast Asia (TAC), a key Asean security protocol.

The second is as an organiser of regional institutions. China, together with Russia, created the Shanghai Cooperation Organisation, becoming a pillar of the regional security initiative. It serves the common interests of the member countries, such as combating terrorism, separatism and extremism, and also reaches out to other countries as observers. It is now developing from a strictly security organisation to include economic cooperation as well.

The third role is as a rider (however, not a free-rider as some in the West would say), on US-led institutions. China is a de-facto rider on the America-organised regional order. In the 1990s, Apec was one of China’s main channels to link with outside economies and also provided a much-needed diplomatic channel for nurturing China-US ties.

There is much discussion about the potential role of China as the dominant leader of the region, but this is not a possibility in the foreseeable future. The United States is still the hegemon in the Asia-Pacific region and China lacks adequate hard and soft power to replace the US position in Asia. Although China has booming trade relations with Asian countries, this is largely symbolic because the majority of this trade is being conducted through foreign companies based in China and other East Asian countries. There are also too many other contenders for Asian power for China to try to pursue regional predominance. If it does so, there is a high likelihood of balancing reactions from countries such as Japan, South Korea, India and others.

Dilemmas facing China

Although China does not seek regional preponderance, it faces a number of dilemmas in the region which it needs to navigate and calibrate carefully. The first is the political dilemma of its relations with other countries. As a norm, China’s growing economic and business relations with other countries have helped it improve political relations. However, economic relations have their limits in bringing about better political relations. This can easily be seen in the China-Japan relationship, which has often been characterised as ‘hot economic but cold politics’. Many of the bilateral and even multilateral interactions between China and other countries can be described in the same way. China’s close economic relations with the US have not changed the nature of China-US political relations.

The second is an economic dilemma regarding the role of free trade and liberalisation. In the past, China deeply doubted and strongly resisted the theory and practice of free trade. But today, as a trading nation and as the ‘world’s factory’, China relies heavily on the sustainability of the free trade system for its economic growth. The country now argues against protectionism in trade and investment. But while taking advantage of China’s opening economy, other countries complain that China’s openness is quite problematic. Tensions between Google and China are being characterised by the US government as
a part of bilateral trade frictions. China’s internet censorship is now considered a new ‘trade barrier’.

The third is a security dilemma resulting from an arms race in the region. The economically booming Asia-Pacific is also a dynamic and energetic centre of an arms race. The US continues to strengthen its regional military alliances. Many other countries in the region are strong military powers in their own right. At the same time, China has to modernise and revolutionise its military in order not only to deal with the worst scenario triggered by the arms race but also to protect China’s growing overseas interests. A growth-oriented China has benefited greatly from the Pax Americana, but it has never been a part of the US-led alliance system. The US and other regional powers justify their strengthened military alliances by citing China’s military build-up.

Prospects for Asian regionalism

A second Cold War – a Cold War between China and the US – is highly unlikely. While China has benefited from a growing, open and cooperative regional environment, it has been constrained and regulated by the existing Asia-Pacific multilateral order. So, although tensions and frictions between China and the US occur, both countries recognise that it is in their interests to continue building a genuinely deeper and stronger relationship.

At the same time, given the complexity of dilemmas and challenges in the region, the need for Asian regionalism is stronger than ever. East Asia (or broadly defined, Asia) needs a political vision, ideal and project to manage international relations and political economy in the region. As Europe needs the European Union, Asia also needs an ‘Asian Union’, albeit of a very different form and suited to the particularities of the region. Indeed, ideas and debates about Asian regionalism have historic origins but these have been difficult to put into practice for a number of reasons. The Asean+3 initiative has come the closest to the practice of Asian regionalism.

However, true Asian regionalism would mean a significant revision of the geo-strategic order in Asia, which has been dominated by the United States since the end of the Cold War. In order for Asian regional cooperation to further develop, the United States has to become less dominant. Unfortunately, the US strategy of a ‘pivot’ or ‘rebalance’ to the Asia-Pacific will have a detrimental impact on cooperation in the region. The US is utilising a divide-and-rule strategy in the region. Its proposal of the Trans-Pacific Partnership (TPP) further reduces the prospects for Asian regionalism. Indeed, the US can easily use competition and conflicts between China and Japan to further undermine East Asian regional cooperation.

While East Asian institutions and trans-pacific institutions have converged, their paths and objectives have diverged. The East Asian community should be a European Union-like body. The EU does not include the US, and an East Asian community should also not include the US. The ultimate framework for East Asia is very much dependent on the policy stances of China and Japan. If they really want to build balanced and equitable relations with the US, a commonly pursued East Asian community is a necessary and legitimate choice. Such an East Asian community should not be exclusive and should be open. The EU and US achieve coordination through transatlantic institutions such as Nato. Like the EU, an East Asian community should have better cooperation and coordination through a number of trans-pacific institutions. However, the future of
multilateral institutions in Asia and the Asia-Pacific is still uncertain. Asian regional institutions will not have strong prospects if America attempts to resume its multilateral domination.

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Elements of Regional Architecture in Asia

<table>
<thead>
<tr>
<th>Name</th>
<th>Year founded</th>
<th>Current members</th>
<th>Function</th>
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<tbody>
<tr>
<td>Association of Southeast Asian Nations (Asean)</td>
<td>1967</td>
<td>Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, Philippines, Singapore, Thailand, Vietnam</td>
<td>Association dedicated to promoting economic cooperation and political stability in the region as well as advancing economic, social, and cultural progress in its member states; Free Trade Agreements with a number of third countries established (e.g. China, India, Australia); Asean Charter adopted in 2007</td>
</tr>
<tr>
<td>Asean+3</td>
<td>1996</td>
<td>Asean members, China, Japan, South Korea</td>
<td>Coordinating body for exchange between the members of Asean and three key players of East Asia; focus on financial stability, trade and economic policy (Chiang Mai Initiative)</td>
</tr>
<tr>
<td>East Asia Summit (EAS)</td>
<td>2005</td>
<td>Asean+3 members, Australia, India, New Zealand, Russia, United States</td>
<td>Forum for strategic dialogue and cooperation in East Asia, comprising all major regional powers; wide range of issues addressed such as trade, regional security, health, environment, and energy cooperation; ongoing negotiations about a Regional Comprehensive Economic Partnership (RCEP)</td>
</tr>
<tr>
<td>Asean Regional Forum (ARF)</td>
<td>1994</td>
<td>East Asia Summit members, Bangladesh, Canada, Mongolia, North Korea, Pakistan, European Union</td>
<td>Comprehensive forum designed to create a platform for constructive dialogue on political and security matters in the Asia-Pacific region</td>
</tr>
<tr>
<td>Asia-Pacific Economic Cooperation (Apec)</td>
<td>1989</td>
<td>Australia, Brunei, Canada, Chile, China, Chinese Taipei, Hong Kong, Indonesia, Japan, Malaysia, Mexico, New Zealand, Papua New Guinea, Peru, Philippines, Russia, Singapore, South Korea, Thailand, United States, Vietnam</td>
<td>Initiative for the advancement of free trade and economic cooperation in the Asia-Pacific region; three pillars: Trade and Investment Liberalisation; Business Facilitation; Economic and Technical Cooperation; ongoing discussions about a Free Trade Area of the Asia-Pacific (FTAAP)</td>
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Section three: Building regional order
Troubled transition: US-China relations and the search for regional order in Asia

Jonathan D. Pollack

These are unsettled times in Asia and the Pacific. Despite the region’s extraordinary economic growth, increasing social and technical connectivity, the absence of major military hostilities, and innumerable pledges of heightened international cooperation, state behaviour does not lend much confidence about the possibilities of enhanced regional peace and stability. Beneath a veneer of international cooperation and an undoubted interest in economic advancement, competing national agendas are increasingly apparent, as the major powers and regional actors seek to protect their separate interests and manoeuvre for geopolitical advantage. There has also been an appreciable enhancement of regional military capabilities and a growing willingness of states to employ such assets in disputes over sovereignty and administrative control. Thus, the building of a new regional order appropriate to 21st century realities remains an urgent but unfulfilled policy challenge.

Five principal issues are shaping the strategic contours of the Asia-Pacific region: the absence of an agreed upon concept of regional order (especially between the United States and China); the resurgence of long-dormant nationalist rivalries; the resurfacing and intensification of contested zones and contested history, particularly in the East Asian maritime domain; an accelerating arms competition and the readiness of states to advance their political and security goals by employing these new capabilities; and the risks of disequilibrium and major crisis, in particular on the Korean peninsula. Despite the presumed attention to Asia as a whole, national agendas and bilateral disputes continue to predominate, with modest attention to the possibilities of a transformed security order. States appear to be principally pursuing autonomous power goals that could preclude or severely complicate movement toward a more inclusive definition of regional stability and security.

Centrality of US-China relations

The long-term Sino-American relationship is the largest factor defining the Asia-Pacific future and is the predominant focus of this essay. US-China relations are deeply enmeshed in all the major issues that presently shape regional security. Optimists draw attention to the unprecedented bureaucratic, commercial and societal interdependence between the US and China and the frequency with which leaders meet and communicate. In the aftermath of the US presidential election and the completion of China’s succession process, Barack Obama and Xi Jinping have both reaffirmed earlier pledges to build a durable, cooperative bilateral relationship. But there are pervasive suspicions voiced within both countries and an ever increasing economic, political, and security grievance list, with particular attention now focused on illicit activities in the cyber domain. Many Chinese observers perceive a larger underlying US design to frustrate or deny China its rightful due as an ascendant major power, even as the US insists that it seeks China’s full incorporation in a rules-based international order. Numerous American analysts express parallel fears that an increasingly powerful China will be intent on undermining the US position and presence in Asia and the Pacific, ultimately enabling Beijing to develop a dominant position in relation to all its neighbours.

Washington and Beijing recognise that the transformation of both economies is far more likely to dominate leadership agendas over the coming
decade. However, both countries acknowledge the need for accommodation and mutual legitimation if they are to avoid intense strategic competition, or worse. There is an imperative need to establish a sustainable centre of gravity in bilateral relations. Without it, the divisive or conflicting elements in the Sino-US relationship could increasingly dominate politics in one or both systems. Though neither power could possibly favour overt confrontation, the gestational elements of a longer-term political-military competition are already evident. US and Chinese strategic concepts do not necessarily mesh well. The United States continues to rely on a political and security framework first developed in the Cold War, and subsequently modified to reflect the maturation of America’s Pacific alliances and the effects of globalisation on formerly autarkic economies (most notably China but also extending to India and Vietnam). But Beijing regards many US-led security arrangements as designed to inhibit and otherwise frustrate realisation of its political and security objectives.

America’s rebalancing strategy
The Obama administration’s ‘rebalancing strategy’ bears directly on Chinese suspicions. The US argues that these policy shifts are fully warranted after a decade of debilitating conflict in the Greater Middle East and appropriate to the Asia-Pacific’s increasing centrality in global politics and economics. The US contends that the rebalancing strategy is not overly weighted to the military dimension of US power and is not intended to undermine or marginalise China. It further claims that a reconstituted US regional role must draw as much or more on the political and economic dimensions of American power, including the ability of US firms to more credibly enter markets still insulated from equitable economic competition. But Chinese strategists express wariness or incredulity that US policies have not been pursued with China in mind, especially as the US buttresses its regional military capabilities and enhances political and security ties with states voicing growing wariness about the growth of Chinese power.

By contrast, most American strategists seem skeptical about China’s advocacy of a new concept of major power relations. To American ears, such a concept seems far too formulaic and content-free to serve as a framework either for US-China relations or for China’s relations with neighbouring states. Beijing seeks to reassure the US and others about its long-term intentions and its supposed adherence to peaceful development, but the military component of Chinese power is increasingly visible and active. China is not the only Asian state whose military capabilities are coming of age. Without agreed upon rules of the road between China and its Asian neighbours, the prospects for a peaceful transition in the Asian security order seem much more problematic.

In the view of the United States and many of Beijing’s neighbours, China’s preference for broad principles to guide international relations is insufficient to build a more mature and credible security architecture in Asia. A more lasting approach will require room at the table for all involved powers, including the United States, and rules of the road to regulate their conduct. Without such strategic understandings, the possibility for meaningful security cooperation (especially between the US and China) will be far more remote.

American and Chinese policy-makers insist that their countries are not fated to repeat the history of conflict between established and rising powers,
but it is not clear how this goal can be achieved. The economic and strategic weight of America and China – the world’s two largest economies – will increasingly differentiate them from the capacities of all other powers. In addition, the Chinese economy seems very likely to surpass the United States in its absolute size over the next decade or decade and a half. But this dynamic does not constitute a G-2 world or (even less) a rivalry akin to Soviet-American relations in the Cold War. The challenge for both is to limit the possibilities of mutual antagonism, forego paths that lock both into an open-ended military competition, and seek to create a shared strategic space in Asia and the Pacific that does not impinge on either country’s vital interests or marginalise the interests of other various regional actors.

The wider neighbourhood

This is easier said than done. Some of the largest questions concern the strategic positions of China’s neighbours, which simultaneously fear a US-China duopoly, the prospect of a widening US-China strategic divide, or a diminished American role and presence that leaves China’s power largely unchallenged. There is also the singular challenge posed by North Korea, East Asia’s conspicuous strategic outlier, whose nuclear and missile pursuits and repeated threats against its neighbours pose an acute risk to all its neighbours, including China. But Beijing until now seeks to stand apart from deeper collaboration to control the risks to peace on the Korean peninsula. It remains a major test of whether China’s leaders are able to transcend history and contribute fully to realising collective goals in regional security.

None of China’s neighbours desire an either-or choice between the US and China or to be enveloped in a larger Sino-American strategic design. But growing numbers of Asian states express private wariness about Chinese strategic intentions. They fear that China’s growing economic weight and enhanced military capacities could trigger Chinese overreach, even as China insists that it will not diverge from the path of peaceful development. Regional states contend that the growing support for the US military presence and enhanced security collaboration with the United States are needed to maintain longer-term power equilibrium in Asia, not to provoke or contain China.

Amidst the uncertainties, suspicions and unresolved legacies of history, a new regional order needs to be constructed. Is there sufficient determination to create such an order, and what are the consequences if the states of the region (and the United States and China in particular) are not equal to the task? These issues will be central to any serious discussion of the regional future and the building of a framework for lasting security and stability.

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Section four: China rising
The harmonious superpower? China’s role in a multi-polar world

Section four: China rising
Building communities of interests: the way to a better future for the world

Wu Jianmin

Under the leadership of Deng Xiaoping, China entered into a process of fundamental economic reform in 1978. The new policy orientation adopted at this time can be characterised as reform and opening-up to the outside world. It is by no means accidental that this concept consisted of these two distinct elements.

First, there are several reasons why China sought to open up its economy after long years of stagnation and decline. For the most part of the past two thousand years, China was a leading power in the world. In economic terms, China's GDP accounted for about thirty per cent of global GDP until 1820. Contrary to this, China lagged far behind the industrialised countries in the modern age. Before the economic reform programme was adopted in 1978, China's GDP accounted for only less than two per cent of global GDP. This drastic decline induced the Chinese leadership to enter into a lengthy process of debate and reconsideration. Finally, Deng Xiaoping recognised that it was self-seclusion that led China to backwardness and prevented economic and social progress. Opening-up to the outside world was therefore perceived as a means of catching up with the advanced economies of that time.

The second element, reform, is derived from a different reasoning. Even though there are different views on this phenomenon, globalisation is considered the trend of our time beyond doubt. China, just like any other country, has to embrace the processes of increasing interconnectedness in order to make use of globalisation to the benefit of economic progress. These two considerations formed the basis for Deng's reform package.

China's re-emergence

Its enormous success becomes clear when looking at developments of the past 35 years. In 1978, China's GDP amounted to 268.3 billion dollars, its rank was the 15th in the world. In 2012, China's GDP had gone up to 8.3 trillion dollars. The country now occupies the position of the second largest economy in the world. In thirty-four years, China's GDP has increased almost thirty-one times. This is unprecedented in the history of the economic development of the world. This strong, steady and sustained growth has brought tremendous improvements in the living standards of the Chinese people.

I have experienced these developments myself. Before 1978, China suffered from wide-spread scarcity of consumer goods. We were short of everything. People of my age know how bad things were in those years. We found food and consumer goods less and less available. They were eventually rationed. Coupons were needed to buy almost everything. But today, rationing coupons have long disappeared. For the Chinese, this is a sea change.

The reforms and their positive effects on the country's economic performance have had implications on China's position in the world. Undoubtedly, China is rising. This rise is perceived in different ways around the world. While some reactions are positive, others look at the country's re-emergence with a degree of fear and insecurity.
People are trying to understand the implications of China’s rise. For this, they need to have a clear and balanced picture of the country. This is precisely what this Foresight China conference aims to help provide.

The concept of a peaceful rise
Zheng Bijian, Chairman of China Institute for Innovation and Development Strategy (CIIDS), was the first to put forward the concept of China’s peaceful rise. This concept was accepted by the Chinese leadership and subsequently incorporated into China’s international strategy. The idea of peaceful rise can include a variety of policy objectives. To my understanding, they consist of three ‘Noes’ and three ‘Yeses’.

The first ‘No’ is no expansion. It means that China will never follow the footsteps of the former colonial powers. The second ‘No’ is no hegemony. It means that China will never follow the footsteps of the former Soviet Union. The third ‘No’ is no alliance. It means that China will never enter into alliance with any country. In the eyes of the Chinese, alliance is something of the past. The policy of no alliances is not only a good policy for China, but also for the world. Should China enter into alliance with other powers, a new Cold War would start. Everybody would be a loser.

The first ‘Yes’ means yes, we want peace. Peace is the *sine qua non* for development. We need peace more than anything else to modernise China. The second ‘Yes’ means yes, we want development. China, as well as the world, is facing daunting challenges. Development can provide solutions. The third ‘Yes’ means yes, we want international cooperation. We are engaged in a huge endeavour, which is the modernisation of the country. We are fully aware that in times of globalisation no country can achieve modernisation in isolation. International cooperation is a must. To make international cooperation lasting and sustainable, we have to conduct it on the win-win basis.

Communities of interests
Starting from the concept of peaceful rise, Chairman Zheng Bijian further developed his thinking. He holds the view that in international relations, we have to identify convergent interests with other countries. It is clear that every country pursues its national interests, but in a globalised world different countries find their interests are increasingly overlapping. On the basis of these convergent interests, we strive to build communities of interests, which in turn will deepen interdependence among the countries concerned. Consequently, the fundamentals of the relations between the different actors will be significantly strengthened and the countries will be in a better position to deal with their differences and discords. Building communities of interests is neither propaganda nor utopia. This is evident for a number of reasons.

First, the concept is based on the reality of our time. In the past thirty-five years, China did very well in catching up with the industrialised countries of the West. As outlined above, its success would not have been possible if its door had remained closed. In other words, international cooperation has proved to be indispensable for the country’s rise. China succeeded because it did not keep the rewards of its economic growth for itself but shared them with the rest of the world. As a result, a lot of communities of interests have been built between China and many other countries. The process of European integration provides us with another wonderful example. Through building communities of interests, the Europeans succeeded not only in making war impossible between Germany and France, which had fought numerous wars over centuries, but also in bringing prosperity to their continent.

Moreover, the concept corresponds with two factors that bring mankind together. The first is interdependence. The world has never been as interdependent as today. The relationship of China and the United States makes this very clear. Without
a doubt, China is profoundly different from the US on a number of levels. However, from Deng Xiaoping to Xi Jinping, all Chinese leaders believe that the common interests between China and US outweigh the differences by far. Some people consider the China-US relationship similar to that between the US and the former Soviet Union. This is clearly a misperception as the two relationships are fundamentally different in their nature. In the US-Soviet relationship, confrontation was the predominant feature. In contrast, cooperation is the predominant feature in the China-US relationship, in spite of competition and differences between the two countries. A look at bilateral trade figures supports this claim. At the height of US-Soviet relations, the trade volume between the two countries amounted to four billion dollars. In 2012, China-US trade amounted almost to five hundred billion dollars.

The second factor is the common challenges that the world is confronted with. They have never been as severe as today. In face of challenges such as climate change, terrorism, pandemics, drug trafficking and others, no country, however powerful it may be, is able to address them alone. As a result, mankind is bound to unite to address these challenges. Expanding convergent interests and building communities of interests is a brand new concept. Personally, I am happy to see this concept enjoying global sympathy and gaining more and more support around the world.

Looking around the world, we can see two mega-trends competing with each other. One stands for peace, development and cooperation. This is the trend of our time. The other trend stands for Cold War-style geopolitics, confrontation and conflict. This is the trend moving backwards to the past. The competition between these two mega-trends will decide the destiny of mankind in the 21st century. By pushing for expansion of the convergent interests and building communities of interests, we Chinese firmly support the first trend. We believe that this concept points the way to a better future for the world.

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China’s resurgence: navigating the duality of global order

Rosemary Foot

The resurgence of China represents one of the great transformations of our age. The global system has not witnessed such a rapid growth in material power since the rise of the United States in the late 19th and early 20th centuries. Understanding the implications of this change in fortunes is complex and has generated high levels of uncertainty. Most prominently, there is uncertainty about how China will use its new-found material strength, and how other states and peoples will react to that rise in power. But there is also uncertainty about the extent to which our analytical categories can usefully explain the implications of and help provide a sensible response to the transformation that we are experiencing.

The complexity of the current global order is understood even if its implications are hard to evaluate. The global order is marked by changes in the distribution of material power and political influence which have been seen to benefit some states more than others. But it is also notable for the extent to which states and peoples have become more deeply interdependent, subject to informal and formal global governance mechanisms designed to address the collective problems facing the planet, and which constrain the exercise of power.

G. John Ikenberry put the issue succinctly in 2012: “There are deep sources of conflict and mistrust generated by the anarchic and competitive structures of world politics. But there are also deep sources of stability and cooperation generated by the interdependence and mutual vulnerability that come with living in the modern era.” China’s rise needs to be interpreted in relation to these dual forces. Moreover, the presence of these twin influences should make us question the easy binary description of rising powers like China as either revisionist or status quo in their orientation towards the norms of global order. China’s resurgence has occurred at a historical juncture where states face global challenges that cannot be satisfactorily dealt with on a unilateral basis. But its position as a relatively powerful state participating in global and regional processes means that it has now become crucial in the shaping of many of those processes, sometimes as a result of its purposeful action and at other times as an unintended by-product of its actions.

Power transition

Some analysts ignore this duality in global politics. They argue instead that a power transition is underway that has rather predictable and ominous consequences, or that shifts in relative power imply a future Chinese hegemony despite the interdependence that imposes constraint. From this perspective, a transition in material power from West to East, or more specifically from the United States to China, suggests that major conflict between the leading protagonists cannot be ruled out. The argument runs that when a dissatisfied power catches up with and even begins to overtake the dominant state in the global system, the newly rising state is likely to spark a conflict. Like Germany and Japan at the end of the 19th century and into the early 20th century, China’s increasing material resources coupled with a sense of dissatisfaction with regard to its position in the global hierarchy is presumed as likely to trigger violence. Less apocalyptically, other analysts argue that even if war is unlikely, China’s

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resurgence will inevitably constrain the options of other states — even the most powerful among them, like the United States. These perspectives often draw on the macro-economic data that illustrates China’s resurgence — from its arrival as the second largest economy in the world in 2010, to holder of the largest foreign exchange reserves at over three trillion dollars. Trading levels have advanced from thirty-eight billion dollars in 1980 to over 3.6 trillion dollars in 2011. China is now the first or second largest trading partner of seventy-eight countries compared with the year 2000 where it was the first or second largest trading partner of only 13 countries. Since the period of reform and opening-up in late 1978, GDP growth levels have often been over ten per cent and even in 2012 stood at about eight per cent. All this has meant that more than 300 million Chinese have been lifted out of poverty. Inevitably, it also has given Beijing new forms of influence especially among states that have come to be more reliant on it as an economic partner.

While many of these changes in China’s fortunes are often applauded, some governments in the global system, and especially some among China’s neighbours, have grown alarmed about the presumed potential leverage this enhanced economic power offers to the Chinese leadership. Moreover, its emergence as a dominant economic power has prompted a reorientation in its strategic outlook, the implications of which feed into the general uncertainty that the rapid resurgence of China has generated. For example, China’s high levels of growth have been greatly dependent on foreign trade and investment. This has generated a Chinese interest in protecting the sea and land routes that transport the resources on which that economic activity depends as well as the goods that will help to pay for those resources. China has emerged as the second largest oil consumer in the world and it has been searching in its region and further afield for new sources of supply and for ways to guarantee safe transport of those energy resources. Increases in defence expenditure have accompanied these changes. China now has the second largest defence budget in the world, although it remains a distant second to the United States. Given that intentions are difficult to read, external actors may well assume that the rising state’s strategic intentions are offensive rather than defensive resulting in a security dilemma, where China’s search for security prompts greater insecurity elsewhere in the global system, and especially in its own region.

Interdependence and mutual vulnerability
This depiction of the implications of China’s resurgence for global and regional order is narrow and incomplete, however, and needs to be tempered by reference to the processes of globalisation and the constraints that these impose on the Chinese state. Power diffusion rather than power transition may actually better describe the current condition of the global order: other states apart from China have risen in power and non-state political actors complicate the world in which the state operates. Moreover, global actors face a range of collective challenges including the negative consequences of climate change, the need to prevent the proliferation of weapons of mass destruction, the spread of infectious diseases, and the requirement to develop regulations to control global financial activities. However, here I focus on the impact of globalisation in the area of production processes because of the central role that China has come to play in the global political economy.

State Councilor Dai Bingguo undoubtedly saw his essay “Adhere to the Path of Peaceful Development”2 in 2010 as a political intervention to challenge the argument that as China’s relative material power has grown it has become more assertive — even aggressive — in trying to further

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2 Dai Bingguo, ‘Stick to the path of peaceful development’, China Daily, 13 December, 2010
its foreign policy objectives. However, despite his political intent, a number of his points are well taken. The world has indeed undergone “extensive and profound changes” as a result of “economic globalisation and development of information technology.” Dai went on: “Countries are more closely linked and interdependent with their interests more closely integrated than ever before. … No country, even the most powerful ones, can stand alone and survive.”

China’s rise to power has strengthened economic interdependence, especially in its own region. As John Ravenhill has carefully documented, the regionalisation of production networks have been the principal engines of growth in Asia, including China’s growth, and have led to high levels of intra-regional trade in components. Product fragmentation has been a particular feature of the global IT and electronics industries and this fragmentation has bound together China, Japan and the other countries of East and Southeast Asia in important ways. For example, nearly half of Japan’s electronics’ output is put together in other Asian countries, including a large percentage of that output in China itself. Given that countries in this region have long regarded economic development as a vital contribution to state and regime security, and performance legitimacy has become recognised as key to the survival of the Chinese party-state, any government would have to think extremely hard before it embarked on war to attain certain policy objectives. The cost-benefit calculation tips the argument strongly in favour of maintaining stability and managing conflict.

Those who argue that similar arguments about economic interdependence putting a lid on violence were made prior to World War I disregard a key difference. Today, this networked form of interdependence means that countries at war would not only lose export markets vital for growth, but much else besides. They would also lose access to inputs that are critical to their wider production processes, and to distribution and marketing channels. The overall effect of this would be seriously detrimental to a government concerned with maintaining economic growth and protecting its political system.

Navigating duality

How does a resurgent state like China, committed to economic development, concerned about its relative power status in global politics, and perplexed about the best means of navigating its way through the current world order behave in order to reach the outcomes it desires? China is tempted to use its newfound strength in ways that are thought likely to heal old sores—for example, through the resolution of sovereignty disputes in its favour, or inclusion in a great power club via promotion of multi-polar power structures. But Beijing is also aware of how the globalised, post-Westphalian world with which it interacts offers it further opportunities for advancement even as it might constrain its policy choices.

Beijing has tried to square this circle by spelling out its core interests and claims that brook no violation — territorial integrity, national unity, economic development, and maintenance of a political system led by the Chinese Communist Party. At the same time it has set out to portray the country as a supporter of global norms that attract a reasonable degree of consensus in the global system. For example, it has retained its faith in the UN Security

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Council as a venue that both accords it special status as well as a degree of prestige associated with adherence to the UN Charter. But where globalised processes appear likely to push it in directions that threaten its core domestic interests, it is those domestic interests that will win out over any concern for the wider global or regional order. Where global norms are seen as intrusive upon and incompatible with important domestic values and interests, Chinese behaviour is unlikely to be consistent with them. These instances of incompatibility matter more in an era where its power and influence have increased. Any failure on China's part to adhere to global norms threatens to weaken the ability of these norms to shape and constrain the behaviour of other political actors in the global system.

China’s focusing on global or regional order through a domestic lens is also responsible for one other feature associated with contemporary state behaviour towards Beijing. That domestic focus in part accounts for the ‘hedging strategies’ that many governments have adopted. They have developed interdependencies of various kinds with China through involving it in multilateral institutions, economic interactions, and social and political exchange. At the same time, they have combined this engagement with forms of deterrence in case the egoistic state interests of Beijing prevail over a broader conception of interest.

Uncoerced leadership of its region will depend greatly on Beijing’s ability to reassure others that it can look beyond the immediate needs of the Chinese party-state. In the absence of this development, and in the context of the dualities discussed above the nature of the transformation associated with China’s resurgence will not be settled any time soon, but will result in a continuing and difficult series of negotiations.

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