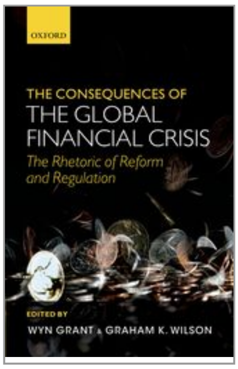

The Consequences of the Global Financial Crisis: The Rhetoric of Reform and Regulation
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Paradigm(s) Shifting? Responding to China’s Response to the Global Financial Crisis

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Abstract and Keywords

This chapter considers how China responded to the impact of the global crisis, and the subsequent debates over what this response means for the balance of power in the global order. A massive injection of funds through both official stimulus packages and an expansion of bank loans helped overcome a sharp drop in exports in the short term, but reignited debates over the structure of economic power in China, and the need to develop a new mode of growth promotion in the long term. Despite some problems related to asset bubbles and increasing bank debt, China’s ability to bounce back quickly from the impact of the crisis has cemented China as a leading actor in attempts to reform global economic governance, and has led many to rethink the efficacy of strong state-led developmental strategies vis-à-vis (neo)liberal alternatives.

Keywords: China, export-led growth, developmental state, global crisis, power transition

Introduction

Identifying clear epoch-changing events and dates is a difficult task, so we need to exercise caution when considering the direct impact of the crisis on the distribution of global power. What Mahbubani (2008) called an “irresistible shift in global power to the East” was identified before the onset of the crisis, and as Nye (2010) argues, we have not come to the end of US global power just yet. It will also take many years before we know the long-term consequences of the crisis—recoveries might turn out to only be temporary, debt problems might continue and spread, and bubbles might appear that need to be deflated (if not burst).

Nevertheless, the crisis has thrown ongoing processes of change into the spotlight, accelerating some of them and through crisis in the heartlands of the neoliberal capitalist world, has arguably added a new dimension to the dynamics of this power shift. For very good reasons: China is widely considered to be the major "beneficiary" of these shifts. The crisis has shown the robustness of the Chinese economic system and the state's ability to mobilize resources to support national goals, has increased China's relative financial power, and has firmly established China at the center of global politics and as a key actor in any attempts to reform the structure of global governance. China already had the world's largest stock of foreign currency reserves before 2008, and emerged from the crisis with the three biggest banks in the world (measured by market capitalization) (Wines and Wong, 2009), as the world's biggest exporter, and as the world's second biggest economy,[1] increasing its contacts with economies across the world in the process. Whatever happens **(p.227)** domestically over the coming years, the sheer size and scale of China—its population, its economy, and its resource needs—will inevitably impact on individual countries, and the global political economy as a whole.

This chapter begins with a consideration of the way in which the Chinese authorities responded to the crisis with a range of measures that resulted in the totemic target of 8 percent growth being achieved with something to spare. While many outside China see this success as an example of the benefits of following a Chinese "model" of development, within China itself the assertion that the crisis actually highlights the key deficiencies of this model has considerable purchase (Yao, 2010). So too does the argument that the response to the crisis has actually exacerbated some of the preexisting structural problems in the Chinese economy (Ding, 2010). So at the same time as China seems to be shifting the dominant global development paradigm, China seems to need its own domestic paradigm shift. But three decades of economic change have created a political economy that seems to have growth (rather than development) impulses written into its DNA. Moreover, while the Chinese *state* remains a crucial actor, interests and dynamics have been created that restrict the central *leadership's* freedom of action and their ability to shape China's economic future as they would like.

There is no necessary contradiction in thinking of the crisis as increasing China's global power while also highlighting domestic fragilities. To be sure, much of the popular writing on China tends to congregate around polarized extremes—either China's inevitable superpower status or an impending implosion and collapse. But this chapter echoes the broad consensus within the Chinese studies community that China's continued rise and what this means for the world will be largely determined by how it handles these “obstacles, deficiencies, and uncertainties” (Wang, 2009: 156).

China’s Response to the Global Financial Crisis

China’s Response to Whose Crisis?

In September 2008, the British journalist and historian Max Hastings (2008) referred to the then unfolding crisis in the United States and parts of Europe as a “Western” one.[2] That this crisis subsequently came to be known as a global crisis is more than just a matter of semantics and is important here for two main reasons. First, the nomenclature of the crisis is important in establishing and/or accepting who or what is to blame. This takes on an even greater importance in light of the widespread feeling in Asia that the United States used its power in global institutions to “unfairly” attack East Asia, or punish the region for following illiberal forms of non-Western capitalism after 1998 (Stubbs, 2011). It forms part of what Chalmers Johnson (1998) termed a “clash **(p.228)** of capitalisms”; a clash that seemed to have been decided in favor of the West in 1997, but given the rise of China and crisis in the neoliberal model has (at the very least) been reignited.

To make matters worse, there was an increasing feeling in China and other parts of Asia that the West was looking to externalize blame for the crisis. As some analysts began to conclude that the real cause lay in systemic global imbalances between deficit and surplus economies (Dunaway, 2009), attention turned from the occident to the orient, focusing in on the consequences of maintaining “managed exchange rate policies” (Astley et al., 2009: 180). Not surprisingly, China’s exchange rate policy came under close scrutiny, with calls for the United States to label China a “currency manipulator” and take punitive action through the International Monetary Fund (IMF) and World Trade Organization (WTO) (Bergsten, 2010). Perhaps China’s mercantilist strategy was even the real root cause of global imbalances (Wolf, 2008).

So the idea of a “global crisis” was taken as a means of deflecting attention away from failings of the Western way of doing things. As Mahbubani (2011) argues:

> Most crises are known by their origin, from the Mexican peso crisis of 1994/5 to the Asian crisis of 1997/8. Given there is no doubt who caused our world’s latest troubles, it should adopt its logical name: the Western financial crisis.

China’s top leaders, including Wen Jiabao (2009), were also quick to assert that the origins of the crisis were not just Western, but specifically rooted in the failure of American economic regulation and the “blind pursuit of profit.”

Second, while the crisis has had a clear global reach, impacting on the economic fortunes of economies across the globe, it is not a global *financial* crisis as such. As we shall see, in the longer term, China’s response to the crisis has generated financial problems that need to be dealt with. But while these problems are serious, the nature of the Chinese political economy makes them somewhat easier to deal with than might otherwise be the case. Returning to the idea of clashing capitalisms, those states like China that had not undergone full financial and currency liberalization and had large foreign currency reserves fared relatively well and had a "good" crisis. It was a specific form of financial regulation (or lack of it) that was in crisis—this was a "transatlantic financial crisis" (Terada and Ong, 2011) with global economic implications.

China's Response: Dealing with Declining Demand

So China, responding to the crisis in 2008 and 2009, did not deal with impending financial collapse, but instead utilized a strong financial situation to deal with "real economy" challenges caused by a collapse in exports. Chinese exporters had already complained about narrowing profit margins **(p.229)** in early 2008, as the impact of a rising renminbi (RMB),[3] cutbacks in tax rebates, and rising wages hit low-tech processing export industries. These challenges were exacerbated as declining demand in the West turned a 21.9 percent year-on-year growth in exports in October 2008 into a 2.2 percent reduction in November—not a reduction in the rate of growth as had happened in the 1997 Asian crisis, but actual negative figures. This was followed by eleven months of continued falls with the overall figure for 2009 showing a 16 percent decrease on 2008. Around 20 million migrant workers are thought to have returned home as factories closed; and though some of these were subsequently reemployed, and the scale of China means the percentage of the overall workforce affected was relatively small, in numerical terms no other country got close to the loss of jobs that the crisis caused in China in 2008 (Zhao and Liu, 2010: 14).

With such factory closures increasing concern over the relationship between unemployment and social stability (Wong, 2008), the government announced an RMB 4 trillion stimulus package on November 9—at the time just under US$ 590 billion. The announcement was rather short on detail and subsequently appeared to be less impressive than at first sight; some of the funding had already been pledged as part of the Sichuan earthquake recovery strategy, and most of the money was meant to be provided by local governments from unspecified sources (Dyer, 2008). But it served an important role in signaling a rather dramatic about-turn in policy. Up to the onset of the crisis, the main aim of macroeconomic policy was to control inflation and slow rates of growth to more manageable and sustainable levels and bring local authorities under closer central government control. This had not proved to be an easy task—for example, despite increasing the bank reserve ratio ten times in 2007, investment in fixed assets actually increased, and Wen Jiabao's targeted growth rate to 7 percent was exceeded by almost half as much again. The announcement of the stimulus package brought this strategy to an abrupt halt—for the time being at least—and the subsequent Central Document 18 effectively gave the green light to authorities at all levels to do whatever it took to promote growth (Naughton, 2009).

In addition to the central government initiative, China’s local governments announced their own stimulus plans that collectively amounted to RMB18 trillion (Yu, 2009: 10). As this was roughly 53 percent of the GDP figure that China finally achieved in 2009, it might be that symbolism was more important than statistical accuracy in some of these announcements as well. But while the actual fiscal stimulus figures might be a bit “fuzzy,” what is clear is that huge amounts of money were pumped into the economy through government-led initiatives of various kinds focusing on infrastructure developments (particularly, but not only in rural China), environmental protection, support for cheap housing, and increased provision for health, **(p.230)** education, welfare, industrial and rural innovation, and R&D. Domestic consumption was also supported through subsidies for rural dwellers, tax breaks on some purchases, and unofficial encouragement for state entities to not just go out and spend, but to “buy Chinese.” And support for exporters was also stepped up with China’s exchange rate policies once again coming under close international scrutiny and criticism.[4]

The expansion of bank credit played a key role in funding much of this expansion. Controlling the spending of local authorities had been a key component of macroeconomic prudence prior to the outbreak of the crisis. Indeed, throughout the post-Mao era, there has been a tension between local governments and the center over how best to arrange financial authority and responsibility—some might even argue through the whole history of the People’s Republic of China (PRC). With local governments being told to take their share in boosting the economy, and with banks not only being allowed to lend more money but also incentivized by the interest rate system to do so (Lardy, 2010: 1), then the conditions were ripe for an expansion of loans to local governments. Standing in the way were legal restrictions that prevented local governments from formally taking such loans—so they did it indirectly via various forms of locally owned companies known as Local Investment Platform Companies (LIPCs) (difang rongzi pingtai gongsi 地方融资平台公司). The exact number of such companies is not clear; when the National Audit Office (NAO) surveyed the combined debt of local governments in 2011, it investigated 6,576 of them (NAO, 2011), but the People’s Bank of China’s (PBOC) analysis of development in China’s different regions reported 10,000 in total at provincial, city, and county levels (PBOC, 2011: 6).

By the end of 2009, new bank loans in China had reached more than double the stimulus package at RMB9.6 trillion, with a further RMB7.96 trillion of new loans lent in 2010 (Osborn, 2011). LIPCs spent 62 percent of their collective money on infrastructure projects and 11 percent on land purchases (NAO, 2011). Given that they received about 80 percent of their money directly from the banks, this means that roughly half of the new loans disbursed in 2009 funded local government infrastructure projects via these LIPCs (Wang, 2010).

Responding to China’s Response: China’s Achievements and Challenges

In as early as January 2009, Wen Jiabao felt confident enough to proclaim that “we have achieved initial success from the policies we adopted to counter the financial crisis” (Waldmeir, 2009). Although export growth continued to fall, growth had slowed but not collapsed, and a sense of cautious optimism began **(p.231)** to emerge as the dominant sentiment (supported by the way in which the statistics were reported in the media). Although the first quarter growth rate of 6.1 percent was the lowest ever recorded in China (such quarterly records were first reported in 1992), the fact that it was higher than most expectations reinforced this “glass half full” way of looking at things (Rabinovitch and Zhou, 2009). With the growth rate rising each quarter, exceeding 10 percent in Q4, the much touted target of 8 percent annual growth was ultimately achieved (and surpassed) with relative ease.

China’s leaders identified a problem, put in place measures to deal with it, and attained their immediate objectives; in these terms the response was a great success. As we shall see, this success subsequently generated a number of challenges—pumping so much money into an economy so quickly without generating any problems at all would be all but impossible. But before moving to consider the consequences in more detail, it is important to repeat Lardy’s reminder (2010: 3) that “the alternative to the massive stimulus program was an even sharper drop in economic growth.” Such a decline might potentially undermine confidence in the leadership’s ability to deliver on its promises; 8 percent growth simply had to be achieved. So the costs of responding to the crisis have to be balanced against the costs of not acting.

Even before the impact of the global crisis began to be felt in China, there was a growing consensus that it was time for a paradigm shift as the existing mode of growth promotion was neither economically nor environmentally sustainable. Even in the short term, the way that growth had been attained had resulted in increasing economic polarity the separation of economic activity from the social base of society; as the economy grew, so did the number of officially recorded mass demonstrations (Chung et al., 2006). In 2004, the Chinese Communist Party (CCP) central committee came up with a rather damning assessment of the party’s own ruling capacity (zhizheng nengli 执政能力) (Central Committee, 2004). The following year, a special Central Party School report concluded that inequality had reached the “yellow alert” level, and was still rising toward a “red alert” level threatening serious political disorder (*People’s Daily*, 2005). The existing “model” was thus reaching the limits of its useful life with the danger of a slide into a Latin American-style experience of economic stagnation, domestic social polarization, and dependence on the global economy (Zha, 2005). The solution was to move away from the mode of growth promotion that had dominated for many years toward a new "scientific" concept of development (科学发展观 kexue fazhan guan) and a new political paradigm that reconnected the party with the people as "a matter of life and death" (生死存亡 shengsi cunwang).

"Scientific" here refers to the application of guiding principles to develop strategies that start from considering the actual impact on real people rather than simply the contribution to raising gross national product (GNP). So, for **(p. 232)** example, policies that might lead to a higher GNP but which also lead to environmental degradation and perhaps exacerbate inequality are not scientifically derived. Three features of this "unscientific" development model are worth considering in more detail here. The first is the consequences of the way in which China had reengaged with the global economy. The last two, the role of local governments as managers/regulators of Chinese economic activity and the problem of bank debts, are very much intertwined and dealt with below in a single section. All three were important in changing thinking on long-term development trajectories, and to varying degrees the global crisis undermined (initially at least) attempts to bring about fundamental change.

Dependence on the Global Economy?

The global crisis was not the starting point for thinking of the long-term benefits of global engagement in China—it was a debate that had been ongoing for a number of years. But as exports dropped in 2008 and 2009, the consequences of the crisis brought these debates back to the fore, questioning not just the wisdom of China's global economic strategy but of the very basis of economic activity. Part of the perceived problem is what we might term the low quality of production in export sectors. With foreign producers in China still sourcing the majority of their components from overseas, neither the tax take nor the upgrading of domestic industries had been anywhere near as large as the leadership expected or hoped for when they embarked on opening China. Other criticisms of China's global role were bound up with considerations of nationalism and the national interest (particularly during the negotiations over WTO entry in 2001). While some intellectuals searched for an "indigenization" of thinking to develop a distinctly Chinese conception of modernity that went "beyond the tunnel vision of a Eurocentric concept" (Zhang, 2002), the more basic idea that China was doing too much to accommodate the diktats of foreign capital gained considerable popular attention (Han, 2000). This idea that liberalizing reforms had made China vulnerable to external economic forces and shocks, and also less capable of responding to potential crisis, became a common theme in the emerging literature on the evolution of new (economic) security issues in Chinese international relations thinking (Yeung, 2008).

Such vulnerability was identified across a range of issues including the ability to get hold of the resources that China will need in the future to meet its developmental needs. While the search for industrial and food resources might emerge as the most important of these challenges in the long run, in the short term the focus was on a form of double dependence on the global economy—on foreign investment to producing goods for foreign markets. Or put the other way round, a consensus of sorts began to emerge that **(p.233)** domestic consumption was playing too small a role in generating growth. For example, figures for 2007 showed domestic consumption accounting for 38.6 percent of growth, domestic investment 37.7 percent, and net exports making up the remainder. This meant that domestic consumption was about 36 percent of overall GDP (not to be confused with its share of GDP growth)—a considerable drop from figures of around 60 percent in the 1980s and 1990s—with exports at just under 40 percent of GDP.

However, these are only headline figures, and the extent to which Chinese growth has become dependent on exports has been the subject of considerable debate. UBS Managing Director Jonathan Anderson (2007) argues that the high level of imported components in many "Chinese" exports exaggerates the contribution they make to the economy. Thus, we should strip out the value of imports which typically brings the figure down to 15–20 percent of GDP (Akyüz, 2010: 7), though Anderson (2007: 3) gets an even lower figure of 10 percent. Critics argue that Anderson's approach ignores the increasing significance of local content and "capital goods and parts and components" in Chinese exports (Cui and Syed, 2007: 7). More important, export industries are themselves key drivers of "domestic" sources of growth like investment and consumption (Cui et al., 2009). Indeed, for Akyüz (2010: 7), when you add these resulting spillovers into the domestic economy, then exports are even more important than previously thought, and account for at least half of Chinese GNP.

And while the academic picture is somewhat murky, the debate in China itself seems to be somewhat more straightforward. Exports and fixed assets investments had come to dominate Chinese growth, with domestic consumption playing too small a role. Or in the words of the *People's Daily* (2008), as the crisis began to have a real impact on growth and jobs in China:

> Although the economy has maintained double-digit growth for years, fixed-asset investment and exports have dwarfed consumption as the two pillars of expansion. With global recession clearly in view, China must sustain itself by exploiting the domestic market to offset weaker demand abroad.

Financing Growth

Identifying the need to change tack is one thing; having the ability to do it is another matter altogether. And here the distribution of economic power within the political system is particularly important. In the 1980s, the decentralization of power from central to provincial governments interacted with the emergence of new forms of economic activity, the switch from plan allocation to bank lending as a key source of finance, and the opening of new sources of finance to result in an important tip in the balance of authority **(p.234)** from the center to localities. This move, while not wholly intentional in the way it occurred, proved highly successful in spurring economic growth—particularly in those provinces that were able to locate themselves in global production networks. However, the numerous individual (and at times competing) policies of local governments often resulted in the duplication of production and overcapacity, and made it difficult for the national government to exercise macroeconomic control. In particular, during periods when the central government was trying to slow economic growth, its efforts were often undermined by local governments continuing to pursue expansionist policies.

From the mid-1990s, the central government set about trying to restore economic control and coordination through a range of fiscal and financial reforms that gradually reduced local governments’ abilities to fund their own projects. These included the abolition of the agricultural tax in 2006, and preventing local authorities from levying ad hoc fees for government services which were both thought to be at the root of some of the increased incidents of rural unrest (Kennedy, 2007). As a result, it was now local governments that found themselves on the wrong end of a power transition with insufficient funds to meet their development commitments at a time when they were being pressed to expand access to health, education, and welfare. Indeed, one of the reasons that local governments have not always been responsive to calls for slower growth is their reliance on the fruits of growth to fund their projects—their “reliance on value-added tax…and business tax means they tend to encourage investments that maximize their fiscal incomes regardless of the overall market situation” (EUCCC, 2010: 11).

As the banking system replaced the plan as a major source of funding in the mid-1980s, production (and therefore employment) in many state-owned enterprises was maintained by the provision of bank loans—many of which were never going to be repaid. Local governments also used their relationship with local branches of banks to support favored local producers. By the time the Asian financial crisis broke out in 1997, the Chinese banking system was, by Western/market conventions, “insolvent” (Harding, 1997) with nonperforming loans that would never be repaid exceeding the capital of the four main state banks—perhaps collectively as high as 50 percent of GDP at the start of the new millennium (Shih, 2008: 3). The extent of bad loans in the thousands of small-scale urban and rural cooperatives simply exacerbated the problem. Through refinancing, debt to equity swaps, the eradication of local branches of the PBOC, stronger regulation of banking activities, and tighter monetary policy, the bad debt problem was gradually eased. This was an expensive project. Chi Lo calculated in 2006 that “China has spent US$ 260 billion on cleaning up its banking system. The amount is about twice as much as Korea spent on restructuring its banks after the 1997–8 Asian **(p.235)** crisis.”[5] But with financial crisis averted, these costs were deemed to be well worth paying.

The Response to the Crisis: Back to the Future

By mobilizing all efforts to offset the impact of the global downturn, policy in 2008 and 2009 entailed a reversal of much that had gone before. As concern with reducing the rate of growth and tackling inflation was replaced by an emphasis on growth and an expansion of finance, this was most clearly and immediately seen in increasing prices in a number of sectors. For example, real estate prices (which had been rising prior to the crisis despite attempts to slow growth) rose by 24 percent across the board in 2009 with much higher increases in some cities (*China Daily*, 2010), raising fears that asset bubbles were being created which could have damaging consequences if the bubbles simply burst. The expansion of credit also exacerbated the problems of overcapacity and oversupply that policy up to the autumn of 2008 was trying to resolve (EUCCC, 2010).

The growth of debt which might turn into nonperforming loans also came back on the agenda after years focusing on reductions and restraint. The total debt that local governments accrued in responding to the crisis is difficult to pin down. The official NAO investigation in 2011 put the combined debt of all levels of local governments including their affiliated LIPCs at RMB10.71 trillion (30 percent at the provincial level, 26.5 percent at county level, and 43.5 percent at city level). Of this, just under half or RMB4.971 trillion is in the LIPCs (NAO, 2011).[6] Moody's argued that the audit underestimated the extent of local government debt by RMB3.5 trillion because it only included those debts formally guaranteed by local governments and not those that would eventually fall on local governments to repay irrespective of their official designation. An overall figure of RMB14 trillion was widely reported (or guessed at) in the financial press (Zhang, 2011),[7] with Victor Shih (2011) combining a number of top-end estimates to get to the highest end estimate of RMB20.1 trillion.

This highest figure would put combined local government debt in 2010 at over 50 percent of GDP. The lower NAO figure is about 27 percent, which, when added to the debt of central government organizations (banks, ministries, etc.), would generate an overall debt to GDP figure for 2010 of around 60 percent. Crucially, this debt is not equally spread across the country. Ten cities and provinces reported that their local investment companies' debts were over 100 percent of local GDP in 2010, with the highest reporting a figure of 400 percent (Wang, 2010). And one of the conclusions of both the NAO and PBOC reports is that the debt to revenue ratios are much higher, and local governments are less likely to generate the money needed to pay off their debts in central and western China than is the case in eastern provinces.[8]

(p.236) As China went into the crisis in a strong fiscal position supported by massive foreign currency reserves, it has been in a stronger position than most. As Chi Lo (2011) argues:

> one should not forget that the government has enormous financial resources, owns the country’s land and controlling stakes in many listed companies. These assets can be privatised, if necessary, to raise funds to fend off any fiscal or debt crisis. In the worst case, even when China had to monetise its debt, its huge current account surplus (a reflection of China being a net creditor to the rest of the world) would ensure that no external-driven crisis would crush the domestic system.

So the focus on debt here is not to suggest that China is moving headlong to a financial crash, but rather to show that the response to the crisis was far from cost-free, and will continue to have repercussions for a number of years. And in responding in this way, government agencies at various levels now face some of the same financial problems that they might have thought that they had dealt with and solved.

However, there is one area where China does face potential problems that add a rather unique dimension to the attempt to deal with the longer term consequences of the crisis. Hsing (2010: 5) argues that as land become commodified but not privatized after 1988, it has “reconfigured the power dynamics” of Chinese politics. What she calls “the urbanization of the local state” (Hsing, 2010: 6) resulted in land and housing bubbles appearing in parts of China long before the onset of the crisis, defying attempts to control growth. Not surprisingly these trends were exacerbated by the postcrisis growth in liquidity with investment in real estate equaling roughly 11.5 percent of GDP in 2009 (Ma, 2010).

Provincial level governments get just under half of their income through transfers from the central government—44 percent in 2010. Of the remainder that they raise themselves, fees from selling state land usage rights (国有土地使用权出让收 guoyou tudi shiyongquan churang shou) has become the major source of income. Such revenues increased by over 40 percent in 2009 (Naughton, 2010: 32), and then more than doubled in 2010 to account for 72 percent of locally collected revenues, doubling the total revenue controlled by local governments in a single year (Ministry of Finance, 2011). Moreover, the loans of local investment platforms are typically underwritten by expectations of rising prices in the future, creating an even stronger link between local government finances, debt and land prices, ownership, and usage. So while rising house and land prices contribute to inflation which Wen Jiabao argues “affects social stability” (Xinhua, 2011), reducing land prices too quickly would impact on local governments’ ability to raise revenue and possibly increase the number of bank loans that become nonperforming (as well as leading to the other “normal” consequences of burst bubbles).

(p.237) The response to the crisis, then, has once more turned the focus back onto many of the problems that economic policy before 2008 was designed to resolve. Local governments were once more able to fund preferred projects with little attention paid to the overall pattern of national economic growth. The problem of a relatively large number of bad loans in the banking system reemerged, exacerbated by the umbilical cord that connects land prices to local government finances. And the (in)ability of the central state to control and moderate growth when necessary was also brought into focus again as inflation continued to grow "despite a series of measures taken to cap price rises" (Xinhua, 2011). Indeed, perhaps more than anything, the response to the crisis, when considered in a little bit of historical contextualization, suggests that it is much easier to facilitate rapid economic growth in China than it is to control it and rein it in. The attempt to begin to move from a growth to development paradigm had already been partly undermined by the policy responses to the drop in exports in early 2008. But the response to the crisis saw the pendulum clearly swing back to growth promotion.

Within this growth promotion, there were elements intended to help the shift in emphasis toward domestic growth—for example, support for rural consumption, support for clean energy technology projects, and infrastructure projects that should facilitate increased economic actability in central, southwest, and northern China. The value added by exports were also less significant in promoting growth in 2009 than before the crisis leading some to assert that China has "decoupled" from the global economy because of the value (Rabinovitch, 2010)—though given the amount of money that China poured into the economy in 2009, it would have been astonishing if this were not the case. And as we have seen, they have also resulted in a return of excess investment and overcapacity and possible debt problems. So perhaps ironically, while the crisis might have further undermined confidence in the existing growth "model," the immediate solutions meant a turn back to that model rather than a transition to a new paradigm. Or at the very least, the response entailed putting the transition on hold and revisiting (and in some cases exacerbating) financial problems that the leadership had been trying to deal with for some time.

Given the advantageous fiscal position China was in 2008, the degree of autonomy provided by a relatively closed financial sector, and the residual strong hand of the state in the economy, these are far from insurmountable problems. Perhaps of more fundamental importance in the long term is that the response to the crisis shows that making the transition toward a new "scientific" paradigm built on slower but more sustainable growth is no mere speech act—simply saying it does not make it real. It is difficult to see how such a switch will not lead to dislocations; some people will inevitably lose out even if the long-term consequence is an improvement for the country **(p.238)** as a whole. The way in which the leadership responded to the crisis suggests that there may not be the political will to push forward in the short term with what in is seen to be desirable for the long term.

Responding to China’s Response—Global Power Shift?

But if the crisis has generated problems for the Chinese leadership, they are problems that other world leaders might well prefer to their own challenges. And to say that China’s response was not cost-free does not mean that it was unsuccessful—far from it. Indeed, as it began to appear that China’s response to the crisis seemed to be working, there was an upsurge in interest within China to the idea of a “China model” that might act as an alternative to Western modes of development. Qian Gang (2010) has traced the phenomenal rise in what he calls “the discourse of greatness” in 2008 and 2009, reflecting a growing national pride in China’s apparent increase in global economic power vis-à-vis the existing (crisis hit) powers. Of course, this seems to contradict the apparent move toward a consensus that the Chinese model has run its course. But it can be reconciled by thinking about what the Chinese model means in most of these discourses.

Identifying what the China model actually entails is a difficult exercise that generates conflicting conclusions. While most analyses point to the importance of a strong state guiding the economy, it is possible to make the counterargument and point to the process of economic liberalization and the emergence of private sector activity in the 1980s as the root cause of China’s success (Huang, 2011). But what the China model actually might be is less important than what it is perceived to be—and it has largely come to be seen as an example of what you can do if you do it on your own terms rather than following the “Western way.” So the China model has become a standard bearer for what it is not; it is not big bank shock therapy liberalization, it is not economic liberalization accompanied by political democratization, and it is not doing what the international liberal global order wants—for example, liberalizing financial sectors and allowing free-floating market exchange rates (Breslin, 2011).

Of course, this does not mean that all developing countries are in a position to simply copy what China has done. But China’s experiences in not just this crisis but also the Asian crisis of 1997 have served to give succor to those who prefer various forms of stronger state controlled versions of capitalism over more (neo)liberal forms (Wade, 2010; Stubbs, 2011). Conversely, according to the man who developed the “somewhat unhappy term of the ‘Washington Consensus’,” one of the main consequences of the “crisis has been to discredit Western views of development” (Williamson, 2010: 1). The crisis also helped **(p.239)** accelerate shifting patterns of economic interactions and the changing balance of economic power. Trading with China instead of the developed West has also been a key reason why resource-rich developing countries like Brazil have been able to recover from the impact of the crisis with apparent speed and ease

(Whalley and Medianu, 2010), while developed economies like Spain, Greece, and Portugal have all benefited from increased investment and trade relations with China (Anderlini and Spiegel, 2010).

China also emerged from the crisis as a key player in any attempt to create new mechanisms of global governance—be that in partnership with the existing global powers through the G20 and reform of the IMF, or in new "blocs" like the BRICS. While Chinese officials remain committed to proving that China is a responsible great power, this does not mean that they are satisfied with the (liberal) norms that underpin the existing order, and the distribution of power within it. But this should not mean that the rest of the world should be concerned by this power shift. China's developmental needs require access to markets and resources that would be made more difficult to attain if China was to destabilize international relations and/or antagonize key players; it is a responsible, dissatisfied, great power (Breslin, 2010). Ultimately, what is depicted (or more correctly, constructed) as China's historical and cultural predilection for peace and harmonies is promoted as being more appropriate for the promotion of global harmony than the existing "Western" system (Su, 2009). For other developing countries, China's rise is depicted as being only a good thing, as China will not behave like previous great powers that treated their colonies as unequals to be exploited. China's rise also benefits developed states, as China has emerged not only as a potential major source of much needed investment, but also, through the development of its own domestic demand, as a *potential* alternative to declining Western consumption. China has become a "stabilizer" of the global economy (*People's Daily*, 2010).

But not everybody is convinced of the ultimate pacific conclusion of this ongoing power shift—not least because China's leaders seem to have found themselves in a position to be more forceful in articulating Chinese positions. As Wang Jisi (2011: 68) puts it:

> In recent years, China's power and influence relative to those of other great states have outgrown the expectations of even its own leaders. Based on the country's enhanced position, China's international behavior has become increasingly assertive.

This assertiveness extended to economic affairs, with calls from the Governor of the PBOC for a new "super-sovereign reserve currency" to replace the dollar (Zhou, 2009). In 2010, an online article suggesting that China should use its foreign currency reserves to cause economic problems in the United States (Xu, 2010) was widely reported and circulated outside China as a reason for **(p.240)** fearing China's financial clout.[9] Such a move is unlikely—causing problems for the dollar when you hold US$2.8 trillion dollars worth of reserves, are a major trading nation, and are trying to keep the value of the Renminbi relatively low through a "managed" exchange rate could "cause more harm to China" than the

United States (Gagnon, 2010: 1). But the debate illuminates both the new confidence and assertiveness of *some* voices in China, and also the concern that some external observers have about the consequences of the apparent ongoing power shift.

China 's Economic Power—Communicating Deterrence, Managing Expectations

Whether China's leaders are able to operationalize its economic power to force others to fall in line with China's interests remains open to question. A number of states did follow China's call to boycott the awarding of the Nobel peace prize to Liu Xiaobo—but the prize was still awarded, the United States still sold missiles to Taiwan, and President Obama still met with the Dalai Lama. Nevertheless, China at the very least seems to have a deterrent power (Drezner, 2009) to prevent others from trying to unduly influence its "core interests" (核心利益 hexin liyi) defined as the "state system and national security," "sovereignty and territorial integrity," and "the continued stable development of China's economy and society" (Swaine, 2010: 4).

China's leaders seem to have no great appetite to use their economic power for anything other than serving what they perceive to be China's interests. Despite its aggregate size, the official message seems to be that China is still a relatively poor country (in terms of per capita income) with over 150 million people still living in absolute poverty and hundreds of millions more lacking the basic standards of living that are enjoyed in the developed world (Dai, 2010). Thus, it is far too soon to expect China to take a leading role on environmental issues, for example—it is the existing global powers that should continue to take the lion's share of global responsibilities for many years yet. Moreover, the task of reducing poverty and inequality is so great that other countries should not try and pressure China for change (e.g., on exchange rate policy). Not only is this good for China but ultimately good for the rest of the world, meaning that "developing its economy and improving its people's welfare" is China's "first and foremost international responsibility" (Chen, 2009: 12).

Conclusion

In some respects, China seems to be the latest in a line of Asian challenges to the dominance of a "Western" world order. China's material and ideational **(p. 241)** influence over large parts of the world has clearly increased; over its neighbors in East Asia in particular and increasingly over resource-rich developing states. The political economy of developed states is also increasingly influenced by what happens in China: not just through the flow of exports from China that has been a feature of global trade for some time now, but through the price and allocation of key resources; through increasing investment flows from China to the West in the search for technology, knowhow, and brands; and as an important market for some producers (though still frustrating the ambitions of many). But it is salient to remember that neither the Japanese challenge nor that from the Asian Tigers ultimately overturned the global order. And despite some of the hyperbole that has accompanied China’s rise, it seems somewhat premature to be writing off the West or seeing China as having the same levels of global power as the United States just yet (Nye, 2010).

The crisis did not mark the start of the rise of Chinese power, but it certainly accelerated it in some areas, and helped undermine the legitimacy of the neoliberal model that China stands as an alternative to (in some minds at least). The crisis also played a similar “catalyst” role in the domestic sphere. In the short term, it has meant a probable return of some of the financial problems that considerable time (and money) had previously been devoted to clearing up. As a result, while China does not face a financial crisis akin to the one that hit transatlantic economies in 2008–9, a number of financial challenges will have to be handled with care and skill as the longer term consequences of the response to the crisis gradually become clear.

More fundamentally, the crisis has highlighted the need to change the drivers of economic growth, and move from a preoccupation with rapid growth to a slower, more sustainable developmental paradigm. But at the same time, the way in which the leadership responded to the crisis suggests that they are not ready, prepared, or perhaps even politically able to face the possible consequences of making the transition just yet. How the leadership manages the next stage of China’s economic transition while simultaneously managing the relationship between the party-state and the people will go a long way to establishing whether the Chinese mode of governance really is something that others will look to as something to emulate in the long run.

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Notes:

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(1.) In currency exchange rate dollars. It is widely assumed that China had long occupied second place in PPP calculations.

(2.) Of course, identifying what the “West” actually is remains a tricky task—it often seems to be shorthand for simply the United States and at other times the neoliberal preferences of the international financial institutions. The use of the term in this chapter is not meant to refer to any fixed idea of what the West is or might be, but instead simply reflects its usage in popular and academic discourses including all the inconsistencies and vagueness that this entails.

(3.) By around 20 percent in the three years from the end of the currency peg in July 2005.

(4.) For more details on how the money was spent (and when), see Nicolas (2009), Zhang et al. (2009), Zheng and Chen (2009), and Snyder (2010).

(5.) Private unpublished paper cited with author's permission.

(6.) As around a quarter of this debt came due for repayment in 2011, about 30 percent in and after 2016 (and the rest at various points in between), these debts had not turned into extensive nonperforming loans at the time of writing.

(7.) Though much of this reporting seems to have been the repetition of previous reports which appear to have been based on a misreading of the PBOC (2011) report.

(8.) The NAO divides China into Central, West, and East, whereas the PBOC also has a separate Northeast grouping.

(9.) This piece was posted on the Qiushi discussion page and was erroneously credited with being published in the *Qiushi Journal*, which is the official theoretical journal of the CCP, and was thus mistakenly taken to represent official policy.