Oxford Review of Economic Policy, Volume 28, Number 3, 2012, pp. 569–586

Seeking a balanced approach on the global economic rebalancing: China's answers to international policy cooperation

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Abstract Despite playing a crucial role in the world economy and in any framework for policy cooperation, there is little awareness among policy-makers in developed countries of China's views and policy directions. Aimed to address this gap, this article attempts to integrate the different views of mainstream Chinese experts and scholars who have influence in shaping the country's foreign economic policy. The author suggests that differentiating between the two concepts of current account imbalance and international currency power imbalance can offer a persuasive explanation of China's positions on international policy coordination, and help advance the global debate on the issue of global economic rebalancing. Chinese analysts generally resist the one-off rapid appreciation of the RMB exchange rate, but they support international collaboration for rebalancing the global economy and emphasize the implementation of China's own obligations by carrying forward domestic structural reforms of the Chinese economy.

Keywords: global financial crisis, global economic imbalance, global rebalancing, current account imbalance, international currency power imbalance, US dollar dominance, Chinese perception

JEL classification: F32, F33, F42, F55

I. Introduction

This paper aims to detail Chinese economists' interpretation of the causes of global financial crisis, global economic imbalance, and their proposals for global rebalancing. Since the global financial crisis the Chinese government has been actively involved in the G-20 mechanism for international cooperation, but in a quite diversified policy context. Domestic policy debate inside China has influenced the formulation of government policy and its commitment to the international agenda. Bearing this in mind, the author presents the different interpretations of mainstream Chinese scholars and

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I gratefully acknowledge helpful comments from the editors of this special issue, Christopher Adam, Paola Subacchi, and David Vines, two anonymous reviewers, Greg Chin, and Mark Beeson. I take responsibility for errors and omissions.

doi:10.1093/oxrep/grs032

experts about the sources of the global economic imbalances and how to achieve global rebalancing through international cooperation. The aim of the paper is to contribute to improving the limited awareness of China's policy process in the Western policy community. The writer does not necessarily agree with every point of view, but presents those views as they are presented in the Chinese media, considering the relative popularity of these Chinese experts and their significance in policy-making circles.

The main finding of this article is that the Chinese academic and policy research community has identified the existence of two forms of global imbalances: worldwide current account imbalances, and power imbalances in the international monetary and financial governance regime. The latter are perceived to result from US dollar hegemony, Western control of the International monetary Fund (IMF) and other international economic mechanisms, and the institutional biases of the macroeconomic policies of the developed countries. The central argument is that they describe a causal 'link' between the two imbalances, and emphasize that imbalances of global governance also bear a significant responsibility for the global financial crisis, as well as global current account imbalances. Highlighting this correlation is not to deny the existence of a current account imbalance, its negative impact, or the obligations that China should take in addressing global rebalancing under the G-20 framework. Rather, it stresses the need to look at the problem of global imbalances from a comprehensive perspective—as resulting from a broader set of factors. Understanding these two very different concepts of current account imbalance and international currency power differentials is particularly important for understanding Chinese interpretations of the causes of the global financial crisis. It is also potentially helpful for finding a possible path towards global economic rebalancing. The policy implications are that China and the international community must commit to addressing the multiple problems of global imbalances, through working on the two kinds of problems at the same time. Only then, can the long-term stability of the global economy be restored.

This emphasis on the link between the two imbalances and their associated impacts, and the comprehensive approach to global rebalancing is different from the mainstream Western views. This paper argues that it is necessary for the Western academy to understand the views of Chinese scholars and policy experts, and that only with such understanding, and by taking them seriously, will the West and increasingly important emerging economies such as China be able to conduct a meaningful dialogue on cooperation to address global rebalancing and the US and European debt crisis, as well as ways to restore stability in the global economic system.

II. The global financial crisis and two 'associated' imbalances

The Chinese academic and policy communities take a broad perspective on the root causes of the global financial crisis of 2008–9 and highlight the two distinct 'global imbalances'. Chinese views of current account imbalances are broadly similar to academic views in the US and other developed countries. This global imbalance is argued to exist between the United States on the one side, and the East Asia economies and petroleum-exporting countries on the other side (Zhang, 2007; Chen and Zhou, 2011). The second concept is the 'unevenly structured' international economic system, characterized by the dominant influence of the United States and the West more broadly, and the under-representation of developing countries in the IMF, the World Bank, and the World Trade Organization—the major pillars of current global economic governance (Zheng, 2010; Liu, 2010).

Many Chinese analysts share the opinion that Western scholarly analysis has put the emphasis mainly on current account imbalances, but ignores the existence of uneven power distribution in the international monetary system, and its causal effects related to the global financial crisis. Chinese scholars argue that these two global imbalances are interrelated, and reinforce each other. The limited representation of developing and emerging economies is said to be a main reason why the IMF has provided a 'non-neutral' risk assessment about the causes of current account surpluses of developing nations (Liu, 2009). Chinese scholars argue that the IMF neglected the risks of US subprime loans and its misaligned macroeconomic policies, and mistakenly targeted the foreign-exchange policies of emerging economies. As a result, the Fund squandered its chance to prevent the financial crisis. Chinese critics argued that, after the onset of the crisis, the US government and the IMF (influenced by the US) once again tried to impose the burden of adjustment of current account imbalances on developing countries, and emerging economies in particular. One example was the pressure that the IMF put on China to appreciate the RMB exchange rate, as a priority in responding to the crisis.

Wang Guogang (2010), the director of the Institute of Finance and Trade at the Chinese Academy of Social Sciences (CASS), has contended that with the gradual recovery of world economy in the post-crisis period, rebalancing of the global economy has become a good excuse for some Western countries to move toward trade protectionism, and to constrain the foreign economic development of developing countries. He argues that the theory of global trade balances is wrong both as theory and as policy practice, and has not been proved correct over the past 200 years, starting with the Industrial Revolution. He adds that in an international monetary system based on the US dollar as the major reserve currency, it is impossible for the US to maintain balanced foreign trade, and that trade deficits are the unavoidable result. Zhang Bin and Wu Ping (2011) of the Policy Research Office of the Ministry of Commerce, are sceptical about US efforts to streamline the US current account deficit because they argue that the dollar-based international monetary system is actually the root cause of global economic imbalances. Because of its privileged position, the US cannot be expected truly to fulfil the responsibility for correcting global economic imbalances. China should, therefore, participate actively in the G-20 dialogue, and work with other members with common concerns to promote the reform of international governance mechanisms.

Chinese economists perceive global economic rebalancing as a complicated process of re-distributing the benefits of economic growth and sharing the costs of adjustment. They do not deny the existence of global economic imbalances, but they are concerned that global rebalancing has the potential to be abused for purposes of trade protectionism. As Chen Jiyong and Zhou Qi (2011) point out, rebalancing the global economy needs stable promotion, and it should not be 'a gorgeous coat' of trade protectionism harboured by the United States and the West. They suggest that rebalancing the global economy requires the parties to commit to gradual adjustment of the mode of economic growth, and more equal distribution of the dividends of economic globalization between the North and South. More of the adjustment costs should not be borne by the developing economies.

III. China's debate on the global current account imbalance

In exploring the role of current account imbalances and their implications for the global financial crisis, Chinese analysts have developed complex explanations of the crisis that range from moderate to radical perspectives. By emphasizing the 'complexity' of the causes of the crisis, incumbent officials, such as the Governor of the People's Bank of China (PBoC) Zhou Xiaochuan (2009), contend that 'factors both at the macro and micro levels played some role'. Zhou insists that 'the crisis originated from Wall Street', 'and many indisputable facts have established that micro factors played an overwhelmingly important role in causing this crisis', including procyclical factors at the micro level, problems with credit-rating agencies, and financial institutions' lax lending standards, excessive leverage, and frivolous development of derivative products.

With regard to 'macro' level factors behind the crisis, Zhou recognizes the role of global current account imbalances, but suggests that we should not exaggerate it because there are uncertainties about its impact. He urges us to consider the following points: (i) there is no consensus about the extent macro factors contributed to the crisis, including the role of global imbalances; (ii) balance is a relative concept in the view of traditional Chinese philosophy, and imbalance is a state of normalcy; (iii) the current global imbalances have 'a counter-intuitive feature': 'That is, in relative terms, low-income countries have high savings rates whereas rich people in the high-income countries have consumed beyond their means' (Zhou, 2009).

Other prominent Chinese policy advisers share Zhou's view and criticize what they see as the 'biased' view on global current account imbalances. For example, Zeng Peiyan, former vice premier and the current president of China Center for International Economic Exchanges (CCIEE), refuted in public statements that the 2008 financial crisis was caused by the high saving rate and high level of exports of East Asian countries. He considered these arguments 'diversionary and irresponsible'. Similarly to Governor Zhou, Zeng insisted that 'the imbalance of the world economic development is absolute and balance is relative' (Zeng, 2009).

Regarding the relative weight of China and US in the current account imbalances, Zhou acknowledges that China and US are part of the imbalance story, but not the whole story. He stresses that it 'is plausible to over-estimate the impact of the two countries because there is no available data on the flow of global savings'.

Zhou argues that, although China's current account surplus is large, it is just a part of the global total. Oil exporters, Japan, and other Asian economies all have a significant share of the global surplus. Among the countries with deficits or low levels of saving, the share of the US deficit is very large (Zhou, 2009).

Some Chinese scholars note that current account imbalance is an importance issue, but they highlight the role of financial globalization in driving trade imbalances. For example, Zhang Liqing (2007) argues that financial globalization has delayed the balance-of-payment adjustments of the United States and other countries because they can easily get financed internationally. While, in the late 1980s, the US current account deficit as a percentage of GDP was only 3 per cent and the US government chose to devalue the dollar, by 2006 the proportion of the US current account deficit to GDP was over 7 per cent but it was still not pressured to adjust. In his analysis, by pegging their currencies to the US dollar China and other East Asian countries, such as South Korea, aimed to take advantage of the situation of imbalances to create a favourable environment for expanding their exports and to urbanize a large population from the agricultural sector. Although the Chinese economy has benefited from this situation, Zhang realizes that the global imbalance is not sustainable, and China has to make efforts to rebalance its own economy.

Some Chinese scholars have critiqued the 'global saving glut' hypothesis developed by US Federal Reserve chief and former Princeton economist Ben Bernanke (2005). Chinese analysts see this explanation as a pretext for US policy-makers to escape their responsibility for the global economic imbalance. According to CASS researchers Li Yang and Lu Jin (2010), the Bernanke hypothesis suggests that emerging countries lend too much money to the US, which leads to low US interest rates and excess liquidity, and eventually to US over-consumption and to global economic imbalances. America is not responsible for high consumption and low savings, but emerging countries should reduce their savings and increase their spending. Li and Lu disagree with Bernanke and argue that since the financial crisis the US domestic savings rate and current account balances have improved rapidly, implying that the US is able to effectively reduce its current account deficit. On the other hand, they suggest that surplus country adjustments do not necessarily correct trade imbalances. For example, in the late 1980s, under US pressure, Japan as the surplus country greatly expanded its domestic spending in domestic infrastructure projects, but these measures did not help much to correct the Japan–US trade imbalance.

Some Chinese analysts, such as Chen Jiyong and Zhou Qi (2011), see the problem in the pattern of economic growth that promotes and fosters imbalances. The global economy seems to be caught in an unbalanced structure, with the US at one pole of the imbalances and the Asian economies and oil-exporting countries at the other. In their eyes, this 'interdependent and symbiotic growth' pattern forms a complicated but fragile network of primary products, semi-finished products, finished products, and cross-border consumers. More serious imbalances lie in the internal economic structure of each national economy caused by problems such as long-term reliance on exports in developing economies, 'de-industrialization' in developed economies, and homogenization of industrial structure and weak consumption in export-oriented emerging economies. As Chen and Zhou insist, the external and internal imbalances have become the greatest barriers to global economic rebalancing.

About the ways of achieving the global rebalancing, Chen and Zhou (2011) suggest that resolving internal imbalances should be enforced before external imbalances are addressed; that is, it is necessary to adjust the internal economic growth model of key economies in order to correct external imbalances.

IV. China's debate on the monetary sources of global imbalance

A large number of Chinese analysts attribute the global financial crisis and the global economic imbalances to the hegemonic position of US dollar and the uneven power distribution in the IMF, which tends to favour the US and the major Western countries. They argue that in order to rebalance the global economy, the international community must reform the contemporary international monetary system and rectify its distortionary effects on the global economy. Without such reform, it would be impossible to have a fair implementation of readjustment plans.

(i) Abuse of US dollar dominance as the fundamental cause

Chinese analysts (Cheng and Yang, 2010; Wang, 2007) attribute the fundamental cause of global economic imbalance to the hegemonic position of US dollar as the major reserve currency. They argue that the end of the Bretton Woods System in the early 1970s did not reduce US monetary power. 'Dollar dominance' largely causes the current account imbalance between the US, East Asia, and the petroleum-exporting countries. Such a reserve currency position has allowed the US to earn disproportionate benefits, including a low saving rate and overspending. In order to ensure these gains, the US government supported Wall Street's stance on international financial liberalization in order to open markets to US banking and financial institutions and maintain inflows of foreign capital into the US markets.

Zheng Xinli, former deputy director of the Communist Party of China (CPC) Central Policy Research Office and currently vice president of CCIEE, has argued that in exploring the root causes of the global financial crisis, Western economists generally ignored the fundamental role of the US dollar as the reserve currency in the crisis.

Zheng claims that the US abuse of its status as major reserve currency issuer caused the so-called 'twin deficits' of the current account and the government budget, and tremendous risks were building up in the US economy. On the other hand, the US credit-rating agencies overstated the economic risks that accrued to the creditor nations, to help cover up the risks of the US as the debtor nation. This produced a situation that he defines as a 'reversed risk relationship' (Zheng, 2010; 2011*a*).

Zheng insists that the US abuse of its key reserve currency issuer status also led to the transformation of the US economy from a manufacturing-based 'real' economy into a financial speculation-based 'virtual' economy. He describes the pre-crisis US economy as 'an upside-down pyramid built on sand' (Zheng, 2010). Based on the data of the Bank for International Settlement (BIS), he suggested that subprime loans of about 2 trillion dollars were the foundation of this financial pyramid, and above this base were the regular housing loans of 12 trillion dollars, and the higher levels of this structure were the corporate debt of about 62 trillion dollars, including collateralized debt obligations (CDOs) and credit default swap (CDS). Sitting at the top of the pyramid were various financial derivatives held by US financial institutions, totalling about 300 trillion dollars. If any section of this financial pyramid were to break, it would destroy the entire edifice. Zheng draws a very important lesson for the world economy, that is, the development of financial products based on a nation's credit must be matched by the proper size of its 'real' (or manufacturing) economy (Zheng, 2010).

Echoing Governor Zhou Xiaochuan's proposal for a supra-sovereign currency and a larger role for the special drawing rights (SDRs) (Zhou, 2009), Zheng suggests building 'three safety doors' to ensure the security of the international financial system: building a new international monetary system in which multiple currencies compete with each other; establishing surveillance and an early warning system over international reserve currencies; and enhancing assistance institutions (Zheng, 2010; 2011*a*,*b*).

Other analysts go further to accuse the US of being the largest 'currency manipulator' despite its accusations towards China. Some analysts describe the ways that the US manipulates its currency. These include releasing misleading investment bank reports and expert analysis that misinforms the market and causes appreciation or depreciation of the dollar; the use of hedge funds to attack other major currencies, such as the euro and the British pound; and the US government's threats of sanctions, such as denial of access to US market and severing bilateral security alliances (Xie, 2006; Liu, 2010).

(ii) Biased IMF surveillance

Chinese academics generally hold the view that the IMF is plagued by the deeply uneven structure of its power, incapable of preventing major financial crises because it is clearly biased by neoliberal policies, and, as a result, the lack of even-handedness in risk surveillance.

Economic neoliberalism and the Washington Consensus are widely regarded as being at the root of the global crisis. Driven by banking and financial sectors, the US government has worked with the IMF to impose the agenda of deregulation and liberalization on developed and developing countries since 1980s. The implementation of neoliberal policies has resulted in financial crises in developing nations more frequently than ever before, because these policies severely weakened the capacity of developing countries to resist financial crises (Cheng, 2005; Cheng and Yang, 2010). On the other hand, IMF staff ignored accumulated financial risks in major developed countries, deliberately or not, driven by their beliefs of economic neoliberalism. These criticisms from Chinese scholars appear to concur with the findings of the 2011 IMF Independent Evaluation Office (IEO) report that tries to examine the reasons why the IMF failed to react with earlier warnings about the impending crisis (IMF IEO, 2011).

China's representative to the IMF, He Jianxiong, confirmed the above assessment on the basis of his experience of working at the IMF (Liu, 2009). He stated that the financial crisis highlighted the weakness of the IMF in terms of its governance structure. Because voting shares determine how much influence a country has on major IMF resolutions, the IMF tends to give less consideration to the positions of developing countries and emerging economies. Though the emerging economies and the developing nations as a whole have greatly increased their economic weight in the global economy and have experienced much faster growth than developed countries, their total voting share only increased 5 per cent in the last three decades (Liu, 2009).

According to He Jianxiong, the uneven voting power structure has led to the prevailing influence of the developed countries in IMF decision-making. For instance, in June 2007, when the possible collapse of the US financial system became evident, the board of directors of the IMF still spent much of their energy discussing and passing a resolution to monitor the foreign-exchange policies and related risks of the emerging economies, and actually ignored the risks that were created by the major reserve currency issuing countries. As He notes, after reviewing the Article IV consultation report on the US, in August 2007, the IMF board of directors insisted on reaching the conclusion that the prospects for the US economy were good, and that the US financial system was extremely strong in terms of its ability to resist risk exposure. Because of such blindness, the IMF missed a chance to provide an objective assessment of the US economy, and to send an early warning about the impending financial risks. He argues that this example exposes the 'unreasonable' governance structure of IMF, which has made impossible any healthy dialogue between the IMF and developing countries (Liu, 2009).

The above critique of the IMF's governance problem is supported by insider observations of IMF officials from developing countries, and by the report released by IMF IEO (IMF IEO, 2011). In this report, IMF IEO lists the factors responsible for the IMF failing to identify risks and give clear warnings, including analytical weaknesses, organizational impediments, internal governance problems, and political constraints. He argues that 'many of these factors represent long-standing problems that had been highlighted for over a decade' (IMF IEO, 2011, p. 24). The report recognizes the influence of 'groupthink' among 'a cohesive group of macroeconomists' in the IMF, who firmly believe that 'market discipline and self-regulation would be sufficient to stave off serious problems in financial institutions'. IMF staff believed that 'crises were unlikely to happen in advanced economies, where "sophisticated" financial markets could thrive safely with minimal regulation of a large and growing portion of the financial system.' (IMF IEO, 2011, p. 24). The IMF report points out this tendency as 'a case of intellectual capture', which actually refers to the asymmetrical influence of developed economies and reflects the low level of independence of the IMF.

With respect to the influence of big countries in the IMF, the IMF IEO report finds that 'many area department economists felt that there were strong disincentives to "speak truth to power", particularly in large countries', and they 'were unduly captured by countries'.

> IMF staff felt uncomfortable to challenge the views of government authorities of the advanced economies on monetary and regulatory issues, given the authorities' greater access to banking data and knowledge of their financial markets, and the large numbers of highly qualified economists working in their central banks. (IMF IEP, 2011, p. 17)

As a result, IMF staff chose to ignore the risks coming from the over-leveraging of capital markets of developed members, and kept their 'focus on the IMF's primary concern—global imbalances and a disorderly dollar decline—as the key risk to global stability, largely ignoring evidence pointing to other risks' (IMF IEO, 2011, p. 17).

V. Is a Chinese version of the Plaza Accord necessary? Debate on the Plaza Accord and its influence

In the discussion about global economic rebalance, China's foreign-exchange policy has become an important issue, a question where trade protectionists and those pro-rebalancing find common ground. In China, though different views do exist on how to deal with this pressure, the majority of Chinese economists are opposed to the one-off appreciation of the RMB. They advise that the Chinese government should beware of the dangers of developed economies imposing a Chinese version of the Plaza Accord, or Plaza Accord II. They argue that the Plaza Accord was the root cause of the decade-long recession of the Japanese economy, and China must not repeat Japan's painful course. Only a small group of scholars urge for exchange-rate adjustment to protect China's own welfare.

(i) The Plaza Accord as the cause of the Japanese recession of the 1990s

Many Chinese analysts ascribe the 1990s recession of the Japanese economy to the Plaza Accord in 1985 and the strong appreciation of the yen.

Chinese analysts believe that the outcomes of the Plaza Accord included the sharp decline in exports, high inflation, the real estate bubble and excessive capital speculation, the erosion of innovation spirit, and the decade-long recession of the Japanese economy in the 1990s. Yu Zuyao (2010), a senior researcher at CASS, argues that the enforced sharp appreciation of the Japanese yen against the US dollar caused serious damage to the export-oriented Japanese economy. The Japanese economy was thrown into the most serious recession since the end of the Second World War (Yu, 2010). Zhang Yansheng, the director of the Foreign Economy Institute, a think tank affiliated to the National Development and Reform Commission (NDRC), believes that the Plaza Accord gave the US economy a chance to adjust and, starting in March 1991, the US economy entered a decade-long 'New Economy' cycle of low inflation and high growth (Zhao, 2008). In the analysis of Zhang and many others, there is a causal link between the US macroeconomic adjustment and the decade-long recession of the Japanese economy. As for the impact of the Plaza Accord on the US economy, Chinese analysts generally believe that large depreciation of the dollar helped to ease the US's economic difficulties, and laid the foundation for its high-speed growth in the 1990s (Yu and Wei, 2003; Zhao, 2008).

Some analysts insist that the Plaza Accord ushered in financial and monetary disasters, and that after the Japanese yen was revalued, the Japanese economy fell into a 'liquidity trap', and monetary policy was ineffective (Yu and Wei, 2003). Rapid appreciation of the Japanese yen created bubbles in capital market and real estate. As Wei Jianing a senior fellow at the State Council Development Research Center (DRC) explains, the forced rapid appreciation of Japanese yen resulted in the sharp reduction of Japanese exports, which caused the long recession in the 1990s. In order to deal with the recession, the Bank of Japan introduced a policy of loose money supply, which created the bubbles in stock and real estate markets. When the bubble burst, the Japanese economy fell into a deep recession for over a decade. Wei suggests that the Chinese government and the public should be extremely careful about the dangers of repeating the Japanese experience (Yu and Wei, 2003).

Chinese analysts call for learning lessons from the Japan case. Yu Zuyao (2010) suggests that Japan lost 'currency sovereignty' under international pressure, and the example of Japan and many other countries experiencing economic impact imply that China must put the defence of currency sovereignty as a top priority. Other Chinese academics warn of the perils of embracing neoliberal ideology. Liu Fengyi, a scholar of Nankai University, argues that after the Plaza Accord, Japan turned to economic neoliberalism, which is another reason for its economic decay of two decades (Liu, 2010).

(ii) For appreciation: different lesson and different approach

Contrary to the predominant view, a small group of analysts offer a different account of the root causes of the Japanese economic recession of the 1990s, and urge for the RMB exchange rate to appreciate. Yu Yongding, the former director of the Institute of World Economy and Politics at CASS, is among the most prominent voices.

Yu Yongding (2007) suggests that appreciation is a reflection of a country's economic performance (prosperity), and appreciation does not necessarily lead to an economic bubble and then to recession. Many people have misread the experience of Japan. Yu contends that Japan's poorly designed monetary policy was the cause of the post-Plaza Accord bubble, which was not triggered by the appreciation of the yen, but by loose or expansive money supply, a policy that was aimed to deal with the misperceived slowdown of economic growth. He argues that in 1985 the Japanese economy had already entered recession, but the decision-makers did not know it at the time. Driven by the yen appreciation, the Japanese economy suffered from further contraction stress. When Japan responded with expansionary monetary policy to lower the discount rate and increase money supply, the result was a bubble economy. According to his explanation, Japan did not have an inflation problem at the time, and only had to raise asset prices. Worried about the prospect of inflation, the Bank of Japan suddenly put the brakes on the economy, and a burst bubble dragged the whole economy into a serious recession.

Having a different judgement on the impact of the Plaza Accord on the Japanese economy, Yu criticizes the predominant view among Chinese analysts on the issue of RMB appreciation. He argues that the biggest mistake lies in the belief that RMB appreciation would only benefit the US economy. His aim is to remind the public and decision-makers not to be too defensive. His view is that 'the question is not the one if we should stop appreciation, but how much and in what way China should facilitate appreciation' (Yu, 2007). He supports 'reasonable' RMB appreciation, emphasizing that the RMB appreciation might be painful in the short run, but would serve the long-term interests of the Chinese economy.

Yu cited the positive example of Germany to support the pro-appreciation position. He examines German economic history in the post-Second World War period and points out that during the three decades from 1960 to 1990, the nominal exchange rate of the Deutschmark against the US dollar increased from 4.17:1 to 1.49:1, accumulatively 1.79 times upwards. The extent of the mark's appreciation was even greater than that of the Japanese yen. In his opinion, in dealing with the 'unholy trinity' of objectives (independent monetary policy, free capital flow, and fixed exchange rate), German monetary authorities chose currency policy autonomy and the free flow of capital, and left the exchange rate of the Deutschmark to float freely (Yu, 2007). Therefore, Yu advised China's decision-makers not to be too concerned about the appreciation of the RMB, and that they should be open to the option of appreciation if it serves other policy objectives.

(iii) Resisting US pressure on RMB appreciation

Most Chinese analysts oppose a Chinese version of the Plaza Accord as the solution to global imbalance, and believe that the dramatic appreciation of RMB only damages the Chinese economy, and would not even help the US economy. US and European demand for the Chinese currency appreciation only serves their domestic political ends.

First of all, Chinese economists argue that the RMB's rapid appreciation would only reduce Chinese exports but would not increase imports from the countries imposing exchange-rate pressures. Based on different comparative advantages, Chinese exports have not yet replaced US manufacturing, but instead compete with the exports of other developing countries. Considering the fact that the wage level of Chinese workers is a mere 5 per cent of the average wage of US workers, as Chen Zhiwu (2011) argues, even if the RMB sharply appreciates by 50 per cent to double China's labour cost to be over 10 per cent of the US labour cost, manufacturing jobs would still not return to the US. The only result would be that the US would import more from other developing economies to substitute for imports from China. Chen suggests that the American public should lower their expectations about the positive effects of rapid RMB appreciation, in terms of reducing the trade deficit or causing job creation (Chen, 2011). Such rapid appreciation does not work to help the US economy, and would do substantial damage to the Chinese economy, and cause instability in China's financial sector (Zhang Yansheng, 2010).

Second, China's trade benefits are limited compared with the greatest potential beneficiaries, the multinational corporations (MNCs). As Zhang Yansheng argues, the trade data show that the trade surplus of China is earned mainly by MNCs, particularly in the manufacturing sector (Zhang, 2010). As a result of economic globalization, China's export growth has been pushed forward by the intra-firm trade of MNCs. Zhang shows the result of a recent study that in China's processing exports to US in 2005, the direct added-value accounts for only 16.6 per cent, and the total added-value only 28.7 per cent, which is far lower than the rates of added-value in US exports to China: 45.2 per cent and 88.5 per cent. Chinese companies only work at the low end of the international value chains that are dominated by MNCs: they are mainly engaged in packaging and metal and plastic components processing and assembly (Zhang, 2010).

Third, since the global crisis, China has sacrificed its trade and other interests to boost the global and regional economy; a stable Chinese economy, not held down by rapid appreciation, is in the interests of the global economy. As explored by Fan and Liu (2010) of Nankai University, their modelling research shows that the RMB exchange rate is currently not undervalued, but actually overvalued. China's exports have experienced the largest falls at the same time that the country is making great efforts to help boost growth in the global economy.

Noticeably, although the Chinese government has stated repeatedly that it opposes any external effort to force the appreciation of the RMB, it has been accommodating to the changing international economic environment, and the pressures for the RMB to appreciate gradually. Since the exchange-rate reforms adopted in July 2005, the value of the RMB against the US dollar has appreciated by about 30 per cent. Chinese Premier Wen Jiabao consistently emphasizes the principle that China should reform its currency exchange mechanism independently, gradually and under government control, calling it a point of national sovereignty (Wen, 2010). His statement may offer an explanation for China's cautious gradual approach to appreciation.

VI. Chinese approaches to global rebalancing: collective action and structural adjustment

Given the fact that China has become deeply integrated into the global economy, it is not surprising that the predominant view among Chinese economists and policy-makers is to support rebalancing the global economy. Chinese leaders have urged joining hands to combat the global financial crisis and revive the growth of the global economy by strengthening the multilateral collaboration forums such as the G-20, and they believe that the momentum of economic globalization must be maintained. As Chinese leaders promised at each session of G-20 summits, the Chinese government would be actively cooperating with other major economies to stimulate the recovery of the global economy and do its best to contribute to the objectives of global economic rebalancing by carrying forward the structural adjustments of Chinese economy. On behalf of the Chinese government, in October 2010, vice governor Yi Gang of the PBoC addressed the IMF and World Bank Annual Meetings and announced that in order to improve the situation of global imbalances, the Chinese government aimed to downsize the proportion of trade surplus to GDP from 5.8 per cent in 2009 to 4 per cent within 3–5 years. The latest data show that China's trade surplus–GDP ratio has already been dropping significantly: the ratio of China's current account surplus to GDP has declined from nearly 12 per cent in 2007 to about 3 per cent in 2011; and over the same period the trade surplus proportion declined from 7.5 to 2.1 per cent. These ratios have dropped substantially, and have been lower than those of Germany and other trade surplus countries (Pan, 2011). Therefore, some researchers point out that the yuan may have been close to the equilibrium exchange-rate level (Yiping Huang, 2012).

On rebalancing the Chinese economy and the global economy, some common approaches have been developed among scholars, policy researchers, and officials. First of all, scholars have advocated the 'common' responsibility theory, emphasizing international cooperation to avoid confrontation. Believing that global imbalances harm all economies, the main countries must work together. The efforts should not come only from some single country such as China. CASS scholar Zhang Ming (2010) argues that since the global financial crisis, the evolution of the imbalance of international payments has been unpredictable and complex, and hence rebalancing the global economy depends on the collective efforts of major imbalanced economies. He suggests that the interaction of internal and external imbalances should be examined from the perspective of the global economy as a whole. Yi Gang stated in his 2010 speech that developed countries should also play their part in the adjustment of global imbalances. Though China has become the second largest economy, Chinese economy is still less than 40 per cent of the US economy and all the G-20 member states should make their contribution to the elimination of global imbalances in accordance with their own conditions (Pan, 2011). Lei Da, a scholar of Renmin University, suggests that there is still lack of experience in solving the problem of the imbalances between the developed and developing countries. For China, it has to adjust its economy and adapt to the changing external economic environment (Lei, 2010).

Second, some economists contend that the Chinese government should maintain its political determination to carry forward structural adjustment of the Chinese economy, no matter how much other countries could help or not in global rebalancing. China should restructure its export-oriented development strategy and reduce its dependence on external markets, and focus on domestic demand as the main driver of economic growth. In order to reduce the current account surplus, the country needs to narrow the gap between savings and investment, and expand consumption. The government must increase fiscal spending to provide sufficient public goods to improve healthcare provision and the social security service. Only this way would the anxiety of people about securing their social welfare be reduced, and they might then be willing to reduce their savings (Yu, 2007; 2010).

Third, in order to reduce China's current account surplus, the country should adjust its foreign direct investment (FDI) policy. Economists stress that the preferential treatments extended to foreign business in China should be cancelled. One commentator (Guest Commentator, 2011) criticizes China's foreign investment policy which extends excessive subsidies to MNCs. Under the pressure of unfair competition, local governments provide multinational companies with land incentives, and help them maintain a low standard of labour protection, which forms the base for China's strong trade position. The commentator suggests that China must adjust its development strategies for its own interests.

Fourth, some other economists argue for improving the financial system, to make full use of domestic capital markets, to ensure the savings can be used by domestic investors. They tend to believe large-scale foreign reserve holdings and purchase of US treasury bonds reflect the structural imbalance of the Chinese economy and the underdevelopment of China's financial industry. China has to make great efforts for the development of its financial market and the building of a welfare system. Only by this, can the problem of the structural imbalances of Chinese economy be redressed. Zhang Liqing (2007) suggested that, in terms of domestic structural adjustments, financial reform and the opening up of capital markets should be an important priority.

Finally, some economists call for curbing the expansion of the state-owned economy as a partial solution to rebalancing Chinese economy. How to assess the role of the state-owned economy has become a hot topic in China since the onset of the global financial crisis. Chen Zhiwu (2011) points out that the state ownership of resources and the government-controlled economy have contributed greatly to China's rapid industrialization, but it has to adapt to the new international economic environment following the global financial crisis, which demands transforming Chinese economy from an export-driven one to a more domestic consumption-driven one. Chen and other economists share the view that by heavily investing in the state-owned enterprises, the state-owned economy actually inhibits the growth of domestic consumption. They suggest extending more rights for the public to oversee the state-owned enterprises (SOEs), and the government should allocate the people more dividends to boost domestic consumption.[1]

[1] Some Chinese economists argue that in the last decade, the Chinese economy has become the one mainly driven by investment rather than consumption. Investment accounts for about 50 per cent of GDP and domestic consumption only one-third of GDP. The rapid expansion of SOEs should take part of the responsibility for the low level of domestic consumption. They suggest ways to improve the situation, including the SOEs' transfer of dividends to government for funding the social welfare system and by this increasing the consumers' income. For a more detailed study of this issue, please refer to Huang Sujian (2008).

With regard to the global economy, Chinese academic and policy researchers urge for reforms in the international economic system. Generally speaking, the mainstream voices among Chinese analysts have recommended not to overthrow but to have a moderate reform of the existing international economic system. Zhang Boli (2009), vice president of the CPC Central Party School, emphasizes that neither anti-globalization nor de-globalization should be the right solution to the impact of the global financial crisis, and strengthening international cooperation and coordination would be the only choice, to echo the statement of Chinese president Hu Jintao at the London G-20 summit: 'this global financial crisis takes place in the context of deepening economic globalization and increasing interstate interdependence. No country is immune, and cooperation should be the right choice.' Zhang argues that deepening the reforms of these economic mechanisms to improve fairness and efficiency has become inevitable. Among all the measures, improving the representation and voting power of developing countries in the IMF and World Bank and enhancing the regime of early warning and surveillance should be the top priorities.

In terms of reforming the existing world economic system, Chinese analysts put some emphasis on restructuring the international monetary system. In an article published in March 2009, Governor Zhou Xiaochuan called for the expanding role of SDRs as some sort of super-sovereign currency, to reduce reliance on the US dollar as the major reserve currency (Zhou, 2009). Though Zhou stated that his essay was merely a 'scholarly thinking' piece, his views have been echoed by other policy advisers and analysts such as Zheng Xinli (2010; 2011*a*,*b*). Most Chinese experts who support the idea of SDR, however, recognize that it may take a long time to replace the US dollar with SDR as the major reserve currency. In the short run, as Zhu Bangning, a professor of political economy at the Central Party School emphasizes, to keep the position of the US dollar as the 'important' reserve currency and stabilize its exchange rate should be in the interest of most countries in the global economy today (Zhu, 2011).

In addition to a larger role for SDR, it is also a popular idea among Chinese analysts to call for the emergence of a competitive multi-currencies system, which is perceived to be a more realistic route to the improvement of the international monetary system. Among many proponents, Zheng Xinli (Zheng, 2010; 2011*a*) argues that to cultivate more currencies as reserve currencies and let them to compete with each other, can not only meet the demand for liquidity in international transaction, but also help check the abuse of currency power by the single reserve currency provider. He argues that 'to set up a diversified and mutually competitive system of international reserve will be the fundamental way to stabilize international monetary system'. According to his prediction, the US dollar, the euro, and the RMB, as major reserve currencies, will compete with and check and balance each other in the future. As he argues, the competitive currency regime would help the major reserve countries to carry forward a stable and robust money policy to stabilize the value of their currencies and maintain credibility. Along with this kind of policy thinking, most analysts support Chinese government efforts to gradually internationalize the RMB. They argue that, as that of an emerging economy, China's currency should play a larger role in the global economy, and contribute to reduce the risks and cost caused by highly volatile foreign-exchange markets.

VII. Conclusion

This paper is aimed at interpreting the perceptions of Chinese mainstream economists and policy advisers about the question of global economic rebalancing, to help plug the gap in the West's understanding of the rising Chinese economy and its relationship with the global economy.

The global financial crisis has brought forth tremendous changes in the global economy. To Chinese analysts, China has become a convenient target of criticism for politicians and interest groups in the West and in the US in particular, in the time of economic recession. To many of them, this criticism is illogical from the perspective of economic theory and is irresponsible and intended politically. To them, this criticism, targeting China, is only the trickery of US politicians attempting to divert the world attention away from the US's responsibility for causing the global financial crisis, and to impose the cost of adjustment on other countries such as China. As the paper has shown, although they have somewhat different views on the causes of the crisis, Chinese economists and policy advisers do not deny the existence of global economic imbalance. They recognize that China is part of the problem, and the best way to achieve the goal of global economic rebalancing lies in international policy coordination and cooperation. What they are strongly opposed to is the argument that China should take the major responsibility for the global economic rebalancing alone, and the scapegoating of China for the crisis by some Western politicians. Naturally, the once-off RMB appreciation based on the Plaza Accord is not favoured by Chinese policy advisers.

The value of the Chinese analysis of the root causes of the global financial crisis and global economic imbalance lies in the way that most Chinese economists look into these questions by highlighting the two associated imbalances, the current account imbalance and power imbalance embedded in the international monetary system. Differently from the dominant explanation in the West, which mainly stresses current account imbalances and the large appreciation of RMB as the necessary solution, Chinese analysts point to the international monetary system as the 'more fundamental' cause. Obviously, this sort of argument is not limited to Chinese analysts, but also shared by scholars and policy researchers in developing countries and emerging economies. This is the intellectual context in which emerging economies have worked together to push forward the reforms of global economic governance in the G-20, the IMF, and the World Bank (Marchyshyn, 2011).

On the other hand, we have to recognize that the mainstream Chinese analysts are not hostile to the West-dominated international economic system. The majority of them call for moderate and pragmatic reform to the existing system, emphasizing the nature of economic interdependence brought forth by the development of economic globalization. On the solution of the issue of global economic rebalancing, they insist that China should adopt a structural adjustment to its own economy which has been over-dependent on exports and incentives to foreign invested enterprises. These policy recommendations have been taken seriously by Chinese decision-makers, though the implementation of this advice will create a lot of hardship.

Generally speaking, the analysis of Chinese perspectives seems to have conveyed a cautiously optimistic message on international policy cooperation to achieve the objectives of global economic rebalancing. Though Chinese and Western views are not necessarily the same, influential Chinese economists are in support of international policy cooperation mixed with enthusiastic urges for reforming the current international economic system.

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