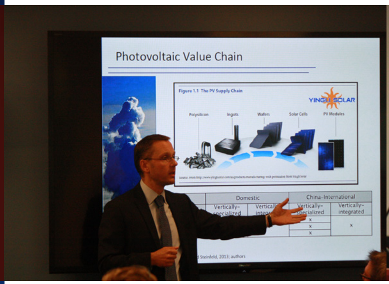
**ASIA REPORT**
ISSUE NO. 27
MAY 2014





Sigur Center
for Asian Studies

THE GEORGE WASHINGTON UNIVERSITY

# Asia Report: Beyond Competition: Anomalies in How States React to a Rising China

As China's influence on geopolitics, energy markets, trade, and the global financial system continues to expand, conventional wisdom might predict growing resistance from Beijing's wary neighbors. The Realist school of thought points to regional territorial disputes and economic rows as evidence of unavoidable competition in the face of a rising China. However, there are several key variances in how countries have responded to this challenge.

This Asia Report explores a seminar hosted by the Rising Powers Initiative on May 7, 2014 where Asia's Economic Challenges project scholars presented their findings on Asian overseas oil investment, responses to China's growing solar exports, understanding China's evolving monetary policies, and the complex India-China relationship. An audio recording of the seminar can be found here. The experts who spoke include:

- **Robert Weiner**, Professor of International Business, Public Policy and Public Administration, and International Affairs, GWU
- **Llewelyn Hughes**, Assistant Professor of Political Science and International Affairs, GWU
- **Jiawen Yang**, Professor of International Business and International Affairs, GWU
- **Deepa Ollapally**, Research Professor of International Affairs and Associate Director, Sigur Center for Asian Studies, GWU

The project – made possible through the generous support of GWU's Centers and Institutes Facilitating Fund and the Carnegie Corporation of New York – will release additional research and reports in the coming months. The project's findings demonstrate to policymakers that there is a greater degree of complexity in how countries respond to Asia's economic challenges than previously assumed.

## Economics Ties that Bind

While each scholar focused on a different economic challenge in Asia, a common theme emerged: the dilemmas of the 21st century require a fundamentally new understanding of why some countries compete and why others elect to cooperate. Nations trade places along the spectrum of economic, military, and political power, and traditional sources of competition may no longer compel conflict and may instead offer collaborative opportunities.

*"Resource nationalism" or the competitive drive for energy supplies has not resulted in "resource poor" countries unfairly paying above market rates for oil relative to "resource rich" ones. Over the long run, it turns out everyone overpays. Policymakers need to understand this economic reality as they design their country's energy security plans.*

As the world's largest oil importer, China impacts global energy markets and energy security policies of Asian powers. Some observers contend China's growing demand for energy resources motivate "unfair" practices to gain access to oil reserves through higher than market value purchases and favorable dealings with unscrupulous governments. Dr. Weiner's research on energy purchasing decisions, however, showed little difference between foreign oil purchases of "resource rich" and "resource poor" countries. Furthermore, Weiner argued China's individual energy company managers are "running the show," rather than party leaders in Beijing. Most of these energy acquisitions are sold abroad and not brought to China. "Resource nationalism" or the competitive drive for energy supplies has not resulted in "resource poor" countries unfairly paying above market rates for oil relative to "resource rich" ones. Over the long run, it turns out everyone overpays. Policymakers need to understand this economic reality as they design their country's energy security plans.

Since the mid-2000s, China has become a leading exporter of solar energy modules and related equipment. Though the European Union (E.U.) and Japan once held that mantle, they now import considerable amounts of renewable technologies from China. Conventional wisdom would expect domestic solar industry and special interest groups to push restrictive tariffs and trade policies to limit Chinese solar imports. Dr. Hughes observed, however, that the European Union and Japan have not engaged in widespread "green protectionism." Domestic solar industries were unable to meet the high demand for solar in their respective countries. Instead, most Japanese and E.U. solar manufacturers became deeply integrated with Chinese firms in the global value chain for solar technologies. Unlike more vertically integrated and self-contained industries, Japanese and E.U. solar firms often rely on Chinese solar modules for their business. Accordingly, Japanese and E.U. leaders have sought cooperative opportunities to meet solar energy goals.

The 2008 financial crisis revealed the extraordinary degree to which the global economy has become closely intertwined. Economic downturns and subsequent recovery plans in one country have tremendous spillover effects elsewhere. China and the United States responded to the financial crisis with substantial monetary policy efforts to inject money into the economy. Monetary theory suggests the more money available for banks to lend at low interest rates, the more spending, investment, and economic growth can occur. U.S. monetary efforts, however, took much longer to impact the United States economy compared to similar attempts in China. Dr. Jiawen Yang studied possible explanations for this discrepancy and concluded the U.S. banking sector has unique qualities that make it less sensitive to monetary policy: access to international financing, an ability to move capital between various subsidiaries, and a greater flexibility in lending policies. Due to these factors, Yang contends U.S. banks play a more active role in the economy than most analysts believe. Chinese banks, on the other hand, are government owned and administered, leaving fewer opportunities for banks to moderate official monetary policy. With China's recent interest in reforming its banking system to mirror the United States, Yang said leaders should be aware of the policy implications this trend could have for the global financial system. During the next financial crisis, countries may no longer be able to lean on China's "efficient" monetary policy and traditional capital flows as the global economy becomes more integrated.

***...The U.S. banking sector has unique qualities that make it less sensitive to monetary policy: access to international financing, an ability to move capital between various subsidiaries, and a greater flexibility in lending policies.***

## Strategic Considerations of India

While India's political-military relationship with China presents numerous challenges, ever-increasing economic interdependence has presented a paradox in the Sino-Indian relationship. On the economic side, trade relations have never been stronger, peaking at $52 billion in 2008 (up from $260 million in 1991). Though India's trade deficit with China has now reached $30 billion in 2013 – accounting for one third of India's overall deficit – China-India economic relations remain generally positive.

On the strategic end, however, unresolved issues persist, including border disputes, energy security competitions, China's perceived containment of India vis-à-vis its "string of pearls" in the Indian Ocean, and India's perceived containment of China vis-à-vis relations with the United States. How has India responded to this complicated picture, juggling economic asymmetric interdependence and strategic rivalry with China?

Dr. Ollapally observed that despite these dissonant factors, Indian domestic debate on China as a threat versus an opportunity is tilting towards the latter. Although Indian media and sections of the strategic elite tend to take a nationalist tone on China, Indian policymakers across parties, along with key business sectors, have been following a much more pragmatic approach. India sees more prospects in economic interdependence than in strategic rivalry with China. Because China is such a major regional player, the general consensus is that India needs good relations with China. Moreover, there is widespread belief that India cannot rely on the United States if it were to become entangled in a face-off with China; this is a big reason India has not joined the U.S. rebalance against China. Given these factors, India has pushed to engage and embed itself more in the Asia-Pacific region through economics and multilateralism. Domestic discourse adds significant explanatory power in understanding India's relations with China. While political discord exists in the relationship, economic interdependence has raised the opportunity cost of engaging in conflict, thereby driving China and India closer to one another.

***Although Indian media and sections of the strategic elite tend to take a nationalist tone on China, Indian policymakers across parties, along with key business sectors, have been following a much more pragmatic approach. India sees more prospects in economic interdependence than in strategic rivalry with China.***

## Conclusion

Contrary to what the Realist school might predict, nations that might be expected to clash with China have instead embraced cooperation with Beijing via economic ties. While some criticize China for its "unfair" practices to acquire energy resources, in fact, research demonstrates that the competitive drive for energy supplies has resulted in both "resource rich" and "resource poor" countries overpaying for oil. Similarly, although China has overtaken the E.U. and Japan as a leading exporter of solar energy modules, Japanese and E.U. leaders have sought cooperative opportunities to meet solar energy goals, rather than pushing restrictive tariffs and trade policies. Monetary policies across the map are becoming increasingly interconnected as global financial crises and recovery efforts keep countries from drifting toward economic islands. In the case of divergent economic-strategic circumstances in the Sino-Indian relationship, India has turned its focus to economic cooperation with China, rather than placing emphasis on strategic concerns that could create economic opportunity costs. All of the above instances demonstrate the range of complexity in how countries are responding to Asia's economic challenges, especially with an eye on a growing China. If U.S. policymakers want to understand how China's neighbors are responding to its rise, they should look beyond the lens of conventional wisdom and examine the domestic debates that shape this important region.

*Timothy Westmyer, Research and Program Assistant, Rising Powers Initiative, Sigur Center for Asian Studies*

*Winnie Nham, Research Manager, Rising Powers Initiative, Sigur Center for Asian Studies*

## *About the Sigur Center for Asian Studies*

Sigur Center for Asian Studies
THE GEORGE WASHINGTON UNIVERSITY

The Sigur Center for Asian Studies is an international research center of The Elliott School of International Affairs at The George Washington University. Its mission is to increase the quality and broaden the scope of scholarly research and publications on Asian affairs, promote U.S.-Asian scholarly interaction and serve as the nexus for educating a new generation of students, scholars, analysts and policymakers.

Sigur Center for Asian Studies
Elliott School of International Affairs
The George Washington University
1957 E St. NW, Suite 503
Washington, DC 20052

TEL 202.994.5886
EMAIL gsigur@gwu.edu
http://www.gwu.edu/~sigur