


## China has changed the global economic order – with the help of Europe

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Ten years ago China was increasingly seen as an important economic power. It had just overtaken France to become the fifth biggest economy, was reaching almost \$1 trillion in foreign reserves and was slowly learning how to successfully operate within the WTO framework. A decade later, **China is the second biggest economy in the world (even the first in purchasing power parity, PPP)**, it has around \$3.5 trillion in reserves and is second only to the US in global power.

The Global Financial Crisis, which started in the US in 2007 and spread to the rest of the world in 2008-2009, was an important watershed in China's rise to the top. It coincided with the Olympics in Beijing, the globally televised event that demonstrated to the whole world that China was again a modern and sophisticated country that could compete with the bests. Before the crisis, China was not part of the G-club. The G8 was formed by the US, Japan, Germany, UK, France, Canada, Italy, France and Russia. However, the bankruptcy of Lehman Brothers and the almost collapse of Wall Street changed that. Very quickly **the Western powers and Japan realized that they needed China's helping hand to overcome the biggest recession** since the 1929 Crash.

China's 2008-09 CHY4 trillion stimulus package was a very important contribution to stabilize the world economy. For the first time the Middle Kingdom was included among the leading nations by participating in the G20, and it also started to behave as a key stakeholder that looks to its domestic interests, while taking into consideration the external ramifications of its policies. **Thanks to China's solid post-crisis growth the world economy recovered.** China's hunger for commodities has helped many economies in **Latin America and Africa** to grow. **Europe**, and especially **Germany**, have also benefitted from exporting more to China. In total, China contributed around 40% to the annual growth of the world economy from 2009 to 2014. Thus, it has taken over from the US in being the global growth locomotive.

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While ten years ago few Westerners could name any Chinese company, today they are likely to know Huawei, Haier, Alibaba and WeChat. China has moved from being the global factory to being a modern economy with its own global brands. **This extraordinary growth pattern has emboldened China to be more proactive in its economic diplomacy.** Consequently, 2015 will go down in history as the year when

China started to change the global economic order. Three major developments occurred this year. The launch of the Asian Infrastructure and Investment Bank (AIIB) in Beijing, the creation of the New Development Bank (NDB) in Shanghai and the inclusion of the RMB in the IMF's Special Drawing Rights (SDR) basket.

These are three major milestones. The NDB has brought together Brazil, Russia, India, China and South Africa (BRICS), some of the most important emerging markets in the world. It is the first multilateral bank that does not have any presence from Western powers. This is historic. It is also important to highlight that while the headquarters are in Shanghai, the first president is an Indian national, K.V Kamath, and all five countries will have the same voting power. Hence, there will not be veto power. This is a very different organization than the IMF and the World Bank where voting powers are adjusted according to quotas.

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The AIIB is even a bigger transformation of the global economic order. **For the first time ever China has taken the initiative in constructing a multilateral institution which includes both developing and developed countries.** Despite active US diplomatic efforts to stop the adherence of European countries to the project, first the UK, and then Germany, France, Italy and Spain (the five biggest European economies) have joined around 60 other countries as founding members. The creation of the AIIB is a major diplomatic victory for China. Not least because it has left the US and Japan isolated.

The presence of the Europeans is particularly significant because China knows that their involvement will give the AIIB more credibility. **Its chairman, Jin Liqun, has recognized that he hopes that the Europeans will take an active role** in designing the organization, strategy, standards and priorities of the new bank. He is fully aware that the Europeans have more than 50 years in organizing and managing multilateral financial institutions focused on infrastructure and development such as the European Investment Bank and the European Bank for Reconstruction and Development. This expertise and know-how is extremely useful for China.

Europe has also been fundamental for China's third major diplomatic achievement this year: the inclusion of the RMB in the IMF's SDR basket. For a long time the US and Japan opposed the inclusion arguing that China needed first to comply with three principles: full liberalization of the capital account, free floating of the RMB and full independence of the central bank. Logically, the Chinese government has always resisted this pressure. The European powers, on the other hand, have always thought that given China's importance in the world economy it would be convenient to include the RMB as a first step towards the full convertibility of the Chinese currency. For the European Union it is important to have China around the table. Thus, the inclusion of the RMB in the IMF's SDR is a victory for Europe too.

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In general, **in Europe the view is that neither the US nor China should ask its European partners to side with them against the other.** The members of the EU want to do business with both. This is reflected in Europe's greater openness to Chinese investment than in the US. As a matter of fact, in the last 10 years China has gone from almost having no presence in the Old Continent, to investing €14bn in 2014, and having an overall stock of €46bn, which is roughly double the amount invested in the US. By China having a bigger presence both in the world economy and its governance, Europe and China are getting closer together. This is a positive development. Hopefully soon the two will sign a bilateral investment and a free trade agreement. This will increase further our mutual understanding and interdependence.

**Ancient Chinese strategists always believed that a tripolar system is the best political configuration for stability.** The same goes for global economic governance, and the three main poles (although not the only ones) should be: the US, China and the European Union.