Book Review: The Evolving Role of China in the Global Economy

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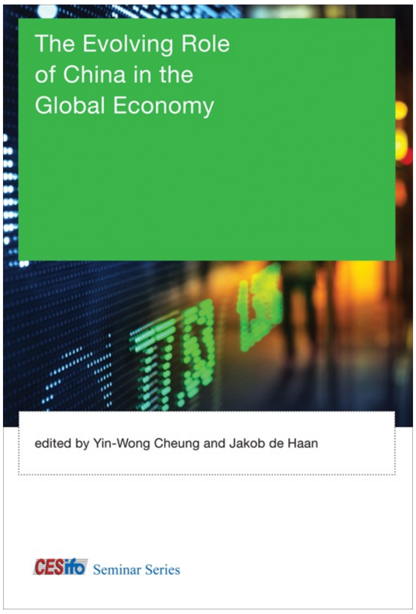
The Evolving Role of China in the Global Economy *is a serious scholarly effort to understand the economic dynamics of the world's second largest economy, writes* ***Ross Harvey****. With sections on exchange rate policy, savings and investment, monetary policy and capital controls, and foreign direct investment, this book seeks to offer a systematic analysis of the factors in China's rapid economic growth.*

The Evolving Role of China in the Global Economy. Yin-Wong Cheung & Jakob De Haan. MIT Press. October 2012.



Find this book:

The Evolving Role of China in the Global Economy is the latest contribution to understanding one of the most remarkable growth stories of the last four decades. Edited by Yin-Wong Cheung and Jakob de Haan, the book provides an orthodox economic analysis of China's growth, using econometric models to explain China's exchange rate policy, savings and investment, monetary policy and capital controls, and foreign direct investment (FDI). For those interested in mathematically-informed analyses of the "Asian miracle", this book is a worthy read; but for those seeking a more political economic perspective which grapples with the "hidden hand" of the Chinese Communist Party (CCP) during this period, the book may disappoint.

Opening with China's exchange rate policy, the contributors provide some welcome insights on the renminbi debate and whether it really is predatorily overvalued. The second part of the book examines Chinese savings and investment, in which Juann Hung and Rong Qian controversially suggest that savings rates are actually not that much higher in China than across the rest of the world. Thirdly, the contributors address China's monetary policy and capital controls, finding that China has largely been able to insulate its monetary policy from international monetary movements. Contributors in this section also find that Chinese authorities can still maintain a significant degree of capital account control while promoting offshore use of its currency. The final section examines the determinants of China's foreign direct investment (FDI) strategy and its quest for resources. In a world that is increasingly asking questions about the impact of China's hunger for natural resources, these two chapters are really important and are the primary subject for this review.

Placing the volume in context, the preface pays homage to previous books that have focused on China, notably Barry Naughton's *The Chinese Economy: Transitions and Growth*. But it fails to mention Yasheng Huang's work, *Capitalism with Chinese Characteristics*, which skilfully critiques Naughton's view and provides a better explanation for the foundations of Chinese growth.

The book would also have benefited from explicitly framing the questions it addresses in the context of China's 12th five-year economic plan, currently underway. This plan envisages a move away from investment-led export growth toward higher levels of domestic consumption and services (which are more labour-absorptive on the margins than manufacturing). But the prerequisite for this move is to complete the industrialisation phase (by 2020), which requires the importation of large quantities of raw materials and significant energy capacity.

Xingwang Qian does a thorough job in chapter 12 of tracing China's quest for external oil supply. The centrepiece of analysis here is the 'going global' policy, under which China's national oil companies began an aggressive global expansion after 2002 (p. 375-376). It was not without controversy and China has been accused of colluding with rogue states such as Sudan, in addition to jeopardising global energy security by shipping oil straight to China. Qian rightly points out, however, that these accusations are largely anecdotal "and lack formal econometric analysis on [the] determinants" of China's oil investments (p. 377). This is a significant problem in the literature that deals with China generally, and China in Africa in particular. But Qian himself begins by asserting that China is diversifying its oil supply away from the Middle East "due to the prolonged instability in the area" (p. 377) and toward Africa for that reason. But stability is hardly a staple of African states. Qian's econometric models suggest that corruption is a key attractor of Chinese oil investment, but this weakens his argument for why it is diversifying away from the Middle East.

Aside from the dubious findings pertaining to the centrality of corruption in determining where China will invest to secure oil, there are problems with the econometrics. For instance, Qian uses real Gross Domestic Product (GDP) per capita as a "typical measure for the level of infrastructure" (p. 384). However, a country's infrastructure levels should be an explicit control variable in the model as its relation to GDP is not perfectly linear. This is important because the model produces findings that "China's ODI tends to go to an oil nation with poor infrastructure" (p. 392), and this is apparently explained by China's proclivity to offer "oil-for-infrastructure deals". But this conclusion does not follow even if the finding itself was accurate. There could be a number of alternative explanations such as the simple need to secure oil supply regardless of local conditions.

Qian also finds that once China has decided to invest in a country, corruption again plays an influential role in determining how much FDI will find its way there. Here at least the explanation is plausible, that China invests in corrupt countries not because it is inherently attracted to corrupt states but because it is a relative latecomer to the global oil game and will invest wherever it can secure supply in the context of fierce competition. And yes, corruption is perhaps less of a concern for Chinese oil companies than it may be for some other international oil companies, but this argument is significantly weakened in light of Shell's history in the Niger delta, for instance.

The regressions also reveal that "a selected oil-producing country with a stable political system and less social tensions attracts China's ODI" but that "China invests more ODI [in] countries loaded with corruption and poor in law and order" (p. 393). The author then concludes that "China's ODI is generally averse to political risks" (p. 410). This is frankly confusing, as there is no argument offered as to why corruption and low levels of law and order are not considered synonymous with political risk and instability.

'China's Investments in Africa', the final chapter, warrants a review in itself, this reviewer feels. It examines the extent to which political considerations and host-country characteristics determine China's FDI in Africa. The authors use two datasets – one from 1991 to 2005 and another from 2003 to 2007 – and find that for the first one, political variables are significant in attracting Chinese FDI, but not for the second. Economic ties and the drive for natural resources best explain Chinese FDI in the latter. These are very different findings and force the reviewer to question their validity on those grounds alone. While the chapter is a welcome addition to the China-in-Africa literature, the econometric models suffer from similar defects to the ones in the previous chapter (the same strategy is followed), and the findings again lead the authors to conclude that China is averse to instability but attracted to corruption. This conclusion is potentially spurious, however, given that resource-security and geopolitical strategy are probably the primary motivators for investing in Africa. Corruption and instability are therefore likely incidental rather than instrumental determinants.

Overall, *The Evolving Role of China in the Global Economy* is a serious scholarly effort to understand the economic dynamics of the world's second largest economy. Even if some of the conclusions inadvertently raise more questions than answers, the book will hopefully steer the debates about China in a more useful and rigorous analytical direction now.

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Ross Harvey is a Ph.D student at the University of Cape Town's School of Economics. His research focuses on the impact of Chinese economic involvement on economic wellbeing in selected African countries. He is particularly interested in whether natural resource wealth extraction in these investment deals will turn out to be positive for these countries' economic performance in the long run, or whether it will simply entrench rent-seeking political elites at the expense of local economic wellbeing. He works as a freelance researcher and was previously a research and communications staffer for the official opposition party in South Africa. He tweets @harvross and can be found on Academia.edu. Read more reviews by Ross.