

China's Soft Power and The Global Financial Crisis

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Three or Four Examples of China's Soft Powers

- Governor Zhou Xiaochuang's SDR Proposal for Reforming International Financial System
- The Global Attraction of "Socialist Market Economy" ?
- A Chinese Spin on Baroque Opera
- Albert Hirschman Exit/Voice Perspective on China's Political System

Zhou Xiaochuan : Reforming the International Monetary System

“Issuing countries of reserve currencies are constantly confronted with the dilemma between achieving their domestic monetary policy goals and meeting other countries' demand for reserve currencies. On the one hand, the monetary authorities cannot simply focus on domestic goals without carrying out their international responsibilities ◆◆ on the other hand, they cannot pursue different domestic and international objectives at the same time. They may either fail to adequately meet the demand of a growing global economy for liquidity as they try to ease inflation pressures at home, or create excess liquidity in the global markets by overly stimulating domestic demand. The Triffin Dilemma, i.e., the issuing countries of reserve currencies cannot maintain the value of the reserve currencies while providing liquidity to the world, still exists”.

Zhou Xiaochuan : Reforming the International Monetary System

“When a national currency is used in pricing primary commodities, trade settlements and is adopted as a reserve currency globally, efforts of the monetary authority issuing such a currency to address its economic imbalances by adjusting exchange rate would be made in vain, as its currency serves as a benchmark for many other currencies. While benefiting from a widely accepted reserve currency, the globalization also suffers from the flaws of such a system. The frequency and increasing intensity of financial crises following the collapse of the Bretton Woods system suggests the costs of such a system to the world may have exceeded its benefits. The price is becoming increasingly higher, not only for the users, but also for the issuers of the reserve currencies. Although crisis may not necessarily be an intended result of the issuing authorities, it is an inevitable outcome of the institutional flaws”.

Zhou Xiaochuan : Reforming the International Monetary System

“A super-sovereign reserve currency not only eliminates the inherent risks of credit-based sovereign currency, but also makes it possible to manage global liquidity. A super-sovereign reserve currency managed by a global institution could be used to both create and control the global liquidity. And when a country's currency is no longer used as the yardstick for global trade and as the benchmark for other currencies, the exchange rate policy of the country would be far more effective in adjusting economic imbalances. This will significantly reduce the risks of a future crisis and enhance crisis management capability”

“Chinese Savings helped Inflate American Bubble”

New York Times, December 25, 2008:

“Others say the Federal Reserve and the Treasury Department should have seen the Chinese lending for what it was: a giant stimulus to the American economy, not unlike interest rate cuts by the Fed. These critics say the Fed under [Alan Greenspan](#) contributed to the creation of the housing bubble by leaving interest rates too low for too long, even as Chinese investment further stoked an easy-money economy. The Fed should have cut interest rates less in the middle of this decade, they say, and started raising them sooner, to help reduce speculation in real estate.

Today, with the wreckage around him, Mr. Bernanke said he regretted that more was not done to regulate financial institutions and mortgage providers, which might have prevented the flood of investment, including that from China, from being so badly used. But the Fed’s role in regulation is limited to banks. And stricter regulation by itself would not have been enough, he insisted.

China: No.1 Holder of US Treasury Bills (in billions of dollars)

	Oct	Sep	Aug (2008)
China	652.9	587.0	542.4
Japan	585.5	573.2	586.0
UK	360.2	338.3	308.0
Carib	219.5	185.3	148.9
Oil Exp	187.7	182.1	180.6

<http://www.treas.gov/tic/mfh.txt>

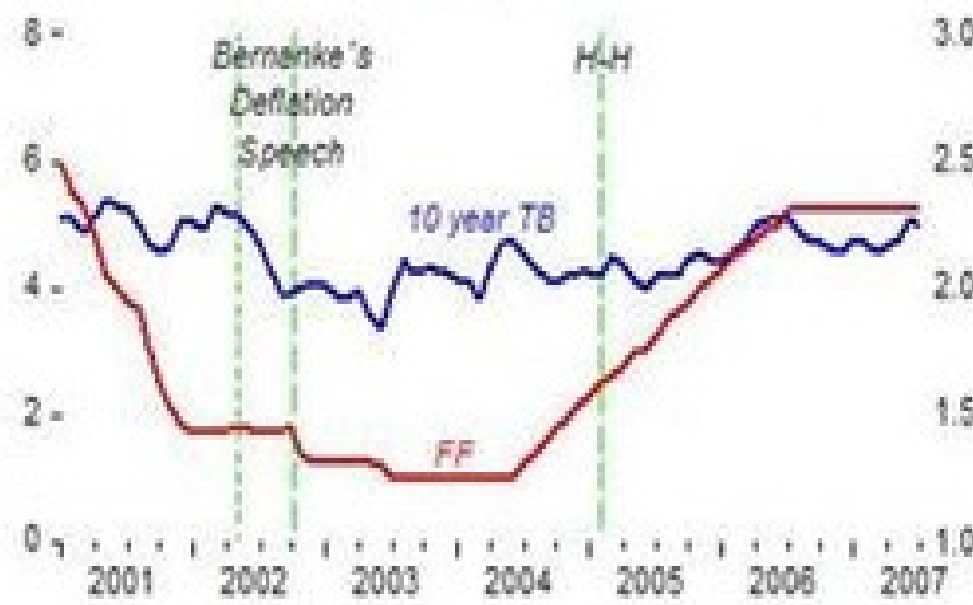
China held \$376 Billion Freddie and Fannie Bonds

The top five foreign holders of Freddie and Fannie long-term debt are China, Japan, the Cayman Islands, Luxembourg, and Belgium. In total foreign investors hold over \$1.3 trillion in these agency bonds, according to the U.S. Treasury's most recent "Report on Foreign Portfolio Holdings of U.S. Securities."

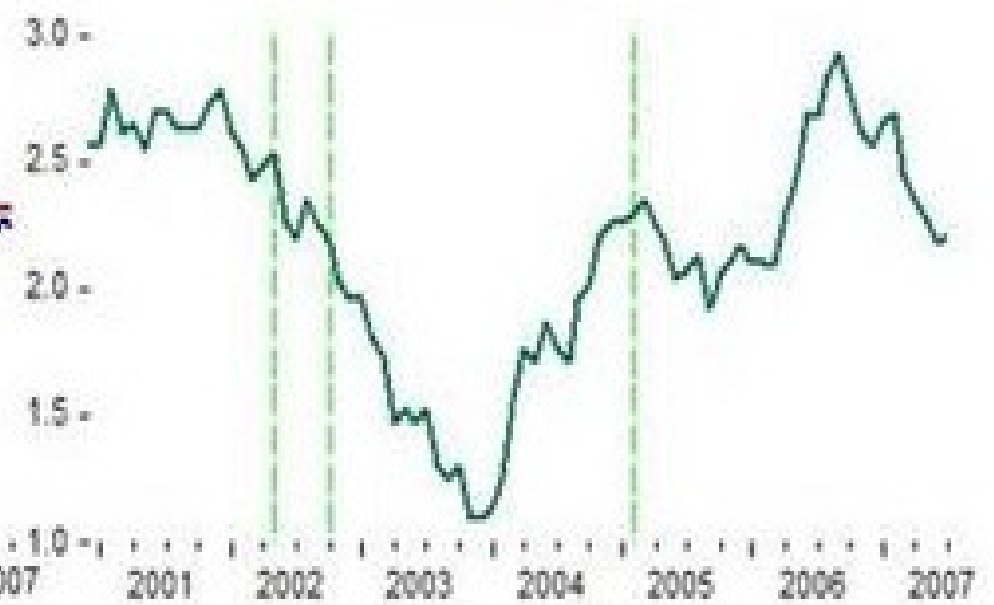
Greenspan's "conundrum"

between June 2004 and July 2006 the Fed raised rates from 1% to 5.25% by increments of 25 basis points in all 17 meetings. In his February/05 H-H testimony before Congress Greenspan used the term "conundrum" (Latin for enigma) to describe the fact that long term (including mortgage) rates had not followed suit.

3 FF & 10 year TB - %



4 Inflation - CPI-C - %



Martin Wolf's Melbourne Lecture 2005

“ A large-scale flow of capital from poor countries to the world's richest nations is perverse. What makes it even more perverse is that strong political forces within the beneficiary country, the United States, resent the generosity of their creditors. Adding to this incendiary situation is the likelihood that the suppliers of finance will ultimately suffer large losses when the United States is called upon to repay – or at least to service – the capital it has received. Indeed, many are already experiencing such losses as the dollars tumbles.”

W.Max Corden

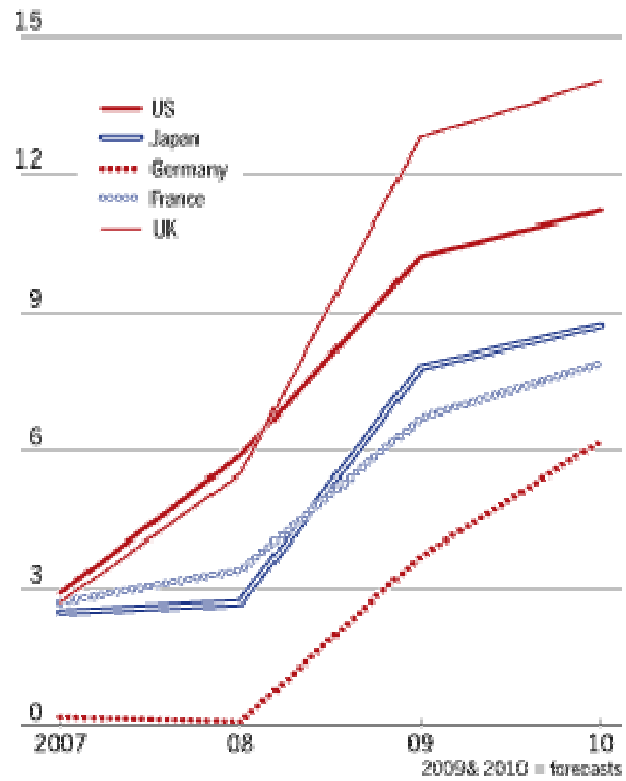
“Temporary Parking Theory of China’s
Current Account Surplus”

China’s Domestic Financial Institutional
Weakness leads to “temporary parking” of
saving abroad

China’s surplus plays only a small part in
determining the current global crisis

Fiscal deficit forecasts

General government financial balance as a % of GDP



Source: OECD

China's "Socialist Market Economy"

- **Looking Glass by Glasshouse Forum No. 3/2009** (Autumn 2009)
- *A China Model? Understanding the Evolution of a "Socialist Market Economy"*, Orion A. Lewis and Jessica C. Teets, 2009, 25 pp.
- From <http://www.glasshouseforum.org/>

Greenspan for Nationalization

Former Federal Reserve chief Alan Greenspan says the U.S. may have to nationalize some banks temporarily to right the financial system and get credit flowing again, arguing it's the least bad option for policymakers. "It may be necessary to temporarily nationalize some banks in order to facilitate a swift and orderly restructuring," Greenspan told the Financial Times ahead of a speech to the Economic Club of New York. "I understand that once in a hundred years this is what you do." Taking temporary control of troubled banks through the FDIC or another mechanism, he said, would "allow the government to transfer toxic assets to a bad bank without the problem of how to price them."

James Meade
(1907-1995)



Hendel's "Semele" Directed by Zhang Huan, staging in La Monnaie

