**Conference[1]: *"Forty years on, how has China changed and how have relations with Belgium and Europe evolved?"***

**Key-note speech by Jonathan Fenby**

**The great meeting: China and the world**

In the decades since Deng Xiaoping launched market-led economic reform and since Belgium and the People's Republic established diplomatic relations, China has undergone a transformation which has not only produced deep domestic effects but also strongly influenced the world as a whole. More people have been made materially better off in the People's Republic in a shorter space of time than ever before in human history. A middle class of perhaps 100 million people has emerged. China has exported deflation through its exports and used the world's largest stock of foreign exchange reserves to help fund the US federal deficit. Chinese demand has become the major influence on commodity markets boosting economies from Brazil to Australia via Africa and the Middle East.

As regards China and Belgium, the two countries have instituted regular high-level exchanges including the visit to Belgium by Prime Minister Wren Jiabao last year during which agreements were signed on nuclear energy, telecommunication, quality inspection and other sectors. Trade has blossomed on both sides. Belgian leaders visit China regularly while the Economic and Trade Commission between the Belgium-Luxemburg Economic Union and the People's Republic provides a forum for discussions on trade and investment. A direct flight between Beijing and Brussels went into service last year. Cities in the two countries have established regular exchanges. In other words, the relationship has developed on a number of levels and forms part of the broader engagement between China, Europe and the world.

Napoleon's often quoted remark about how the world would be amazed when China woke up is, in fact, historically inaccurate – in his time, China already accounted for an estimated one-third of global wealth. But I would argue that, two centuries later, the global impact of the world's most heavily populated nation and the establishment of increasingly substantial relations with the rest of the planet constitutes the most important international development since the end of the Cold War.

I would also suggest that, in retrospect in a few years' time, the last three decades in which China's annual growth has come to average around 10 per cent and hundreds of millions of rural residents have been brought into the global labour force, will turn out to be only the preface for even greater change which will throw up challenges of a kind not experienced since 1980.

To begin with, as the nation which may have most benefitted from globalization, China now faces the problem that a decline in its main export markets, in Europe and the United States, will impact its economy at a time when domestic consumption has still not advanced sufficiently to compensate. The

[1] It is obvious that the points and statements made by the speaker and the discussants do only reflect their personal views and do not engage anybody else.

rebalancing toward consumption and away from capital formation and exports is underway, spurred by large increases in the minimum wage and the development of a national health service that will reduce the need for precautionary saving by households, but this is still work in progress.

China is so large and still has much ground to make up in vital areas with the result that it will take time for this fundamental economic change to take full effect. The impact on domestic progress of economic trouble elsewhere can be over-stated, but still cannot be ignored which is why policy-makers in Beijing are so insistent that Europe and the United States must put their own houses in order rather than looking to a bail-out from the People's Republic. There are threats of trade measures against China in Washington which would be particularly dangerous at such a time of global uncertainty. Small and medium-sized exporters in China are under pressure from wage costs, high interest rates and slow payment by foreign purchasers. The government is involved in a continuous attempt to get control of the excess liquidity which flowed from the credit loosening of 2009 launched to alleviate the threatened downturn without tightening too far and driving small companies out of business.

Such challenges are inherent in the growth pattern and will throw up continual reports of difficulties. But, short of a fully-fledged recession, I believe that growth will remain strong in the range of 8-9 per cent range. This is important for the political leadership as the composition of the Politburo, the supreme Communist Party decision-making body, changes next autumn followed by the formation of a new government and appointment of a new State President in early 2013.

The leadership transition has been well prepared and we believe that we know the future leaders who will steer China through to 2022. They will gave formidable challenges in ensuring not only continuing growth but also the transformation of the economy to boost domestic consumption, develop services and, vitally, to move industry away from low cost manufacturing towards more sophisticated technologically advanced products with higher value added to move the People's Republic closer to the developed nations of the West and Japan.

It is easy to focus uniquely on the economy where China is concerned. But economic growth has produced enormous social change, the expansion of cities in what had always been a predominantly rural nation and growing involvement of the People's Republic in international affairs. Tens of millions of Chinese now travel abroad each year. Society has been revolutionised in many ways and this will continue. Yet major areas have not been fully addressed - some of which have political and social significance. Though China has become the world's second largest economy, it still contains many relatively poor people and remains a country seeking, in the words of its present leader, Hu Jintao, the route to moderate prosperity. It confronts the world with a series of unprecedented issues which underlie the international relations that are the main concern of the Egmont Institute. To take a few:

Never before has a country still in the stage of development competed so strongly with far richer nations and become a global provider on such a scale with a treasure chest of foreign exchange that could buy the whole of Italy or all the sovereign debt of Portugal, Ireland, Greece and Spain (as of 2011), plus Google, Apple, IBM and Microsoft plus all the real estate in Manhattan and Washington, DC, plus the world's fifty most valuable sports franchises.

Never before has a country had such a mismatch between the size of its population (21 per cent of the world's total) and its relative lack of natural resources (seven per cent of global arable land and renewable water but still has such an impact on global commodity prices and shipping rates.

Never before has the world's superpower been so dependent on funding and cheap imports from a state whose population means that its per capita wealth is equivalent to that of Angola raising major geo-political questions - 'How do you get tough on your banker?' as US Secretary of State Hillary Clinton summed up Washington's dilemma. Yet, on the other side of the Pacific, the PRC finds itself stuck with a huge stockpile of dollar-denominated securities it would prefer to be without but cannot dispose of.

Never before has a nation come back from such a long history of revolts, invasions, repression and natural disasters to awe the world. Never before has China been so involved with the rest of the world with a permanent seat on the UN Security Council

Never before has a country whose ruling party aims to apply ‘socialism with Chinese characteristics’ and to follow the path of ‘scientific socialism’ pursued such a red-blooded approach to market competition and economic growth.

China’s growth during the 30 years we mark today has been astounding. How it will develop in the next decade – not to look further into the future – may be the single most important long-term global question with significant impact on such worldwide issues as climate change and energy supply. There are no easy answers. Those who forecast that China will inevitably rule the world are simply doing a straight line extension from the past decade into the further future without taking account of the challenges ahead. Those who predict a China collapse are wrong, too., The process started in the 1980s will not stop even if its rate of expansion may slow down, a development which, as it happens, the authorities in Beijing might welcome as they confront what the Prime Minister has described as an unbalanced and unsustainable rate of growth.

China is not going to rule the world or implode. Its value system will continue to differ from that in the West in important respects. It will insist on running its own affairs without foreign interference. There will be political and economic tensions.

But China’s size and the scale of its global impact mean that even small tremors in the People’s Republic will have wide repercussions. China has woken and is amazing the world. But its continuing progress will throw up many tests that have to be dealt with in the first place by the authorities in Beijing but, it must be hoped, in an increasingly internationalised context. China and its foreign partners have to find ways of moving ahead together, reconciling interests which may sometimes diverge, and forging new political and economic relationships. Thirty years on, we are still, in many ways, only at the start.

Jonathan Fenby

**Discussion, Q&A session[i]**

- **Mr. CHEN Fei, General Manager - Belgium, IBCB**
  **Industrial Bank and Commercial Bank of China**

Belgian-Chinese commercial relations are influenced by a set of evolutions. On the one hand, our commercial relations are influenced by major developments in China and Europe. On the other hand, evolutions in the direct relations between Belgium and China also play an important role. Both types of evolutions offer opportunities for more intense commercial relations.

In China, the general strong economic growth is having a number of consequences. It causes the country to look at how to make the best use of the resources at its disposal. For this reason, China is moving beyond its more traditional role as a producer of basic industrial goods. The country starts to invest in more advanced manufacturing products, as well as logistics and services. Not only is the Chinese industrial production changing, production is also spreading to a wider range of regions. This changing face of Chinese production offers several opportunities to Belgian investors.

The types of Chinese firms that participate in international trade can also change in the future. Currently, there is a wide-spread believe in China that state-owned firms are safer and more reliable than privately owned-firms. It is probable that this way of thinking will change in the future, as people notice that private companies can also be reliable partners.

Besides these evolutions in China, the financial and sovereign debt crisis in Europe also influences the commercial relations between Belgium and China. The current eurozone debt crisis should not only been seen in terms of risk. In fact, the Chinese word for crisis is composed of two characters. One signals risk, while the other character indicates opportunities. Indeed, the crisis in Europe can also create a number of opportunities. China can help to tackle the eurozone debt crisis, by providing liquidity, jobs and confidence.

In terms of bilateral relations, Belgian-Chinese commercial relations are already strong. Chocolates and steel are major Belgian export products in China and the country is increasingly importing Belgian diamonds. Chinese investors are also active in Belgium, as is the case for the Chinese participation in Delvaux and the Volvo factory in Ghent. While commercial relations are already strong, they can still be improved by increased mutual understanding.

Increased knowledge of China would increase Belgian exporters' success in the country. Belgians should be better aware of the fact that some Belgian products are well-known in China, ranging from chocolates to fictional characters as Tintin and The Smurfs. Furthermore, Belgian investors should pay more attention to the Chinese commercial mentality. Often, people in China tend to be more interested in what they can do for you, instead of what you have to offer them. Doing business in China requires taking this mindset into account.

Conversely, the Chinese perception of doing business in Belgium can also be improved. Chinese investors often believe that human resources and taxes present high costs in Belgium. Yet, they are insufficiently aware of the many exemptions and tax deductions that are available. Belgium should display these advantages more.

By expanding the commercial relations between the two countries, additional opportunities can be exploited. If Chinese entrepreneurs are better informed on compliance issues, they will be willing to invest more in Belgium. Conversely, Belgium could become more active in China. For instance in the field of information sharing, the business opportunities are plentiful. Both Belgium and China would benefit if entrepreneurs were to take advantage of these opportunities.

- **Mr. Peter VANDEN HOUTE, chief economist at ING**

When I started to work in the bank as an economist at the end of the eighties, people looked at the world from a very different perspective. The US, Japan and a few European countries dominated the discussions. Now, China plays a much more prominent role in our analysis. The same phenomenon can be seen on the financial markets. 25 years ago, a strange and sudden movement in asset prices was attributed to the Saudis. Nowadays, newspapers often believe that China is behind such movements.

It is of course more than obvious that China played an important role in the international economy over the last decade. I even argue that China has indirectly been at the origin of the subprime crisis. We saw a very strong growth of international trade with China after the country's accession to the World Trade Organisation. This was one of the elements that kept inflation low in Western economies. Because of low inflation, central banks kept their monetary policy loose. On top of that, bond yields in Western economies remained extremely low, partly because of the Chinese investments in these bonds.

Both the loose monetary policy and the low bond yields led to a regime of low interest rates in Western economies. This in turn created real estate bubbles. If we combine this with a lack of regulation and some financial engineering, we have the origins of the subprime crisis in the US. The rest is history, but unfortunately a history that we are still living today with the debt crisis in Europe. All of this is of course not China's fault, but the WTO accession of China certainly contributed to the conditions that led to the crisis.

Whereas China had a deflationary impact on world prices up to 2006, the opposite was true thereafter. China has become an important source of demand for world commodities, ranging for copper and other base metals to various energy sources. In fact, China overtook the US as the world's biggest energy consumer in 2010. All of this means that inflation in the Western economies now strongly depends on what is happening in China. A slowdown in the West no longer pushes commodity prices down, as was the case in the past, if it is not accompanied by a deceleration in China.

What will be the influence of China over the coming years? Let's hope that China will become a source of growth for the West. The country certainly has the potential to do so. China is also able to have a very strong influence on the rest of the world as an investor. China has been buying public bonds, both in the US and the EU (including its peripheral countries). I think China will gradually shift from a bond investor to an equity investor, an evolution that is already taking place. It is the best proof that China is now fully part of the global economy.

To conclude, if someone were to ask me which event has changed the world economy most over the last decade, my answer would not be 9/11. Actually, it happened two months later, in November 2001 with the signing in Doha of the accession of China to the World Trade Organisation.

- **Question and answer session**

A number of interlinked topics were discussed during the question and answer session. This report focuses on some of these topics.

First of all, the **international role of the Chinese currency**, the Renminbi, was considered. A participant asked the panellists whether the fact that Chinese exports can now be expressed in Renminbi will have a substantial impact on the international role of the currency. In response, Mr. Chen stated that more and more companies like to use the Renminbi in trading as it avoids foreign exchange risk. However, the currency is still not fully convertible and it will take some time before the Chinese government will change this policy. Nonetheless, Mr. Chen believed that the currency will become fully convertible in the future. Mr. Fenby added that the Renminbi will most likely only play an important international role when it is less tightly controlled by China. Mr. Vanden Houte told the participants that China would need a more developed financial market in order for the Renminbi to become an international reserve currency. For this reason, it will take some time before the Chinese currency will be able to compete with the euro and the US dollar.

Another issue raised during the Q&A was the **alleged undervaluation of the Renminbi**. Mr. Vanden Houte stated that China would be reluctant to let its currency float more freely, as that could lead to wide swings in the currency's value. Mr. Fenby did not expect a major appreciation of the Chinese currency, as domestic factors require strong economic growth in China. He believed that the Renminbi would only appreciate 5% compared to the US dollar in the coming year. Real market exchange rates will have to wait for some years, he added.

The **Chinese trade surplus** was another topic that was discussed during the session. A participant wondered whether balancing world trade should be left to the markets, or whether public authorities need to contribute to more balanced world trade. Mr. Chen explained that China will need to continue to increase its exports in order for it to finance its internal investments. Mr. Fenby believed that China will not give up its trade surplus easily. Instead, it will try to become less dependent on the US dollar and will increasingly use its surpluses to invest in economies worldwide. Over time, China will turn more towards internally generated growth, which can reduce its trade surplus. However, this is a long-term project. Mr. Vanden Houte explained that it is most difficult to have an international agreement on counterbalancing trade surpluses and deficits. Even in the eurozone, policymakers have a hard time finding a solution. He thus questioned whether it would be possible to have an international agreement on the matter.

Finally, a participant asked the panellists whether they saw a risk of increased **protectionism** in international commercial relations with China. Mr. Fenby stated that up until now, there had been relatively little protectionist measures. However, pressure for more protectionism is mounting in the US and some Southern European countries. It is thus not excluded that we will see more protectionism in the future. Mr. Vanden Houte added that we need to keep in mind that not everyone benefits from free trade in the same way. Some will only benefit from globalisation in the long run. In the short term, globalisation can have a negative effect on some people's income. For this reason, more protectionism could occur in the future. Besides, he stated, countries are likely to put more emphasis on the security of supply, for example in the case of energy.

---

[i] It is obvious that the points and statements made by the speaker and the discussants do only reflect their personal views and do not engage anybody else.