

## **THE DRAGON AND THE TIGER REVISITED**

One could argue that the most important relationship for the US in the next twenty years or so will be that between the US and China. In the next twenty years, China is likely to continue to develop as a world power – possibly to match the global superpower status of the US. However, in the era of globalisation, the one depends upon the other. The US will need China as a producer nation, and China will need the US as a customer nation. We must not presume that this interdependence is symmetrical. That the US and China will continue to need each other is not to argue that each will be as important to the other.

With the focus of the world economy moving towards Asia, it is only natural that the interest of the US will move in that direction. As China is in Asia already, where will be the Chinese focus? At present, we could argue that the focus of China is to the east – to Japan and to the US. In recent years, Japan has been the largest source of FDI into China and the US has been the largest consumer of Chinese manufactured goods.

This may start to change as early as the end of the current decade. China is rapidly becoming one of the largest creditor nations in the world. To date, much of Chinese savings have been channelled into US T-Bonds. The Chinese authorities are starting to diversify their future acquisitions into other currencies (such as the Yen and the Euro) and other asset classes (such as sovereign nation funds). In finance, what goes around also comes around. With the diversification of its holdings, the reliance of China on FDI to fund growth is likely to be diminished somewhat.

The indications are that, as a Chinese middle class develops, they will also start to acquire the consumption tastes of the more developed nations. If this trend continues, then there will be a point in the near future when the focus of Chinese manufacturers will shift away from exporting to overseas markets and towards satisfying the huge domestic market within China. If that were to happen to any significant degree, then it would help to diminish the importance of the US as a trading partner.

If these two contentions are correct – that Japan lessens in importance as a source of FDI to China, and if the US diminishes in importance as a trading partner to China – then, we might ask, to where will the focus of China move?

We feel that the focus of China will move to the West – to the ‘Stans’ as a source of oil and natural gas and to India as a trading partner. Within twenty years, we feel that the most important relationship to China will be that between China and India.

The development of China and India provides an interesting parallel. Looking further into the future, say, to 2050, it is often argued that India will have the developmental edge over China because India is a functioning democracy and China isn’t. Leaving aside the possibility of China becoming a functional democracy by 2050 (a heroic assumption), does the long term advantage rest with India? To ask this more generally, do democracies develop better than autocracies?

The evidence is mixed, to say the least. It is true to say that, historically, there has been a link between democracy and development. However, the causality is not readily seen. Do nations develop because they are democracies? Or do nations become democracies because they have developed? In Europe, development came before democracy. In the US, democracy came before development.

The post-war experience of decolonisation provides a mixed picture. We could argue that India provides a model of how a large nation can establish a pluralistic, multi-cultural democracy. And yet, to date, India has not quite lived up to its development potential. China provides a model of how a large nation can develop economically. However, it would stretch matters to a point to argue that China has a functioning democracy.

If we take India and China as two polar extremes, then we have a standard by which other nations can be assessed. The evidence suggests that autocracies have an edge over democracies when it comes to development. The causality in the model is quite simple. As prosperity increases due to development, the democratic process is called into action in order to share the increase in prosperity more widely. In turn, this slows the process of development as funds that otherwise would have been earmarked for investment are instead used for wealth redistribution.

There are a number of examples of this process in action. The Indian government, emulating the Chinese government, have attempted to establish special economic zones. This process has been inhibited greatly by protests – both legal and extra-legal challenges – to the detriment of the policy. In India, as the actions of government are subject to democratic review, policy-makers do not have the same freedom for action as the policy-makers in China. Local interests are not so easily swept aside for developmental projects as they are in China. In this case, the functioning of the democratic process is helping to limit the potential for further development.

An interesting conundrum for the future emerges. If the model is correct, then, as nations develop into the future, so we would expect the pressure for democratic reform to grow as well. If it doesn't, then we ought to seriously question the linkage between democracy and development. If it does, then the process of development might start to stall.

In the context of China, if the Communist Party maintains its control over the polity, then we might expect China to pull ahead of India in developmental terms, and stay there. This is not necessarily a bad thing for India. Whilst China may pull ahead economically, it will also have more of the consequential costs of development (environmental degradation, pollution, income disparities). To stylise the position, China might be a richer nation, but India will be a nicer place to live.

Strangely enough, we have seen this argument before. A number of commentators have stylised the relationship between Europe and the US in this way. For example, Jeremy Rifkin, in his book 'The European Dream', suggests that the Europeans have consciously chosen to have a poorer existence in material terms in return for a richer existence in terms of lifestyle. There are many who would echo this view.

Placing this argument into an Asian context in the near future, could China play to the US whilst India plays to Europe? There are, after all, those who see India as a candidate nation for joining the EU by about 2050. Additionally, by 2050, will we see the development of a 'special relationship' between India and China, as is now claimed by Europe in relation to the US? We cannot be sure about what the future will hold for us. However, we can be reasonably certain that the seismic changes currently taking place in geopolitics will ensure that the past is very unlikely to reflect the future.

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