China's Global Economic Leadership: Who are the Followers?

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ABSTRACT: In order to provide global economic leadership, China must have followers. Why are the leaders of some nations more interested in China's global leadership than others? We argue that the pull of economic benefits is only part of the story – foreign leaders are also being *pushed* closer to China by unresolved grievances with the current U.S.-led international economic order. Grievances about global financial instability are particularly important push factors. But grievances about IMF conditionality, global governance, and discriminatory U.S. trade policy also play a role. If the United States and other supporters of the current global economic order want to increase the appeal of the U.S.-led world order, they should take steps to address these grievances.

1. Introduction

In January 2017, as Donald Trump was about to assume the presidency and declare that he would put "America First," China's President Xi Jinping was defending economic globalization at the World Economic Forum in Davos and indicating that China was ready to assume the mantle of global economic leadership.

Leadership, by definition, requires followers. But who is following China and why? While the conventional wisdom emphasizes China's own efforts to attract followers with economic benefits, this perspective ignores the possibility that foreign interest in China's global leadership might also stem from *dissatisfaction* with the current international economic order led by the United States.

To build a more complete theory of global leadership transition, we consider both forces in this paper: on one hand, a new potential leader like China can offer benefits to pull in followers; at the same time, dissatisfaction with the current order and its leadership can have the effect of *pushing* countries toward the new leader.

Since the common wisdom is about pulling, we focus on the *push* factors. We argue that grievances about the current U.S.-led international economic order fall into four categories:

1. **Grievances about international financial instability**. Financial instability has plagued the current global order since the United States and the IMF began insisting that nations remove their controls and regulations on short-term capital flows. We present evidence that leaders from nations that have experienced more financial volatility under the current order are more likely to follow China's global leadership.

2. **Grievances about IMF conditionality.** Nations harbor resentment about IMF interventions because the IMF imposes politically-sensitive policy conditions before it disburses its loans. We show that countries that experienced more domestic social unrest while under IMF programs are more likely to follow China's global economic leadership.

3. **Grievances about global governance.** The governance of the IMF and the World Bank have generated another grievance with the current international order. The multilaterals wield enormous power and influence in the world economy but leaders of emerging market economies and developing countries feel that they have too little voice within them. We examine whether leaders

of nations that are underrepresented at the IMF are more likely to support China’s global leadership

4. **Grievances about discriminatory U.S. trade policy.** While the rules-based multilateral trading regime has been a boon for globalization, the United States generates resentment when it violates the very same WTO rules that it helped to establish. We show that nations that have lodged more complaints against the U.S. at the WTO are more likely to show interest in China’s global economic leadership.

In order to evaluate these claims, we devise a measure of *foreign support for China’s global economic leadership*. Our measure is based on leader participation in the “Belt and Road Forum for International Cooperation,” which President Xi announced at the 2017 World Economic Forum. The goal of the summit, held in Beijing on 14-15 May 2017, was to “discuss ways to boost cooperation, build cooperation platforms and share cooperation outcomes.” All nations were invited. The heads of state and government (hereafter, “heads of state”) of 29 nations participated and another 56 nations sent cabinet ministers. Six nations – including the United States and several close allies – chose to dispatch lower level officials.

Since the summit was organized by President Xi to validate China’s role in fostering global economic cooperation, we leverage participation as a proxy for *foreign support for China’s global leadership*. We assume that head of state attendance sent a stronger signal of support for China than cabinet minister participation, and that non-attendance, or attendance by a low-level official, indicated ambivalence or opposition to China’s global leadership. **Table 1** lists the rank of participants, by country.

While this is not the only metric for whether a nation is following China’s leadership, it has advantages. First, the Belt and Road Forum was China’s first high-level diplomatic summit to focus on global economic cooperation since the U.S. began turning inward under President Trump. Although the aim of the summit was to form a consensus on a basic framework for global economic cooperation, it can be used to judge the level of foreign support for China’s global economic leadership. Second, the “Belt and Road” aspect of the summit meant that attendees understood

Table 1: Participants at the Belt and Road Forum, 14-15 May 2017

Country	*Participant*	*Country*	*Participant*	*Country*	*Participant*
Argentina	Head of state	Belgium	Minister	Syria	Minister
Belarus	Head of state	Bosnia Herzegovina	Minister	Thailand	Minister
Cambodia	Head of state	Brazil	Minister	Timor-Leste	Minister
Chile	Head of state	Brunei Darussalam	Minister	Tonga	Minister
Czech Republic	Head of state	Cyprus	Minister	Trinidad Tobago	Minister
Ethiopia	Head of state	Korea DPR	Minister	Tunisia	Minister
Fiji	Head of state	Denmark	Minister	Ukraine	Minister
Greece	Head of state	Egypt	Minister	UAE	Minister
Hungary	Head of state	Eritrea	Minister	United Kingdom	Minister
Indonesia	Head of state	Finland	Minister	Uruguay	Minister
Italy	Head of state	France	Minister	Vanuatu	Minister
Kazakhstan	Head of state	Georgia	Minister	Venezuela	Minister
Kenya	Head of state	Germany	Minister	Yemen	Minister
Kyrgyzstan	Head of state	Iran	Minister	Canada	Lower Official
Laos	Head of state	Iraq	Minister	Japan	Lower Official
Malaysia	Head of state	Israel	Minister	Mexico	Lower Official
Mongolia	Head of state	Jordan	Minister	Morocco	Lower Official
Myanmar	Head of state	Kuwait	Minister	South Korea	Lower Official
Pakistan	Head of state	Lebanon	Minister	United States	Lower Official
Philippines	Head of state	Madagascar	Minister		
Poland	Head of state	Maldives	Minister		
Russian Federation	Head of state	Mauritius	Minister		
Serbia	Head of state	Mozambique	Minister		
Spain	Head of state	Nepal	Minister		
Sri Lanka	Head of state	New Zealand	Minister		
Switzerland	Head of state	Peru	Minister		
Turkey	Head of state	Portugal	Minister		
Uzbekistan	Head of state	Qatar	Minister		
Viet Nam	Head of state	Moldova	Minister		
Afghanistan	Minister	Romania	Minister		
Albania	Minister	Samoa	Minister		
Armenia	Minister	Saudi Arabia	Minister		
Australia	Minister	Singapore	Minister		
Azerbaijan	Minister	Slovakia	Minister		
Bahrain	Minister	Slovenia	Minister		
Bangladesh	Minister	Sweden	Minister		

they were participating in a uniquely Chinese version of global leadership. Unlike the Asian Infrastructure Investment Bank (AIIB), which is modeled on existing multilateral institutions, the Belt and Road project is unconnected to the current world order and inspired by China's ancient land and sea trade routes. It is also a bilateral project, which is important because multilateral governance allows foreign nations to have influence over the AIIB, which can obscure motivations for participating. For example, some nations may be participating in the AIIB, not because they support China's global leadership, but because they want a "seat at the table" in order to sway decisions toward their own global objectives.

Third, participating heads of state signed a consensus document on global economic cooperation at the close of the summit that outlines a framework for cooperation centered on China: *The Joint Communiqué of the Leaders Roundtable of the Belt and Road Forum for International Cooperation*. The communiqué motivates the need for cooperation by listing major economic problems in the current world order, such as "eradicating poverty, creating jobs, addressing the consequences of international financial crises, promoting sustainable development, and advancing market-based industrial transformation and economic diversification." It reaffirms participants' shared commitment to "build an open economy, ensure free and inclusive trade, and oppose all forms of protectionism." It also pledges signatories "to promote a universal, rules-based, open, non-discriminatory and equitable multilateral trading system with WTO at its core." Since President Xi was first among equals at the summit, and since China played the largest role in crafting the joint communiqué, we infer that the heads of state that put their imprimaturs on the document support China's global leadership.

With this measure, it is possible to assess both the push and the pull factors that motivate nations to follow China. Our theory of leadership transition pays particular attention to followers' grievances with the current order, but we also consider the economic benefits that China, the erstwhile leader, is offering. In the next section, we flesh out these push and pull factors and then present a preliminary analysis, using participation in the Belt and Road Forum as a proxy for *support for China's global leadership.*

2. Grievances that push nations closer to China

a. International Financial Instability

The current order has generated grievances about international financial instability, IMF conditionality, global governance, and discriminatory U.S. trade policy. Arguably, grievances about financial instability are the most salient.

Financial instability imparted by large and volatile short-term capital flows has been the most problematic area of the current global order. Since the 1980s, the U.S. Treasury Department and the IMF have pressured nations to liberalize their capital accounts by removing restrictions on short-term capital movements. But the policy has been a disaster for many nations as it led to boom-and-bust cycles and financial crashes. The financial crises that rolled through Latin America, East Asia, and Europe were devastating events that brought sharp political costs to incumbent politicians and governing coalitions. Governments were voted out of office, parliaments became more polarized, and policymaking was gridlocked for years to come.

The high domestic political costs of financial crises gives leaders a personal incentive to be dissatisfied with the current international order. China's brand of leadership may be attractive in this respect because regulating short-term capital flows has been a hallmark of China's policy. Observers credit the policy for insulating China from global financial crises. In addition, China's restrictive capital account policies help its planners maintain exchange rate stability and monetary policy autonomy, in line with the constraints of the open-economy "Trilemma." China is distinct from the United States in giving priority to exchange-rate stability and monetary policy autonomy over capital account openness, which might makes its leadership appealing to followers that have suffered from destabilizing financial flows under the current order.

China reinforces the argument that it has a better financial model to offer its followers. In his 2017 speech at Davos, Xi Jinping said that the 2008 global financial crisis was "not an inevitable outcome of economic globalization; rather, it is the consequence of excessive chase of profit by financial capital and grave failure of financial regulation." Experts like John Williamson also think that the 2008 crisis helped fortify the "Beijing Consensus" at the expense of the "Washington Consensus."

A related financial grievance is that U.S. monetary policies reverberate around the world, generating a "global financial cycle." The *Taper Tantrum* in 2013 illustrated the point as mere anticipation that the Federal Reserve was about to start unwinding its quantitative easing programs caused large capital outflows and asset price volatility in emerging markets. Emerging markets in particular are affected by the global financial cycle. They experience large capital inflows when U.S. interest rates are low and investors search for yield, and sharp capital outflows when U.S interest rate rise, as investors reduce their appetite for risk and sell off their emerging market assets. The consequence is that monetary policymakers in emerging markets are forced to mirror the policies of the Federal Reserve, regardless of their exchange-rate regime.

We proxy for financial grievances with two alternative measures of financial instability. The first is a nation's history of financial crises since 1990. Our expectation is that the leaders of countries that have suffered more financial crises will be more likely to follow China's global leadership. We also gather data on the variability of capital account policy restrictions imposed by the government. This measure captures the actual variability of capital control *policy* and directly reveals problems nations have had with global finance.

Figure 1 presents the relationship between financial crises and our proxy for support for China's global economic leadership. The crisis data are from Reinhart and Rogoff and cover banking crises, currency crises, and sovereign debt crises. We group nations by their participation status at the Belt and Road Forum and present the average number major financial crises between 1990 and 2016 for these groups. The figure supports our claim that nations with more financial problems under the current global order are more likely to support China's global economic leadership. Nations sending their top leaders to the Forum experienced about twice as many financial crises on average as nations that sent cabinet ministers, lower-level officials, or did not participate.

Figure 2 replicates this analysis with our policy-based measure of financial instability: the variability of capital account policy. Nations are grouped by their participation status at the Belt and Road Forum, where the degree of capital account policy volatility is measured as the standard deviation of the Chinn-Ito Index of capital account openness between 1990 and 2015. This evidence supports the argument that leaders of nations that have had a more financial trouble under the current regime are more interested in China's model of global economic leadership. Nations that sent heads of state to the summit had the most trouble maintaining a stable capital account policy.

Figure 1: Average Number of Major Financial Crises since 1990 and Leader Attendance at the Belt and Road Forum

(Reinhart and Rogoff data)

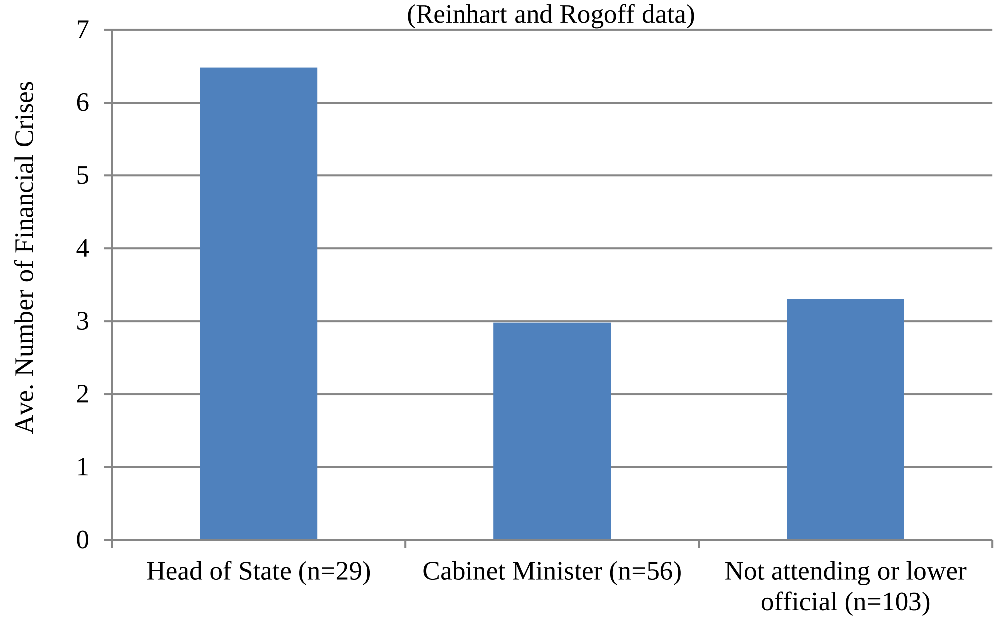
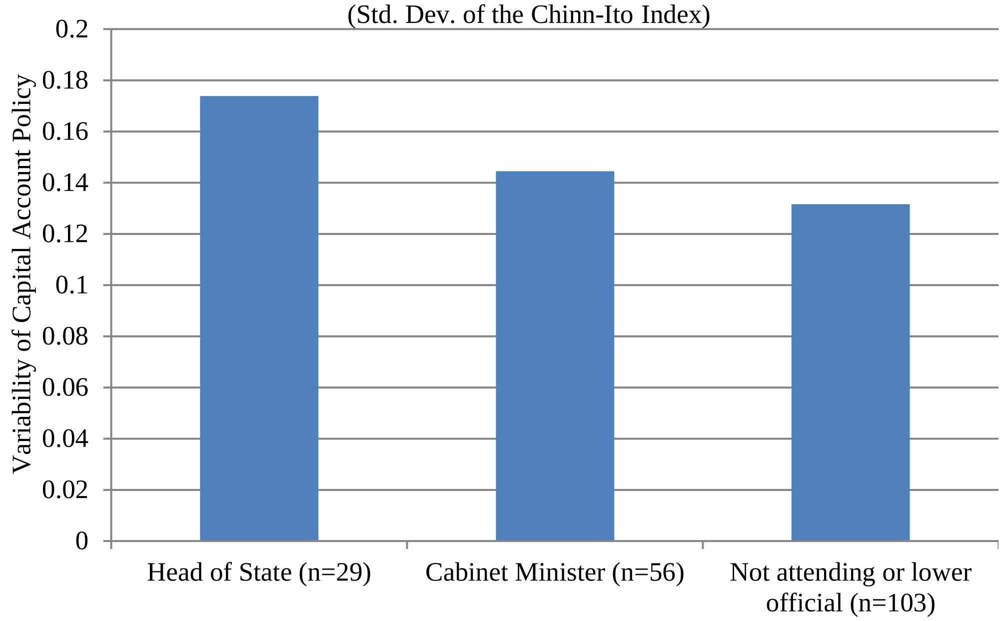


Figure 2: Variability of Capital Account Policy since 1990 and Leader Attendance at the Belt and Road Forum

(Std. Dev. of the Chinn-Ito Index)



The global financial system is the weakest part of the current global order, generating major crises on a regular basis. When a crisis looms, nations often have to turn to the IMF for support, which can generate another type of grievance.

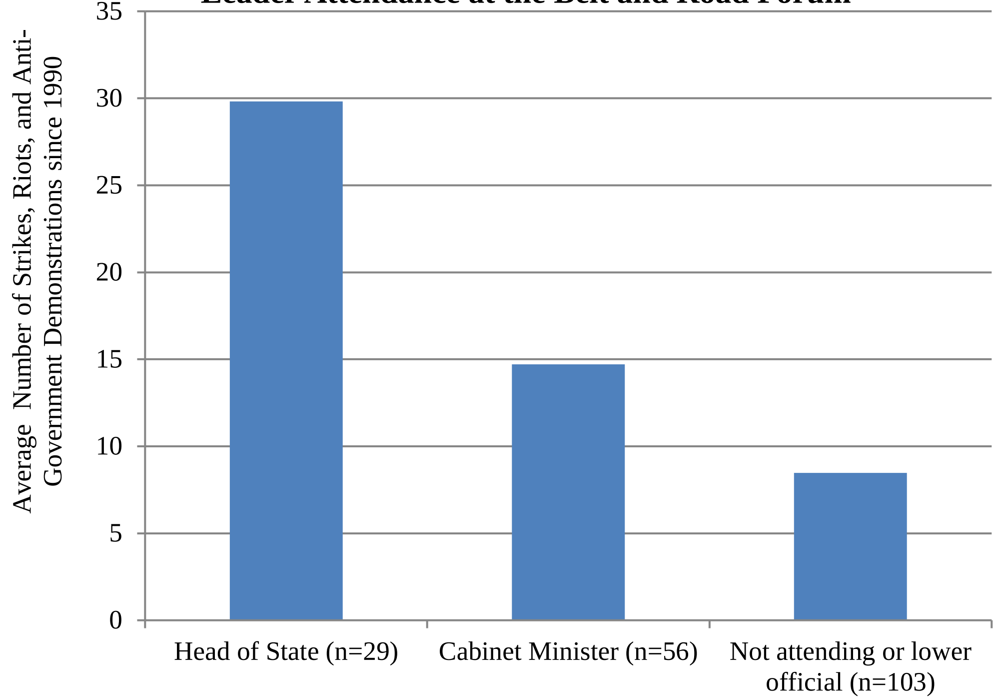
b. Grievances about IMF conditionality

Nations also harbor resentment about IMF interventions that follow the onset of a financial crisis. When a crisis prevents a nation from borrowing to fund its external deficits, the IMF stands ready to provide emergency loans. However, the IMF imposes policy conditions before it disburses its loans and this conditionality has been a source of conflict with borrowers. This conflict arises because IMF conditions often require cuts in politically-sensitive social programs. Since we are interested in why leaders follow China, we examine whether the level of domestic social unrest that occurs during IMF interventions is associated with more interest in following China.

We measure the level of domestic social unrest that occurs under IMF programs. Our measure of social unrest comes from Cross-National Time-Series Data Archive and includes labor union strikes, government crises, anti-government demonstrations, and riots. We count all such social disturbances that occurred in countries while they were in an IMF program between 1990 and 2017. **Figure 3** presents averages of social instability for each type of participant at the Belt and Road Forum. Nations that sent their heads of state to the cooperation summit suffered about 30 strikes, government crises, demonstrations, or riots on average between 1990 and 2017 while nations that sent lower-level officials, or no one at all, suffered about 8 of these events over the period. This supports the claim that grievances about IMF interventions motivate interest in China's leadership.

Inasmuch as China stresses self-determination as one of its core foreign policy values, its followers may be anticipating fewer politically-destabilizing interventions under China's leadership than under the current regime. However, China and the IMF appear to be moving toward a collaboration in which the IMF will play a supervisory role to ensure the fiscal sustainability of Belt and Road projects, as discussed at the April 2018 *Joint People's Bank of China - International Monetary Fund High-level Conference on the Belt and Road Initiative*.

Figure 3: Social Unrest during IMF Programs since 1990 and Leader Attendance at the Belt and Road Forum



c. Grievances about global governance.

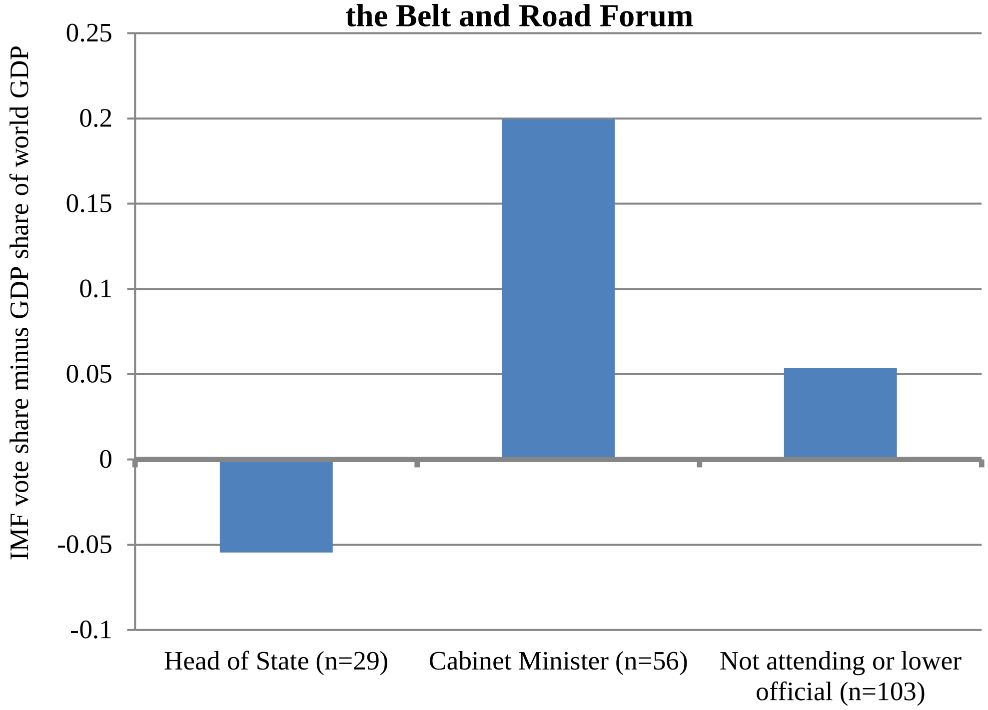
The governance of the IMF (and the World Bank) causes controversy because emerging market economies feel they are not fairly represented. In principal, each country's vote share at the IMF is supposed to reflect the relative size of its economy, based on formulas that weigh various measures of output and trade. But these formulas have not been accurately employed and deviations, reflecting political considerations, are common. Emerging market nations complain that they remain underrepresented despite their growing shares of the world economic output.

The IMF finally passed a governance reform in 2010 but the reform was delayed for five years because the U.S. Congress refused to ratify it. This added fuel to the grievance. Our expectation is that leaders of nations with vote shares in the IMF that are lower than their economies' shares of the global economy will be more likely to show interest in China's leadership. In other words, we think governance grievances are about the highly political process that prevents emerging market and developing nations from having a level of influence commensurate with their global economic position.

We measure IMF governance deficits by subtracting a nation's share of votes at the IMF from its GDP share of total world GDP. Negative values indicate that the country is underrepresented at the IMF. We take values in 2015, before the 2010 IMF governance reform went into effect, because we think the five-year delay caused by the U.S. Congress caused lingering resentment that was still present at the time of the Belt and Road Forum.

Figure 4 indicates that the 29 heads of state that attended the summit came from nations that are, on average, underrepresented at the IMF. However, the average size of their governance deficit is small. Their vote shares are about one-half of one percent smaller than they should be on average.

Figure 4: IMF Governance Deficits and Leader Attendance at the Belt and Road Forum



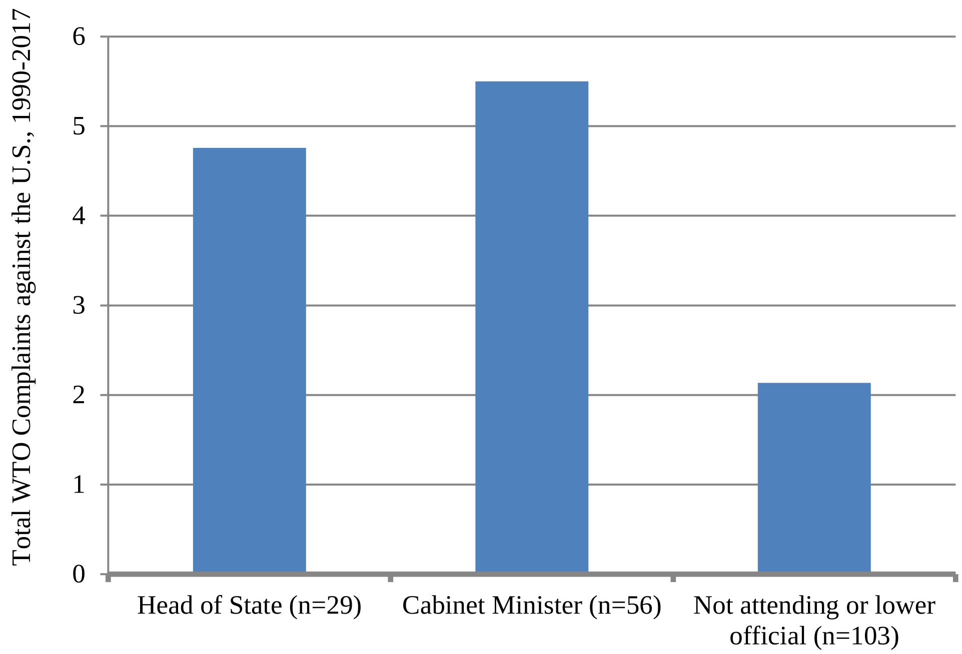
d. Grievances about discriminatory U.S. trade policy

There is also dissatisfaction with the United States for making anti-dumping and countervailing duty (AD/CVD) barriers its preferred policy tool for restricting imports. AD/CVD are classified as "escape clause" exceptions to the WTO principle of non-discrimination, but the U.S. has abused this loophole more than another other nation. Since the 1990s, the U.S. has been the largest user of AD/CVD, imposing duties on thousands of companies, on hundreds of separate products, and on more than 50 different WTO members. As a result, the U.S. is the most frequent target of WTO complaints involving AD/CVD, accounting for 39 percent of all such cases.

We argue that this resentment has pushed some nations into closer relations with China, especially since China is a strong supporter of the rules-based WTO system. We expect that foreign nations that have lodged more complaints against the U.S. at the WTO are more likely to follow China's global leadership.

Figure 5 provides support for this argument. It shows that nations that sent heads of state or cabinet ministers to the Belt and Road Forum lodged over twice as many complaints against the U.S. at the WTO between 1990 and 2017 than countries that did not participate in the summit or sent lower-level officials. These averages suggest that the nations that are following China have had more trouble with discriminatory U.S. trade policy.

Figure 5: WTO Complaints against the U.S. and Leader Attendance at the Belt and Road Forum



3. Economic benefits that pull followers to China

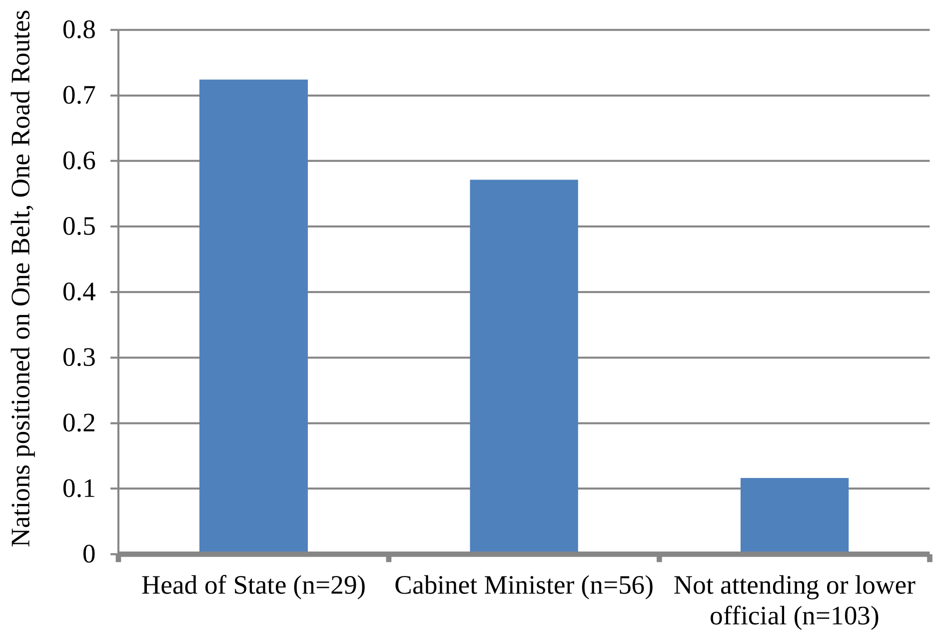
In this section, we briefly consider the economic benefits that China is offering its followers – the pull factors. We focus on access to Chinese infrastructure investment and trade.

China has focused on financing infrastructure projects in its global initiatives, providing obvious benefits to followers. In fact, the foreign demand for China's infrastructure projects has been so high that there is growing concern that partner nations are taking on too much debt and verge on "debt dependence."

Clearly, China's infrastructure projects are attractive to potential followers. We measure this attraction by identifying the countries that lie geographically along the "One Belt, One Road" routes that China is using to motivate the revival of its ancient trade linkages. Since a map of these routes identifies where China is planning to focus its infrastructure investments, we use it to proxy for the attraction of this benefit.

Figure 6 provides evidence that infrastructure investment is related to foreign support for China's leadership. The figure shows that 72 percent of the countries that sent heads of state to the summit are spatially located adjacent to the planned One Belt, One Road routes. By contrast, only 11 percent of the countries that did not participate in the summit (or sent lower officials) are positioned along these trade routes. Since the revival of these routes will require massive infrastructure investment, we take this as evidence this benefit is pulling followers to China

Figure 6: "One Belt, One Road" Position and Leader Attendance at the Belt and Road Forum

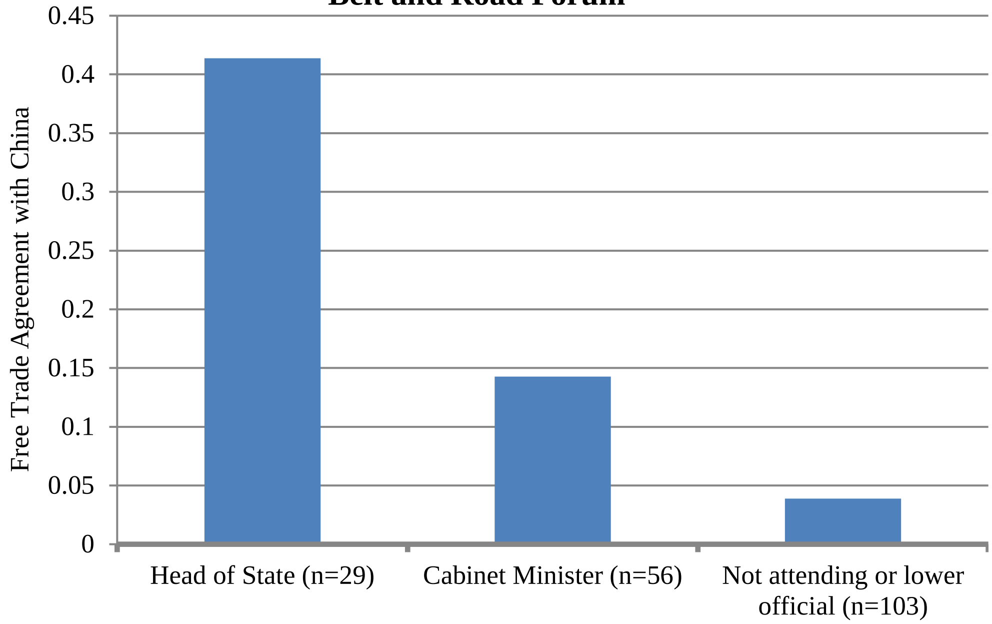


China is a trading powerhouse and the attraction of trade linkages with China is another benefit that pulls in followers. We measure this benefit by way of the existence of a free trade agreement (FTA) with China. A FTA with China demonstrates eagerness to enhance bilateral trade with China and, potentially, to follow China's global leadership.

Figure 7 illustrates a strong relationship between having a FTA with China and participation in the summit. Over 41 percent of the nations that sent chief executives to the Belt and Road

Forum on global cooperation have a FTA with China, but less than 4 percent of the nations that did not participate (or sent a lower official) have one.

Figure 7: FTA with China and Leader Attendance at the Belt and Road Forum



4. Conclusion

Our theory of global leadership transition is that potential followers of the erstwhile new leader consider both the grievances they have with the *status quo* – the push factors – as well as the economic benefits offered by the new leader. Since the novel aspect of our argument involves push factors, we conclude with a discussion of the policy implications for increasing the appeal of the current international economic order.

An optimistic policy implication is that the United States and other supporters of the current order can work together with China to take steps to address the grievances that we have highlighted and measured. China is and remains a major supporter of multilateralism and welcomes efforts to strengthen the global economic order. But since the grievances are self-generated by policy decisions in the U.S., the current leadership can act on its own to resolve them.

To address the dissatisfaction that international financial instability has caused, the U.S and the IMF should reduce support for unrestricted short-term financial flows and promote foreign direct investment (FDI) instead. FDI investors cannot easily liquidate their assets and depart from a nation, which makes FDI a stable form of cross-border investment. By contrast, portfolio investments are highly volatile. By supporting FDI as the basis of the global financial system, dissatisfaction with IMF conditionality will also be greatly reduced, since there will be fewer financial crises for the IMF to manage.

Grievances about global governance can also be addressed from within the current regime, provided that the U.S. Congress is on board. American legislators might be more willing to support redistributing more IMF votes toward emerging markets if they realize that failure to do so is pushing nations away from the current global order. The same holds for excessive use of the WTO's escape clause loophole. If U.S. policymakers knew that discriminatory trade barriers cause resentment overseas and damage the attraction of the current world order, they might be less willing to employ this form of protectionism every time a domestic industry asks for it.