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*Nicolás Salmerón**

RECALIBRATING THE GLOBAL BALANCE OF POWER

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Abstract:

The last decades have brought the rise of Asian powers, in particular China. In parallel, the United States has shown signs of relative decline over the same period. This notwithstanding, social, (geo) political, demographic, energetic, military and, most importantly, economic factors point to significant challenges for China as it moves up the ladder of development on the one hand, and to a renewed North American strength and momentum on the other. In light of these data, the unstoppable nature of the rise of the Asian giant – and the decline of the world's current superpower – is being put to question.

Keywords: China, United States, Economy, Demography, Democracy, Energy, Military

Resumen:

Las últimas décadas han traído el auge de los países asiáticos, y en particular el de China. En paralelo y durante el mismo período, los Estados Unidos de América han dado muestras de declive relativo. Sin embargo, factores sociales, (geo) políticos, demográficos, energéticos, militares y especialmente económicos ponen de manifiesto, de una parte, los importantes retos que China tendrá que superar en su camino hacia el pleno desarrollo y, de otra, una renovada fortaleza norteamericana. Estos factores permiten cuestionarse el carácter imparable del ascenso del gigante asiático así como el inevitable declive de la actual superpotencia.

Palabras Clave: China, Estados Unidos, Economía, Demografía, Democracia, Energía, Ejército

RISING DRAGON, SHATTERED DREAM

China seems determined to take over the United States (US) as the world's leading superpower. Since 1976, when it last registered a negative economic growth, China's economy has been growing at an average of just under 10 per cent yearly. The 'Asian giant' doubled its Gross Domestic Product (GDP) between 1997 and 2005, and again between 2005 and 2012, placing its economy at $4.5 trillion, third only to that of the European Union and United States at $14.6 and $14.3 trillion respectively.[1] This extraordinary growth has lifted millions out of poverty. In 1990, 60 per cent of China's population was living on less than $1.25 per day.[2] In 2009, the last year for which data is available, this percentage had fallen to 12 per cent. Within a decade, from 2002 to 2012, Chinese per capita GDP more than doubled in real terms, increasing from $3.108 to $7.958 per year in terms of purchasing power parity (PPP).[3] In comparison, China produced the equivalent of Greece's GDP in less than 3 weeks in 2011, with an annual output of over 18 times that of the Mediterranean country in real terms.[4]

By matter of contrast, for the first time there are more Americans who think that US President Barack Obama is not respected by other world leaders than those who believe he is, according to a February 2014 Gallup poll. This represents a dramatic shift from 2009, when only 20 per cent believed that President Obama was not respected by other world leaders, as opposed to 67 per cent who believed he was. In addition, 61 per cent of US citizens has said to be dissatisfied with the position of the United States in the world, up from 51 per cent a decade ago. Indeed, persistent imbalances, the severity of the economic crisis that erupted in 2008 and the recent domestic political deadlock that brought the world's first economy close to default, amongst others, has led many to believe that US supremacy might be coming to an end.

A FLIGHT OF ICARUS?

Notwithstanding China's astounding economic performance in the past three decades, the country still has a long way to go in order to become a global superpower. China faces a series of significant challenges, which will increase in complexity as well as in number in the years to come.

Farewell to the masses

China has undertaken discreet but constant political reform since it started its economic expansion in the mid-1970s. One of the most significant impacts of the economic and political 'revolutions' over the years has been an alteration of the country's constituency.

[1] World Development Indicators, constant 2005 $, figures for 2012, available at: http://data.worldbank.org/
[2] World Development Indicators , PPP, 2005 international prices, available at: http://data.worldbank.org/
[3] World Development Indicators, constant 2005 $, available at: http://data.worldbank.org/
[4] World Bank, GDP China constant 2005 $: 4,194 trillion; GDP Greece constant 2005 $: 0.223 trillion $, in 2011, available at: http://data.worldbank.org/

The Chinese leadership now faces a population endowed with more resources 'in terms of money, talent, and information', notes Professor David Lampton, Director of China Studies at the Johns Hopkins Paul H. Nitze School of Advanced International Studies (SAIS).[5] As the population becomes increasingly plural, Chinese societal homogeneity has been fractured. Leaders no longer have to respond to the Chinese 'masses', but to different constituencies within the country. The GINI coefficient, which measures inequality in the distribution of income, increased by over 40 per cent from 1981 to 2005, the first and last date for which data is available. In addition, the population has shifted from being primarily rural to increasingly urban: whereas only 19 per cent of the population resided in urban areas in 1980, the figure was 52 per cent in 2012, with urban population growth rates amounting to 3 per cent annually since 2008. Employment rates have followed a similar pattern: from 69 per cent in 1980, the figure of total agricultural employment had dropped to 35 per cent by 2011. Finally, the literacy rate increased from 66 per cent of the total population to 95 per cent over the same period.[6]

As Professor Lampton suggests, those who believe social and political stability can be maintained 'without dramatically reforming the country's system of governance' are profoundly wrong. China has today a much stronger, active and vocal civil society despite increased pressure and enhanced crackdowns by the Chinese authorities.[7] The number of civil society organisations has increased at constant pace. According to the Institute for Security Studies (ISS), the total number of civil society groups has risen by around 12 per cent annually in recent years, with 253.000 'social groups', 2.510 foundations and 202.000 non-profit organisations (NGOs) registered within the Ministry of Public Administration in 2011.[8] This does not take into account underground movements and organisations, which should not be neglected. Moreover, the number of Internet users has also rapidly increased, amounting to 42 per cent of the population in 2012.[9]

In light of these trends, political and social turmoil, with unpredictable consequences, cannot be discarded, and there lies one of China's most significant challenges. In fact, popular dissent could increase if, as will be analysed below, slower economic growth materialises and censorship, crackdown and repression intensify.

Economic cool-down

The 'Asian giant' is undergoing a substantial transformation, moving away from an export- and investment-led growth model towards one in which private consumption takes centre stage as the engine for growth. The financial crisis exposed the limitations of a model that

[5] How China is Ruled, Council on Foreign Relations, 2014
[6] World Development Indicators, available at: http://data.worldbank.org/ for GINI coefficient, employment and literacy rates. Data for literacy rates until 2010.
[7] http://www.transparency.org/news/feature/chinas_chance_to_reform
[8] http://www.iss.europa.eu/publications/detail/article/chinese-civil-society-at-a-time-of-leadership-change/#_ftn3
[9] World Development Indicators, available at: http://data.worldbank.org/

was biased towards investment and exports, and thus dependent on third countries. As the capacity of industrialised economies to absorb products from Asia diminished, Chinese exports fell considerably, from 38 per cent of GDP in 2007 to 27 per cent in 2012. In addition, the crisis intensified Japanese efforts to stimulate the economy via monetary easing. Consequently, the renminbi appreciated relative to the yen, which in turn reduced the competitiveness of Chinese products. By boosting investments, the Chinese government was able to reduce the impact after 2007–8. There was, however, a price to pay in terms of delays in the transformation of the Chinese economy, thus increasing risks inherent to the old model. Moreover, it might have also resulted in over-capacity. Indeed, the importance of Gross Capital Formation (GCF) in China has been – and still is – very significant, accounting for over 40 per cent of China's aggregate demand in the years leading to the financial crisis of 2007–8. GCF amounted to 49 per cent of GDP in 2012, which contrasts starkly with the 19 per cent figure for the United States. On the other hand, household consumption as a share of aggregate demand declined from 47 per cent in 2000 to 35 per cent in 2012 (65 per cent in the United States).[10] In light of the intrinsic risks associated with a model based on high investment rates, high exports and high growth, the Chinese authorities now wish to transit to a model based on less investment, less exports, and more consumption, accepting more moderate growth. Despite making sense economically, the Chinese authorities will face many difficulties to turn China into a consumer society.

First, the Chinese economy has recently experienced a slowdown despite increasing investments to counteract decreasing net exports. Indeed, GDP growth fell to around 7.7 per cent in 2012 from an average close to 10 per cent in the past decades.[11] The International Monetary Fund (IMF) predicts even lower rates until 2018 of around 7 per cent on average. Chinese experts have pointed to the possibility of even lower growth of 6.5 per cent between 2018 and 2022.[12] There are several risks associated with such a 'low' growth rate. In particular, this figure would place the Asian country below the 7.5 per cent threshold which, according to the German Institute for Economic Analysis (Deutsches Instiut für Wirtschaft; DIW), could be necessary to ensure appropriate employment opportunities for migrant workers. Although it is deemed to be under control, if such a scenario were to become a reality, political friction could develop. Moreover, according to British economist and journalist Martin Wolf, such a significant decline in growth would trigger a reduction of the investment rate in productive capital strong enough to 'cause a depression all on its own' if it happens swiftly.[13]

Second, Chinese state-owned banks' balance sheets could have significantly deteriorated as a consequence of a loose loan-extension policy applied during the crisis years to stimulate the economy. Indeed, many loans seem to have been granted to unproductive and unprofitable sectors. If, as will likely happen, unprofitable businesses are not in a position to

[10] World Development Indicators, available at: http://data.worldbank.org/
[11] International Monetary Fund, available at: http://www.imf.org/external/pubs/ft/weo/2013/02/weodata/weorept.aspx?sy=2011&ey=2018&ssd=1&sort=country&ds=.&br=1&pr1.x=40&pr1.y=6&c=924&s=NGDP_RPCH&grp=0&a=
[12] Why China's economy might topple, Financial Times, April 2013
[13] Why China's economy might topple, Financial Times, April 2013

deleverage, the Chinese state will need to absorb unpaid debts which would, in turn, result in a substantial increase of public debt – which is already increasingly worrying – possibly leading the Chinese economy to a downward spiral which is all too well-known in Spain. Tellingly, China suffered its first corporate bond default in recent history on 7 March 2014, 'after a small Shanghai-based solar power company failed to pay out interest on a security it sold two years ago'.[14]

Third, private consumption has been stagnant at around 35 per cent of GDP since 2006.[15] Christian Dreger from the DIW in Berlin points to a high savings rate[16] to explain this. According to the expert, the Chinese social security system – pensions, medical care and unemployment benefits – is not sufficiently developed. Consequently, households are forced to save significant parts of their income in anticipation of more difficult times. China's one-child policy adds to the problem, whilst an increase in government investments to improve the system is not foreseeable in the short term, according to the DIW. In addition, given the underdevelopment of the financial system and the resulting absence of loans to finance private consumption, families need to be able to save to pay for basic consumption products that are expensive. Since a fall in the savings rate is unlikely, increasing consumption – absolutely central to shift to a consumer society– would require an increase in income. Whereas this is feasible according to Mr. Wolf, it could nonetheless have a negative aggregate impact on the Chinese economy, as declining profits would reduce investments (further) and increasing wages would negatively affect competitiveness.

Fourth, China faces a two-sided problem as regards the housing market. On the one hand, China is experiencing a housing boom, with property prices steadily rising – according to *Financial Times* data, real estate prices doubled between 2003 and 2012 – and the construction of 15 million new houses per year, sufficient for every household in China to own a home.[17] On the other hand, price hikes may be in part triggered by the absence of 'incentives to cool down the sector',[18] which is the greatest source of revenue for regional and local governments and has also proven quite lucrative for corrupt officials.[19] Also, according to Nomura economist Zhiwei Zhang, real estate has critically contributed to GDP growth over the past five years.[20] This situation constitutes a dilemma for the Chinese authorities, who would like to avoid further encouraging the property boom, but who may not be in a position to curtail soaring prices, particularly now with slowing GDP growth.

More worryingly, adds Mr. Zhang, 'the government may not have the proper policy tools to manage a situation where oversupply eventually causes property prices to fall, particularly in

[14] China suffers its first corporate bond default, Financial Times, 2014
[15] World Development Indicators, available at: http://data.worldbank.org/
[16] According to the World Bank, Gross Domestic Savings as a share of GDP amount to roughly 50% of GDP in China since 2006 as opposed to 15% in the United States.
[17] Available at: http://www.bloombergview.com/articles/2014-01-30/china-can-t-afford-to-let-its-housing-bubble-pop
[18] China property boom shows no sign of abating, Financial Times, 2013
[19] Winners and losers in the new China, Financial Times, 2014
[20] Available at: http://online.wsj.com/news/articles/SB10001424052702304610404579401832066853554

third- and fourth-tier cities'.[21] Indeed, a cool-down could be already underway. In January 2014, prices rose by 8.98 per cent, in comparison to an increase of 9.17 per cent in December 2013.[22] Professor Gan Li, economist at Chengdu University, estimates that 65 per cent of China's household wealth sits in real estate, in a country where 90 per cent of the population owns homes. This puts the government in a 'catch-22' situation, where inaction might lead to a housing bubble burst and intervention would also entail negative economic consequences.

Finally, the 'outside world' could add to internal challenges. Tightening monetary conditions in the United States could have a severe impact on capital flows, which could constitute a serious additional threat to China's economy if not managed correctly.

A broken contract

A (significant) reduction in GDP growth has the potential to disturb social and political stability in China. Ever since the crackdown on protesters in Tiananmen Square, 'the Chinese Communist Party (CPP) has depended on economic growth to ensure stability', admits Johan Lagerkvist.[23] In China, an important component of the social contract has been the exchange of political legitimacy for economic growth and increasing living standards[24]. Changing the economic model and other (planned or unplanned but needed) reforms 'could dislocate large swaths of society, including migrant labourers, university graduates, and disgruntled civil servants', opines Mr. Lagerkvist. The decision to rebalance the economy has been accompanied by the creation of 'a new State Security Committee', implying 'further consolidation of power in the hands of China's security sector' and General Secretary Xi Jinping himself', who now has more power to 'crackdown on popular dissent', he adds. But the plan could backfire. China's population is more educated and has greater access to information and technology. Also, evidence suggests that the population's well-being and level of satisfaction – central to the social contract – has not kept pace with GDP growth. The United Nations Human Development Index (HDI) points towards stagnation in human development.[25] Additionally, the 'percentage of Chinese who describe themselves as very happy fell from 28 per cent in 1990 to 12 per cent in 2000', according to the World Values Survey.[26] As notes political scientist Christian Welzel, most Chinese have seen their *relative* wealth decline despite extraordinary growth rates and increases in *absolute* wealth. This has resulted in a generation of 'frustrated achievers' who have become 'poorer relative to those above them'.[27]

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[21] Available at: http://online.wsj.com/news/articles/SB10001424052702304610404579401832066853554
[22] Available at: http://graphics.wsj.com/econtracker-china/index.php#ind=houseprice
[23] China's risky reforms, Council on Foreign Relations, 2014
[24] A thoroughly analysis of the China's internal challenges can be found in GARCIA SANCHEZ, Ignacio. "China's inner ring. Strength or weakness?" available in: http://www.ieee.es/en/Galerias/fichero/panoramas/Geopolitical_Panorama_2013.pdf
[25] United Nations, Human Development Reports, available at: http://hdr.undp.org/en/countries
[26] China's risky reforms, Council on Foreign Relations, 2014
[27] China's risky reforms, Council on Foreign Relations, 2014

SHATTERED DREAM?

Unlike the Euro zone, the US economy seems to be finally taking off after a period of recession, stagnation and slow recovery. More importantly, growth rates seem to be outperforming IMF forecasts, currently at 2.8 per cent and 3.0 per cent for 2014 and 2015, respectively. This optimism is supported by different factors, as noted by Martin Wolf at a conference at the Rafael del Pino Foundation on 4 March in Madrid. First, in contrast to what is happening in China, house prices in the US seem to have almost returned to levels similar to those of the second half of the 1990s. Second, the US seems to be successfully deleveraging. According to McKinsey Global Institute, US private-sector debt has fallen relative to GDP in all categories since the end of 2008.[28] Financial-sector debt has declined from $8 trillion to $6.1 trillion and stands at 40 per cent of GDP, below the mark of 2000. In addition, among US households, 'debt has fallen by 4 per cent in absolute terms', some $584 billion.

Indexing real GDP figures (base year 2008) for the US, France, Germany, Japan, the UK and the Euro zone yields interesting results. From the first quarter of 2008 onwards, the US economy had been falling, reaching an absolute low of approximately 96 points. Outperforming other advanced economies, in early 2011 the US was back to the level of the first quarter of 2008, and has been rising since. Today, the US economy is over 106 points (that is, 6 percentage points above the 2008 base year), while the second-best performing economy – that of Germany – stands at around 103 points.[29] US productivity figures are also encouraging. According to the Organisation for Economic Cooperation and Development (OECD), labour productivity measured as GDP per hour worked (in constant prices) increased by 7.7 per cent between 2007 and 2012. By way of contrast, productivity rose by 4.5 per cent on average for all OECD countries, 2.8 per cent for the Euro zone and 10 per cent for the United States between 2002 and 2007. These figures point to significant growth potential for the United States in the years to come. It also casts a shadow over the Euro zone – excluding Spain which boasts encouraging productivity data – and the UK.

Most importantly, the United States is said to be steadily moving 'towards meeting all of its energy needs from domestic resources by 2035'.[30] According to World Bank figures, US net energy imports (as a percentage of energy use) peaked in 2005 at 30 per cent after rising steadily since the 1990s. Since then, however, net energy imports have fallen substantially, halving in 7 years to reach 15 per cent in 2012. These figures are most striking if compared to those of China, which has rapidly swung from being a net energy exporter (with net exports equalling -0.2 per cent as a percentage of energy use in 2001) to becoming a net energy importer, with imports amounting to almost 11 per cent of energy use. The International Energy Agency (IEA) estimates that China will become the largest oil-consuming country by 2030. The US could benefit from reduced dependence on imported

[28] Available at:
http://www.mckinsey.com/insights/global_capital_markets/uneven_progress_on_the_path_to_growth
[29] World Bank Data, Martin Wolf's presentation at the Fundación Rafael del Pino on March 5th, 2014
[30] World Energy Outlook, WEO, 2013, available at: http://www.worldenergyoutlook.org/publications/weo-2013/

energy – especially from outside North America – both geo-politically, as a given country's dependence on imported oil from potentially unstable regions could prove a strategic weakness relative to the United States, as well as economically.

Indeed, existing price differentials - partly derived from increased energy self-sufficiency in the United States - play a significant role in determining a country's ability to compete in the global economy, and thus its ability to enhance growth. The IEA 2013 World Energy Outlook estimates that Chinese industrial consumers pay on average double for electricity relative to their US counterparts. This puts pressure on the Chinese economy, which competes mainly on the basis of low prices, as sustained differentials in energy costs – a critical input – could significantly hamper its competitive advantage vis-à-vis the United States and the world. Regional differences in energy prices, which could severely affect the competitiveness of countries with high relative costs, are forecasted to remain high through to 2035, according to the IEA[31].

Finally, *national accounts* – such as GDP or the Balance Payments – could be ill-suited to capture the economic underpinnings of modern power in a context of increased globalisation. As illustrated by Sean Starrs of York University,[32] the fact that China is the 'world's largest electronics producer since 2004' does not imply that China, as a nation, is leading the electronics industry, given that today's world is characterised by transnational corporations. Based on different countries' GDP and corporate sales figures, economists Sarah Anderson and John Cavanagh concluded that in 2000 out of the 'largest economies in the world, 51 [were] corporations [and] only 49 were countries'.[33] They added that the combined sales of the world's 200 major corporations were larger than the combined economies of all countries worldwide minus the 10 richest nations. Consequently, arguing along the lines of Chinese GDP versus US GDP (a US corporation producing in China is part of Chinese GDP) could lead to significant miscalculations with regard to actual economic, and thus political, power. As Mr. Starrs argues, if the world's top transnational corporations are analysed, 'the resulting picture of economic power is 'startling'. Of the 25 economic sectors analysed by Mr. Starrs, US firms 'have the leading profit share in 18, and dominate (with a profit share of 38 per cent or more) in 13 of those sectors'. Japan is the only other country in the world to dominate an economic sector (and only one, namely trading companies). In addition, argues Mr. Starrs, many of the sectors that are behind Chinese growth are dominated by US corporations, implying that the 'rise of China' in effect increases US power, to the extent that these top corporations are owned by US individuals.[34] Also, 65 of the top 200 corporations in the world are American ($556.5 billion in profits), whereas only 16 are Chinese ($196.2 billion in profits).[35]

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[31] A thoroughly analysis of the China's energy security can be found in GARCIA SANCHEZ, Ignacio. "The rise of China and its energy supply" available in: www.ieee.es English
[32] America did not decline, it went global, Politico, 2014
[33] Anderson and Cavanagh, 2000
[34] Sean Starr's research shows that, on average, more than 85% of top 100 U.S. transnational companies' shares are owned by U.S. citizens
[35] Own calculations based on the Forbes Global 2000 list of the world's biggest companies, total profits: 1553.4 billion.

IT'S ALL ABOUT THE PEOPLE

Demographic pressures inevitably play a major role in the (social and political) performance of any economy, including those of the United States and China. In this regard, five variables – population, population growth, labour force, the age-dependency ratio and fertility rate – are key.

The United States has experienced consistent annual population growth of 1 per cent since the 1990s, from 250 million people in 1990 to 314 million in 2012.[36] China's annual population growth averaged 1 per cent between 1990 and 2008, but has since been stable at around 1.4 billion people. In particular, between 2000 and 2010, the Chinese population grew at an annual rate of 0.57 per cent, whilst the world's population grew at more than twice that rate.[37]

The Chinese labour force has followed a similar pattern, growing importantly between 1990 (630 million) and 2008 (770 million), and remaining constant since. The United States labour force has remained practically stable since the second half of the past decade, at around 155 million workers. However, the age-dependency ratio – defined as the share of those below 15 or over 64 relative to the working-age population (15 to 64) – has improved substantially in the past three decades (the lower this rate, the better). This notwithstanding, according to World Bank and OECD data, this ratio reached an all-time low in 2012, at 36 per cent. As the population ages and fertility rates decline, this figure is expected to increase sharply in the years to come, reaching 50 per cent by 2030 and 80 per cent by 2070.

China's fertility rate[38] descended from an average of almost six children per woman in 1970 to two in 1991. The OECD estimates China's current Total Fertility Rate (TFR) to be at 1.18 children per woman. Due to under-reporting of births partly as a consequence of the one-child policy, China's actual rate could be a little under 1.5. This not only implies that China's fertility rate is below that of developed nations, but also that the Asian country is 'approaching lowest-low fertility rates', with potentially dramatic demographic and socioeconomic consequences.[39] In the US, the ratio has averaged around 2 children in the last four decades.

These figures point to similar patterns of little (US) to no (China) growth in population, labour, and fertility rates in both countries. However, the 'Asian giant' faces much bigger demographic challenges than the US. First, despite stable fertility rates in both nations, the US has levelled at a ratio almost double that of China. Second, if current trends continue, China's population growth will turn negative by 2027.[40] Third, China is ageing (too) quickly.

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[36] World Development Indicators, available at: http://data.worldbank.org/
[37] OECD China, The silver and White economy, pg. 5
[38] Definded by the World Bank as the number of children that would be born to a woman if she were to live to the end of her childbearing years and bear children in accordance with current age-specific fertility rates.
[39] OECD China, The silver and White economy, pg. 7
[40] OECD China, The silver and White economy, pg. 6

In the capital Beijing, the percentage of people over 60 went from 10 per cent in 1990 to 12.5 per cent in 2010 (and it is expected to reach 20 and 30 per cent in 2020 and 2030, respectively), according to OECD data.[41] Finally, estimates place the percentage of over 80's at roughly 3 per cent of the population by 2030, fully converging with that of the United States (which will be 5 per cent by 2030) by 2050. By then, 7 per cent of the population in both countries will be over 80 years of age, and 25 per cent over 65 in the developed world as well as China, painting a somewhat gloomy picture especially for the Asian giant.

A TALE OF TWO MILITARY POWERS

The United States Armed Forces are – much like the rest of Western nations – currently subject to budget pressures, which are likely to continue in the near future. Between 2010 and 2012, the US reduced its annual defence spending by $45 billion to reach a total spending of $645.7 billion.[42] During the same period, China increased its spending by $26 billion, reaching $102.4 billion.[43] China has announced plans to continue this upward trend in 2014. Currently, the US Armed Forces total 1.5 million men, compared to 2.3 million in China.[44]

China could eventually overtake the United States as the world's largest defence spender. Double-digit annual percentage GDP growth rates during the past decade have allowed for the rapid modernisation of China's People's Liberation Army (PLA). A slowdown in GDP growth could force the country to halt down military spending. The International Institute for Strategic Studies (IISS) questions whether China's military technology will continue to improve at the same pace. The IISS estimates that a convergence in defence spending between the US and China would occur 'after 2028 rather than before, should it occur at all'.[45] Defence-spending projections are inextricably linked to uncertainty. This is even more so in the case of China, whose eventual challenges could lead to spending on defence giving way to other more pressing needs. But even if Chinese and US military spending were to converge around 2030, this does not imply that China could rival the US. It could take many more years for China to reach the level of *accumulated* US spending and, more importantly, US military know-how. In addition and contrarily to what could seem logical at first, the period of reduced military and defence budget the US faces in the short and medium terms could actually improve US military strategy, as it will force Washington to 'think strategically, something it rarely does when times are flush', argues Professor Melvyn P. Leffler of the University of Virginia.[46]

[41] OECD China, The silver and White economy, pg. 6
[42] The Military Balance, International Institute for Strategic Studies, 2013
[43] China's defence spending as a share of GDP declined to 1.24 percent between 2010 and 2011, remaining stagnant in 2012. The U.S.' defence spending declined in absolute terms as well as relative to GDP -from 4.76 percent in 2010 to 4.12 percent in 2012.
[44] The Military Balance, International Institute for Strategic Studies, 2013
[45] The Military Balance, International Institute for Strategic Studies, 2013
[46] Defence on a Diet, Council on Foreign Relations, 2013

Mr. Leffler opines that 'contrary to conventional wisdom, the consequences of past US defence cuts were not bad'. The US cut back its defence spending from around 17 per cent of GDP in 1919 to less than 2 per cent three years later, and scaled down its military from 3.5 million soldiers to 146.000 over those years, amongst other measures, even before the Great Depression forced the US government to engage in further cuts.[47] Scholars cited by Mr. Leffler have shown that, despite the Pearl Harbor attack, 'the low levels of US military spending in the 1920s and early 1930s […] neither compromised nor thwarted significant technological innovation and organizational change'. Resource scarcity in a context of crisis forced Harold Stark, then chief of naval operations, to prioritise and 'come up with a strategic concept that would shape US foreign policy for the next half century'. In sum, 'the negative consequences of defence austerity have been exaggerated', as problems that erupted during times of scarce spending 'were rarely, or only partly, the result of austerity itself', argues Prof. Leffler. Tight budgets can in fact help develop 'a coherent strategic concept, a clear assessment of threats, a precise delineation of interests and goals, and a calibrated sense of priorities', all of which are essential components to defence.

CONCLUSION

While the US seems to have entered yet another wave of 'declinism', all eyes are set on China's assumed rise. However, the other side of the story questions the irrevocable nature of China's ascent, and paints a brighter picture for the world's superpower.

In China, a combination of slower economic performance, structural changes including an economic rebalance, and several challenges that could further decelerate growth could trigger popular dissatisfaction and social unrest. This, in turn, could worsen economic conditions, leading to renewed protests or riots, especially in light of the population's increasing unwillingness to tolerate abuse, injustice and rising inequality. The consequences are hard to predict, especially if Beijing continues to apply a neo-authoritarian governance model combined with intensified crackdowns. In addition, China is ageing quickly and thus facing very significant demographic challenges. While this demographic trend is also evidenced in the West, including in the US, China is at a very different stage in terms of economic and social development. China has benefited enormously from the demographic dividend, which has been a fundamental source of abundant and cheap labour, and thus an engine for growth. Whereas the United States is a fully industrialised economy, China still needs to successfully avoid the middle-income trap, and it will have to do so as the demographic dividend fades away. Finally, the rise of China as the world's leading nation in terms of its military (spending) is questionable in light of China's macroeconomic and demographic challenges, and of a global world order in which military strength ultimately depends on economic performance.

In the United States, productivity has increased during the crisis years, which is a symbol of future economic strength and enhanced well-being. Firms and households are deleveraging,

[47] Defence on a Diet, Council on Foreign Relations, 2013

and the country seems to be moving towards energy self-sufficiency, whilst industrial consumers already pay on average half for electricity relative to their Chinese counterparts. Whereas the US also faces demographic challenges, these are not as important as they are for China. In addition, the reduction in US defence spending could be small relative to the rest of the world. In 2012, the US still spent more than the next 10 highest-spending countries combined, including China.[48] Finally, subsequent budget cuts in US defence spending could, far from compromising US strategy, power and military capabilities, actually enhance them.

The Asian continent has dominated the world economy for a significant part of the last two millennia. It should not come as a surprise if China-led Asia were to play a greater role in the global economy in the future. But so far there is no guarantee that China will become the world's superpower in the near future. Indeed, important challenges lie ahead, especially as China must avoid the so-called middle-income trap as it paves its way to further development, successfully switching from a low-wage and low-cost model to one which produces high value-added items. History has shown that very few countries have been able to do that in the last half century. It would be brave at this point to affirm that China will be another one of them.

Nicolás Salmerón[49]
Research Assistant at FRIDE
http://fride.org/expert/662/nicolas-salmeron

[48] Military Expenditure Database, Stockholm International Peace Research Institute, available at: http://www.sipri.org/research/armaments/milex/milex_database