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China's Tail Wagging the Dog

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China has always regarded itself as the center of the world, the Middle Kingdom surrounded by hostile or subservient barbarians. Now, after a hiatus of several centuries, this view once more corresponds to reality as China emerges as a global economic superpower.

With China at the center, global economic processes of the past two decades are seen in a new light. Since the early 1990s, economists have been insistently predicting the bursting of the Chinese bubble. No major crisis has occurred, but even now there are dire warnings that China invests too much and suffers from excess borrowing, which should lead to disastrous consequences.

Don't blame the economists. Periodic crises have been common in all rapidly growing Asian countries, from Japan to South Korea and Thailand, and, by extension, should have been perfectly normal in China according to economic logic.

However, those Asian Tigers and Cubs, as they were called, were economic satellites of the U.S.. After World War II, the U.S. economic dreadnought sailed on relatively smoothly, whereas smaller economies were going through regular boom-and-bust cycles. China, however, is a dreadnought in its own right. Moreover, it can be argued that it is a dominant economy in the making, and the rest of the world, including the U.S., Europe and Russia, are becoming its economic satellites.

Since the emergence of China as a manufacturing hub, the U.S. has been the key market for Chinese goods. The dollars that China earned were used to build its industry and infrastructure. U.S. companies, outsourcing production to China, supplied the bulk of investment funds.

The U.S. didn't do it for China's sake. For its own political reasons, Washington maintained easy monetary policy to stimulate domestic demand and allow Americans to buy lots of Chinese goods. But the result disproportionately benefited China. While U.S. infrastructure and investment were neglected and government debt skyrocketed, China built roads, airports, cities and factories and became the world's largest creditor, with reserves of $3.7 trillion.

Similarly, while the Pentagon maintains military presence in some 100 countries and fights endless wars for its own strategic reasons, it creates a stable world order in which China prospered.

Russia and other oil producers also benefited from the printing of dollars by Uncle Sam, which supported China's demand for oil and boosted oil prices to record levels.

Throughout this period, the Chinese economy has been stable, avoiding turmoil and growing at a steady pace averaging 8 percent. It was the U.S., Europe, Russia and other countries that went through boom-and-bust cycles typical of satellite economies — first from 1995 to 2002 and then from 2005 to 2009. Now, a new bubble is inflating in U.S. financial markets.

China is entering a new stage of development, shifting from export-led growth to domestic consumption. Beijing has just announced several measures pointing in this direction, which included a partial relaxation of the country's one-child policy.

China is once more predicted to go through a period of economic uncertainty as it changes course. But more likely, changes in China will trigger severe turbulence elsewhere, starting with the U.S. Eventually, the role of other countries vis-a-vis China may also change, and they may begin to supply China's enormous market with commodities and consumer goods as well, just as they have been supplying the U.S. market up until now. How wealthy other countries will be in this economic system may depend on how much China values what they sell to it.

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