Tradeoff: China's Control of the RMB and its Economic Sovereignty

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Abstract

Currency mobility policy has been not just an economic, but an ideological tool in the years of PRC rule. China has used it to assert independence, and – to a disputed degree – used it as a development tool. Now, as China becomes more integrated into the world economy and its institutions, China's ability to use currency mobility policy as a way to maintain economic sovereignty is being reduced. This paper will outline this process, and then interpret it through the use of classical and post-Western IR theory, drawing the conclusion that China is going through the process of financialisation – which inevitably removes control of the economy from the levers of government.

Keywords: China, Currency, Financialisation, World Systems

China's currency policy has long been a bugaboo in international economic debates. Accusations of Chinese currency manipulation are not just common in world bodies such as the WTO and IMF, but are as much a mainstay in US presidential politics as guns and God.

While American politicians have been unified in their assertions of Chinese currency manipulation, the academic community has not been so inclined to consensus. While it is generally accepted that China has had the structures in place by which they could manipulate the relative price of their currency on the world market; what has been less agreed upon is the degree to which the rate of the renminbi has differed from what would have been the hypothetical market price in the absence of government interference.

Thus this paper will follow a progression through the issue. First, it will outline the history of the policy in question – China's currency mobility policy in the PRC era. Then, it will cover the debate about the degree to which China's policy choices have and continue to distort the relative market position of the renminbi, its motivations, and effects. Finally, these results will be interpreted through international relations theory. First, there will be an application of realism, to understand the choices of China in a traditional, Western IR structure. Then, the interpretation will advance to a post-Western perspective, utilizing the Chinese concept of Tianxia – all under heaven. The paper will then conclude with a variant on critical theory, wherein the concept of finanicialisation is applied to world systems theory.

All of this will bring us to the central argument of the paper: that despite its history, China's moves towards deeper integration with the global economy and its institutions have reduced its ability to exercise control over its currency mobility going forward. Increased vulnerability to capital flows, combined with China's commitments to international governing bodies such as the IMF, mean that China's future capacity to use currency mobility policy as means of ensuring economic sovereignty has been depleted.

Historical Background

Since the Communist party has come to power, currency policy has been central to the party's vision for a strong China. Currency stability was at the centre of Mao's economic policies – as he saw inflation as a scourge of the working masses, and a sign of the inherent economic weakness of the capitalist West and 'revisionist' Soviet Union[1]. A combination of currency and price stability, combined with a total aversion to internal or external debt, thus shaped Chinese policy for the remainder of the Mao years. It was not until the death of Mao, and the rise to power of the reformist Deng Xiopeng, that China's currency policy modulated to any degree of significance.

This took the form of extreme central control of all forms of currency exchange[2]. The state had, from the rise to power

[1] Hung, Yin Han, and Tsai Cheng, China's renminbi: one of the few most stable currencies in the world, Foreign Language Press, Beijing, 1969

[2] Goldstein, Morris, and Nicholas R. Lardy, *The Future of China's Exchange Rate Policy*, Policy Analyses in International Economics 87, July 2009

in 1949 until the late 1970s, fixed an artificially strong value on the exchange rate as part of the Maoist goal of import substitution and self sufficiency[3]. From the 1950s onward, all export earnings and other foreign exchange were required to be deposited in the Bank of China, which was the only institution with authority to handle foreign exchange. Only state-owned companies were permitted external trade, and then the accumulated reserves would be allocated according to state priority. This system continued largely uninterrupted until Mao's death in 1976.

The rise of Deng Xiaopeng

Mao's death led to an openness to reformist ideas, under Liu Shao-Chi[4] and primarily under Deng Xiaopeng. in December 1978, the Third Plenum (of the Eleventh Central Committee of the CCP) the new leadership declared the advent of the *gaige kaifang* policy[5]. This policy basically meant an opening to the outside world, and a renunciation of Mao's more extreme leftist policies.

In terms of currency mobility and exchange, 1979 marked the beginning of this opening up to the outside. Exporters and the local government to which they paid taxes were allowed to hold a portion of their foreign exchange earnings, as opposed to handing them over in their entirety to the Bank of China.[6]

There was another adjustment to currency policy at the same time, which was more complex. Similar portions of earned foreign currency were allowed to be retained, such as those accumulated from remittances, port fees, and tourism. These were all subject to varying levels of permitted retention, but the overall move was a significant shift to market-based incentives to export and engagement with the international economy. In half a decade, these retained portions had risen to 40 percent of overall foreign exchange remaining in the purview of the trading firms and their respective local governments.[7]

Having said reserves in hands outside of the Bank of China, at levels that surpassed the immediate need for overseas purchases, inevitably led to the need for an exchange market of some sort.[8] This led to, as it often does in closed economies, a dual-exchange rate system, introduced in 1981. This began in Shanghai – the traditional hub for foreign trade in China, and gradually led to the introduction of 'swap centres' in dozens of cities.[9] The government initially tried to control the rates of exchange in these, but foreign exchange routinely was valued higher than the official rate.

This market signal, clearly indicating overvaluation, ties with the other major reform undertaken in the same time frame. There was a move to devalue the official rate of the renminbi, beginning in dramatic fashion in January of 1981. At this time, the State Council announced a new internal settlement rate of 2.8 renminbi to 1 US dollar.[10] This was a substantial move from the previous rate of 1.5 renminbi, representing a devaluation of almost 100 percent. This cemented the dual-exchange system, as non-trade transactions were still done at the official exchange rate. Gradually, then, the official exchange rate was lowered, so as to bring it even with the internal settlement rate – which it did in 1984, at the rate of 2.8 Renminbi. Thus merged, in 1985 the internal settlement rate was disbanded, although the swap centres did continue to operate at lower-valued, market-driven prices, with slight fluctuations in the exchange price therein because of 'imperfect arbitrage between swap centres".[11]

The authorities then continued their series of devaluations. They moved 15 percent overnight in July 1986 to a value of 3.7 renminbi to 1 US dollar, and then in 1989 to 4.7 renminbi.[12] This "experiment in gradualism" eased the transition to a more accurate value for the renminbi and to a market economy, with the swap centres forming a platform for market mechanisms

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[3] "The overvaluation of the currency allowed the government to provide imported machinery and equipment to priority industries at a relatively lower domestic currency cost than otherwise would have been possible." *Ibid*.p.3

[4] Previously referred to as a "traitor and scab" that had fomented "counter-revolutionary schemes" for opposing Mao's economic policies, particularly forbidding inflation (Hung, p.29)

[5] Huenemann, Ralph W., *Economic Reforms*, 1978-Present, Oxford Bibliographies, April 2013, http://www.oxfordbibliographies.com/view/document/obo-9780199920082/obo-9780199920082-0008.xml

[6] Goldstein, Morris, and Nicholas R. Lardy, *The Future of China's Exchange Rate Policy*, Policy Analyses in International Economics 87, July 2009

[7] *Ibid.*

[8] Huang, Haizhou, and Shuilin Wang, *Exchange rate regimes: China's experience and choices*, China Economic Review 15, North Holland Publishing, 2004, p. 336-342

[9] Goldstein, p.5

[10] *Ibid.*

[11] Huang, p.337

[12] Goldstein, p.6

outside of central planning.[13] Finally, following a series of more gradual devaluations, the dual exchange rate system, in all variations, was finally abandoned on 1 January 1994. The price of the official exchange rate was moved to the prevailing swap-market rate of 8.7 renminbi. The rate was moved to 8.3 renminbi gradually over the following year and a half, and then settled there more or less all the way until 2005, even during the pressures of the Asian financial crisis of 1998.[14]

Since 2004, China has committed to gradually moving towards a flexible, floating currency regime.[15] Following up on this, China has revalued the renminbi gradually, and has faced widespread calls for further pushes upward in value from international economic and political circles.

Where We Stand Today

Perhaps the most striking aspect of the academic conclusions on the Chinese currency situation is the entire lack of consensus. There is continuous disagreement on if the renminbi has been held at an artificially low value, and even amongst those that do agree that it has, there is no consensus on by how much. Indeed, there are even some that now say that, if anything, the renminbi is overvalued, and that recent currency flight is to get out ahead of an inevitable devaluation to closer to its true floated market value.[16]

There are of course many who argue that China has been selling renminbi and buying US dollars and euros in order to keep the trading value of the renminbi artificially low, thus giving China an advantage in the exportation of its manufactured products. Feldstein argued that not only is China's currency value being held artificially low, but that the resultant current account imbalances pose four specific threats to the world economy.[17]

The first of these is, always popular in election seasons, the pressures created toward protectionist policies in the countries experiencing the deficit. While thus far the reactions have been largely rhetorical, the imbalances raise threat for 'cascading tariff increases' not unlike those that exacerbated the economic crises of the 1930s. Indeed, as Ge points out, such proposals have been seriously discussed in the US congress.[18]

The second is another reactive policy that can arise from such situations. Countries being subject to these distorted capital flows will sometimes make moves to restrict the inflow of foreign capital to prevent their currencies from further appreciating. Such moves of course serve their primary purpose, but can also prevent productive investment, and can cause a 'misallocation of capital among nations.'[19]

The third threat posed by these current account imbalances is that the flood of capital into economies such as the US push interest rates down to artificially low levels. This could be seen in the lead up to the crash in 2008, as investors seeking high yields moved to unconventional and riskier assets. By pushing down interest rates, these imbalances could be leading to more excessive risk taking.

The fourth threat listed by Feldstein is that the prevention of currency appreciation can lead to inflation in those countries in which demand is excessive. Similarly, preventing depreciation can lead to deflation in those with account deficits.

Y. Wang et al. argued that, while the renminbi was undervalued, China had already taken the necessary steps to allow for the eventual market pricing thereof.[20] They cite specific policy changes in China's capital account control policy that would loosen the state hold on foreign exchange. Such changes included the 150 percent increase in the allowable amount of foreign currency a Chinese resident could purchase ($20 000 up from $8 000). Secondly, Chinese institutions were then allowed foreign currency accounts in commercial banks, and insurance companies with the need for foreign exchange transactions were given permission to invest in foreign securities. Another relaxation was Chinese commercial banks being given permission to invest in foreign securities on behalf of their clients.[21]

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[13] Mehran, Hassanali, Monetary and Exchange System Reforms in China: An Experiment in Gradualism, IMF Publishing, 1996

And Huang, p.336

[14] Tobin, James, Asian Financial Crisis, Japan and the World Economy 10 (1998), Elisevier, p. 351-353

[15] Reuters, "Timeline: China's reforms of yuan exchange rate", Business News, 14 April 2012, http://www.reuters.com/article/us-china-yuan-timeline-idUSBRE83D03820120414

[16] Krugman, Paul, *Small News On The Yuan*, The New York Times, December 1, 2015 http://krugman.blogs.nytimes.com/2015/12/01/small-news-on-the-yuan/

[17] Feldstein, Martin, The role of currency realignments in eliminating the US and China current account imbalances, Journal of Policy Modeling 33, Elsevier, 2011, p. 731 - 736

[18] Ge, Wei, "The Chinese Currency and Global Rebalancing: A Discussion", *from China*: An International Journal, Volume 11, Number 1, pp. 55-74, NUS Press Pte, April 2013

[19] Feldstein, p.732

[20] Wang, Y. et al., Estimating renminbi (RMB) equilibrium exchange rate, Journal of Policy Modeling, 29, Elsevier, 2009, p. 417-429,

[21] *Ibid*., p.427

These policies, the authors argue, will expose the renminbi to sufficient market forces to expedite its movement to its real effective exchange rate. They argue that there has been very little renminbi misalignment over the post-reform era, and that steps such as these will serve the purpose of bringing about full convertibility in a way that makes dramatic command revaluations redundant, or at best only serving as a temporary measure in a process that was unfolding regardless.

Yajie et al. similarly argue that, based on the behavioural equilibrium exchange rate (BEER), the renminbi has largely traded at its appropriate value over the open era.[22] Likewise, Cheung et al., using the relationship between relative price and relative output levels, argue that the renminbi's alleged undervaluation has been "Overvalued." [23]

As said above, though, these views do not represent a consensus. Eichengreen, specifically condemns the conclusion that the undervaluation has been overvalued.[24] Amongst other reasons, he questions the validity of Chinese data used to make the claim. As he states, China has been known to wildly revise its economic numbers, such as the 2005 revision of its purchasing power parity per-capita income up 17 percent for the year, making such claims based upon the data unreliable at best.

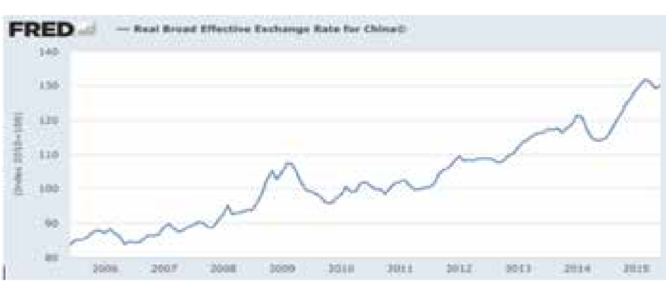
Tung and Baker, long ago argued that China had been valuing the renminbi at least 15 percent below fair market value.[25] They called for a 'maxi-revaluation' of 15 percent, and this just as a way point for moving to a more flexible exchange rate regime in the medium and long term.

Navarro forcefully argued that China was not only manipulating currency prices to its advantage, but that it must be confronted head-on because of this.[26] He claimed that "The most potent driver of China's competitive edge is not cheap labour, as it is commonly believed, but rather a potent set of illegal trade practices," and that "the most destructive, and least understood of China's illegal trade practices is currency manipulation."[27] His paper likens Chinese currency policy to a tariff of 40 to 50 percent on US goods.

Former Governor of the Bank of England Mervyn King has laid out the case that China, having long limited upward market pressure on its currency, will now find that "its exchange rate comes under downward pressure," and recommends the abandonment of the attempt of fixing the exchange rate.[28]

Similarly, Nobel-winning economist and columnist Paul Krugman has followed the developments full circle on the issue. In 2010, he vehemently argued that "at this exchange rate, Chinese manufacturing has a large cost advantage over its rivals, leading to huge trade surpluses."[29] At the time, he concluded that "Chinese mercantilism is a growing problem, and the victims of that mercantilism have little to lose from a trade confrontation."

By 2015, however, the circumstances have changed. First, he points to the appreciation in the relative value of the renminbi, as shown in this graph (fig.1)[30]



Not only has the real exchange rate risen, but the underlying factors of the Chinese economy no longer indicate the necessity of trying to hold down the value of the currency. Indeed, with growth slowing and competition from other emerging markets increasing, in terms of the renminbi" China was destructively undervalued in 2010 but overvalued now."

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[22] Wang, Yajie, et al., Estimating renminbi (RMB) equilibrium exchange rate, Journal of Policy Modeling 29, Elsevier, 2007, p. 417-429

[23] Cheung, Yin-Wong, et al., The overvaluation of renminbi undervaluation, Journal of International Money and Finance 26, Elsevier, 2007, p. 762-785

[24] Eichengreen, Barry, Comment on "The overvaluation of renminbi undervaluation", Journal of International Money and Finance 26, Elsevier, 2007, p. 786-787

[25] Tung, Chen-Yuan, and Sam Baker, RMB revaluation will serve China's self-interest, China Economic Review 15, North Holland Publishing, 2004, p. 331-335

[26] Navarro, Peter, Confront China Now, World Affairs Journal, Washington DC, September/October 2012

[27] *Ibid*., p.28

[28] King, Mervyn, The End of Alchemy: Money, Banking, and the Future of the Global Economy, W.W. Norton and Company, New York, 2016

[29] Krugman, Paul, China 2015 Is Not China 2010, New York Times, August 13, 2015 http://krugman.blogs.nytimes.com/2015/08/13/china-2015-is-not-china-2010/

[30] *Ibid*.

Analysis: Previous Control Now Lost

PWhile the above has demonstrated that there is a lack of consensus on the degree of Chinese manipulation of its currency exchange rate, there is agreement on one aspect: they have historically had the ability to so do. Today, however, that is no longer irrefutably the case.

This argument rests upon three tenets. First, that, when exposed to capital flows, there is no such thing as a truly fixed currency. Second, that China is now subject to the pressures of capital flows. This leads to the conclusion that China, facing new exposures to capital flows, cannot sustain its previous hold on currency mobility, and has therefore lost a degree of control over its own economy.

James Tobin, Nobel-winning economist in the subject of the destabilising effects of capital flows, gives emphasis to the first tenet. Citing the example of the 2008 Asian financial crisis, he states:

> *As general background, remember that a fixed exchange rate, to which a central bank has committed its reserves of hard foreign currency, is always vulnerable. For instance, Korea has promised to pay one dollar for any 1200 won presented to its central bank by anyone, resident or foreign. If people begin to doubt that the Bank of Korea has enough dollars to make good on the promise, they will rush to sell won for dollars. As the Bank's dollar reserves are depleted, it has no choice but to abandon its commitment and the won falls in the market that is, it takes more, many more than 1200, won to buy a dollar. `Fixed rate' is a misnomer; the rate cannot be irrevocably fixed unless the won is abandoned in favor of the dollar, as francs, lire, and other European currencies are scheduled to be merged into the euro next year.*[31]

In short, a fixed rate is only good as long as no one expects it to change. As soon as revaluation is expected, speculative movement of capital will bring to bear great pressure on the state/central bank. The government/central bank can perhaps withstand this pressure temporarily, using its foreign currency reserves to maintain the fixed rate, but – as such reserves are never infinite – cannot so do indefinitely.

The second tenet, that China is more exposed to capital flows today and going forward more than it has been historically is hardly a controversial supposition. As referred to above, China has vastly increased the access to foreign exchange for its citizens, especially its institutions and businesses.[32] The level of exposure was exhibited this year, when in exchange for the renminbi being added to the basket of currencies for special drawing rights (SDR) for the IMF, China had to make further reductions in capital flow barriers. As Bloomberg reported:

> *Xi seems to realize that he paid a high price for the honor of having the Chinese yuan included, starting this October, in the International Monetary Fund's basket of reserve currencies along with the dollar, the euro, the yen, and the British pound. To be included in the basket, China had to demonstrate that the yuan was "freely usable." That forced it to lower some investment barriers—enabling the capital flight now bedeviling the leadership. The Institute of International Finance estimated in October that net capital flows out of China would reach $478 billion in 2015. New estimates due this month could show even larger outflows, the IIF says.*[33]

Thus, China's deepening integration with the world economy and world institutions such as the IMF and the SDR basket inherently mean deeper exposure to capital flows.

The combination of these two truths leads us to the third tenet. Given that China has new exposure to capital flows and the pressures therein, and that there is no such thing as a fixed currency when it is exposed to said capital flows, it follows that China will not be able to maintain the same rigid control over its exchange rate that it has historically enjoyed. Eichengreen and Kawai point out that no matter the scope of China's goals for its currency internationalisation and capital account liberalisation, there are Pandora's box vulnerabilities that come with such degrees of exposure:

> *The risks of evasion and arbitrage – the likelihood that once the PRC moves to basic account convertibility, remaining limits on international capital movements will become increasingly porous and difficult to enforce – should not be underestimated.*[34]

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[31] Tobin, p.351

[32] Wang, Y. et al., Estimating renminbi (RMB) equilibrium exchange rate, Journal of Policy Modeling, 29, Elsevier, 2009, p. 417-429,

[33] McCoy, Peter, "China's Capital Flight: Money is pouring out of China as rapidly as it once poured in. That's a dilemma for Xi Jinping.", *from* Bloomberg, 14 January 2016, http://www.bloomberg.com/news/articles/2016-01-14/china-s-capital-flight

[34] Eichengreen, Barry, and Kiasharo Kawai, eds., Renminbi Internationalization: Achievements, Prospects, and Challenges, Brookings Institute, Washington D.C., 2015, p.12

The move towards a market-based exchange rate, consequently, is treated as more of an inevitability than a choice. The question then becomes one simply of process – or 'sequencing' as it is referred to in this work and Wang, amongst others.[35] It is seen that China's path now has one logical destination, a market-based currency valuation – thus removing that policy arrow from Chinas economic quiver.

IR Interpretation

Now, the task comes to contextualising this result. If China's ability to control its currency exchange regime has been diminished, what does it mean for its place in the international order? In order to explore this, a mixture of IR theories will be applied. First, the classical IR approach of realism will be used, to examine the power implications of this change. Then, the approach will move to critical theory, with world systems theory being used to explore China's position in the global economic order. Then the approach will move on to a Post-Western theory, using the Chinese approach of Tianxia to offer an alternative to the predominant Western slant of traditional IR. Then, the paper will conclude with a mixture of these approaches, adding the modern theory of financialisation, so as to try to bring a holistic close to this contribution to the issue.

For the Western theories, these where chosen, as in McDonald, since "these are normally seen as divergent theories; world systems theory arriving as a critical response to older realist perceptions of the world order."[36] Realism is state-centric, world systems is systemic, and the use of both allows for a suitably representative sample of the possibilities of IR analysis of the matter. First, these theories shall be summarised, as presented in previous work.[37]

Dougherty has given a six-point framework for realist thought that will serve as the working definition for this paper.[38] These can be summed up as: 1) the state is the primary actor, 2) that international systems are inherently prone to conflict, 3) that states have sovereignty – but that "nevertheless gradations of capabilities" exist, 4) that states are unitary actors, 5) that states are rational actors seeking to benefit national interest, and 6) that national interest lays in obtaining and preserving power. It is upon these tenets that realism will be defined in this paper. Consequently, the operation of the international system in realist expectation is, if not predictable, at least comprehendible. States, as the primary and sovereign actors, will make rational choices – within the constraints in which they are held – that will enable them to maximise the power they can attain.[39]

In contrast to the state-centric view of realism, the other theoretical approach to be used in this paper is less confined by boundaries of a geographical nature. These divisions are more economic and, to a degree, cultural. World systems analysis goes beyond the view of a state as a dominant, unitary, and rational actor. The structure of the system is instead divided into core, semi-periphery, and periphery actors, which do not necessarily correspond with state boundaries.

The core, as defined by Wallerstein and Kuznar, comprises areas in which elites control most wealth, technological, and military resources with which to dominate the system.[40] While Wallerstein concentrates on food in this example, others, such as Kardulias have included more "sumptuous precocities" to augment this work.[41]

In order to sustain this position, the core areas use the discounted resources and labour of the periphery. These areas/actors are, often removed from the dominant core culture in the form of language, traditions, and development history. This is a function of "the social organizations of work, one which magnifies and legitimizes the ability of some groups within the system to exploit others".[42]

To bridge this divide, actors within the sphere of the semi-periphery are utilised. These play the role of intermediary,

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[35] Wang, Y. et al., Estimating renminbi (RMB) equilibrium exchange rate, Journal of Policy Modeling, 29, Elsevier, 2009, p. 417-429,

[36] The author has also used these definitions in: McDonald, Terry, "Battered, but Unbroken: Epistomological and Theoretical Challenges to Western IR Theory (Realism and World systems Theory)", European Scientific Journal, Special edition volume 1, June 2014, used here again to facilitate case comparison

[37] McDonald, Terry, "Follow the money: winners and losers in the evolution of global currency mobility regulation", Society and Politics, Volume 10, Issue 1, pp. 170-187, Warsaw, 2014

[38] Dougherty, James and Robert Pfaltzgraff, Jr., Contending Theories of International Relations: A Comprehensive Survey (4th ed.), Longman, New York, 1997

[39] McDonald, *Society*, p.173

[40] Wallerstein, Immanuel, "World Systems Analysis", in Social Theory Today, Anthony Giddens (ed.), Stanford University Press, 1987, and

Kuznar, Lawrence, "The Inca Empire: Detailing the Complexities of Core/Periphery Interactions", in World Systems Theory in Practice, Nick Kardulias (ed.), Rowan and Littlefield, Boston, 1999

[41] Kardulias, N.P., "Fur Production as a Specialized Activity in a World System: Indians in the North American Fur Trade", American Indian Culture and Research Journal, volume 14, number 1, 1990

[42] Wallerstein, p.349

and often feature a mix of the means and capabilities of the core states, such as educational opportunities and core-style institutions, while retaining peripheral characteristics in cultural and labour-division aspects to relegate them to their non-core status. These do not necessarily have to be divided along national boundaries. In China, for example, Shanghai billionaire financiers share a national boundary with peasant rural farmers, many of whom are among the million Chinese who live below the official "absolute poverty" line of $90 US dollars per year.[43]

Analysis:

Realism

If one agrees with the opinion that China has been using its ability to control its currency exchange rate as a means of incurring balance of trade and payments advantage over other states, then it is clear to see how these developments would affect its standing in a realist perspective. China's economic rise since the beginning of its economic reforms has propelled it to major power status. Having so arrived, now some debate whether the long discussed concept of 'peaceful rise' should give way to a 'martial spirit'.[44] The argument is that a military rise should develop from its economic rise.

Here, then, represent how the changes to the China's ability to control its currency exchange rate will affect its status in realist terms. If China's rise was indeed predicated upon the advantages afforded to it by currency manipulation, then does the loss of this ability imply a reduction in power? Does China, with its still-underdeveloped financial services sector, have the capacity to make the transformations necessary to compete on a level playing field, without the advantages of currency manipulation? If not, then China's power, both economic and military, will decline as a result.

World Systems Theory

If one looks at the state as a whole, then China clearly began the reform era as a peripheral state. In fact, the Maoist explanation of China's economic policy could very well have been taken directly from the world systems playbook. The line "Chairman Mao wisely sets forth the principle of maintaining independence and keeping the initiative in our own hands and relying on our own efforts," in referring to rejecting all foreign debt and using an overvalued currency to encourage import substitution, shows that China had an awareness of the means of exploitation inherent in the world system.[45]

In fact, it could be argued that China used its ability to manipulate its currency exchange rate to overcome the trappings of the peripheral states in the world system. By eschewing manufactured foreign goods, China was able to incubate its own industries, and its lack of foreign debt and positive current account balance meant it was not caught in the debt trap and had enough foreign currency reserves to retain a large degree of economic independence.

China has used this opportunity to advance a great deal, but in an unequal manner. As referred to above, China has glaring levels of economic inequality, with the world's highest number of billionaires, and still with many living on less than $90 per year.[46] Additionally, in opening the economy in the era of reform, China has left the protections it had used from systems of exploitation behind in pursuit of integration with the world system. China now has private and public debt, and its workers are exploited for low pay labour and resource extraction, with high-end imports being sent back from the core. Thus, integration into the world system has afforded some Chinese to enter the upper echelons of core status, but in so doing has exposed others to the exploitive cycle that makes up peripheral existence.

Post-Western

While both interpretations above fit with traditional approaches to IR, there has of late been a movement to expand the horizons and perspectives utilised in the study of global affairs. In fact, John Hobson has proposed that the entirety of IR scholarship has been founded upon six myths. They are:

1. *The' noble identity / foundationist myth' of the discipline*[47]

    - Hobson asserts that IR has always had a delusion that it was born in the bloody aftermath of 1919 in the fields of Europe. It was thus thought to be imbued with the noble purpose of avoiding such bloodshed in the future, born pure of heart. Hobson argues that this veils the truth, that since at least 1760 international theory has been Eurocentric and

[43] Moyo, Dambisa, How the West was Lost: Fifty Years of Economic Folly and the Stark Choices Ahead, Douglas and McIntyre, Vancouver, 2011

[44] Kissinger, Henry, On China, Penguin Books, New York, 2011

[45] Cheng, Tsai, China's Renminbi: One of the Few Most Stable Currencies in the World, Foreign Language Press, Beijing, 1969

[46] Moyo, p. 167

[47] Hobson, John M., The Eurocentric Conception of World Politics: Western International Theory, 1760-2010, Cambridge University Press, 2012

worked to defend and celebrate the West.

2. *The 'positivist myth' of international theory*

    - This is the myth that IR theory has a foundational 'value-free epistemological base'.[48] Hobson states that this is undermined by Cox's "well known critical theory mantra, that 'IR is (almost) always for the West and for the Western interest'." He quotes Keohane referring to the idea of humanitarian intervention being necessary because the 'politics of malign neglect' would "deny the backwards East the privilege of developing into an advanced Western form." [49]

3. *The 'great debates myth' and reconceptualising the idea of the clash of IR theories*

    - Here, Hobson says that the much celebrated 'great debates', such as realism versus idealism, or positivists versus post-positivists, are not actually particularly great. He states that these are all minor variations on the same underlying themes, and that, viewed from a non-Western lens, the differences are miniscule.

4. *The 'sovereignty / anarchy' myth*

    - Here Hobson argues that the underlying basis for this myth, that all states possess sovereignty in an anarchic system, is a falsehood. He says that Western states have been granted an implied hyper-sovereignty. Eastern states, alternatively, have at best a conditional sovereignty, which can be withdrawn if "civilized conditions are not met". [50]

5. *The 'globalisation myth'*

    - Here the myth presented is not that globalisation does not exist, but that it is a modern phenomenon. Hobson posits that it has been around since at least 1760, and that it could easily just be called Western opportunism in the mission to recreate the world in a Western image. This still rings true, says Hobson, for post-1989 liberal internationalists like 'end of history' Francis Fukuyama, who preach a similar form of Eurocentric paternalism.

6. *The 'theoretical great traditions myth'*

    - Here, Hobson speaks of the 'epic rendering' of the great traditions of IR theory. He posits that in presenting theories such as realism as continuous strains of pure intellectual thought that can be traced from Thucydides to Kissinger is another falsehood that glosses over large differences in the name of convenience and fitting the Eurocentric metanarrative.

Given this, it is thus beneficial to move outside of Western influence to gain an alternative perspective on the issues presented. Thus we move to the Chinese concept of *Tianxia*.[51] Its literal meaning is a combination of tian – heaven, and xia – under; so, in essence, it means that which is under heaven. Its more nuanced application, though, is that of a system of order in world affairs. In this system, China is the centre of the world order, in a political system of unequal but independent nations. Nations can choose whether or not to enter this arrangement of their own volition, but if they do, they must acknowledge their inferior status.

In its modern incarnation – purely theoretical in a utopian sense – the idea is to move beyond a world in which the nation state is the highest entity. There cannot be world order, so it is explained, unless the world itself is the highest level. In practice, it is not clear exactly what is meant, except that there is a decided idea of non-values-based international cooperation, but is formed around the Chinese cultural philosophical and historical ideas.

In terms of the issue at hand, there are some inconsistencies – in that China's mercantilist approach hardly lends itself to a harmonious global order. Nonetheless, on examples such as human rights, China has been an advocate for allowing states to decide their own internal affairs. Perhaps China's own design for its own economic system, particular to its own historical circumstance, would not be at odds with other states, running their affairs as they see fit, but without interstate conflict.

Financialisation

It is most useful to explain these events and lessons through the lens of financialisation. This is a newer theory in the context

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[48] *Ibid.*, p.17

[49] *Ibid.*, p.18

[50] *Ibid.*, p.19

[51] Chang, Chishen, Tianxia system on a snail's horns, Inter-Asia Cultural Studies, Volume 12, Number 1, Routledge, 2011

of IR application. Originating from Epstein, it is the idea that financial markets, financial institutions, and financial elites and their motives are increasing in importance in the operation of the economy and its governance.[52] It is Streek's and Mair's application of this concept though that has paved the way for its use in this project.[53] In these, political and popular control of the economy has increasingly given way to 'expert governance', so that political parties, left and right, are reduced to tinkering and social issues, as opposed to fundamental questions of the organization and goals of this now 'financialized' economy.

Now, financialisation had been mostly concerned with the loss of democracy and of democratic governance. Of course, in China this has not been the system going into the reform era, or since. Nonetheless, there are still issues of economic sovereignty and self governance at play, not matter the domestic political system. While the citizenry has not been allowed to vote, the government has had the insular ability to run its economy as it sees fit. Now, through the integration with the world system and incorporation into global economic institutions, the levers, such as the ability to control the currency exchange rate, have been removed from domestic hands. The process of financializtion is not about the domestic system of governance – it is about the end result – the removal of the option of opting out of the dominant global economic order from the hands of any political party, actor, or governing body. Financialisation is about the removal of all threats of resistance to the global economic order. Through the integrative processes discussed above, China has exposed itself to the conforming pressures of global capital flows. Having reduced its capacity to set its own exchange rate has thus fully removed China from the original Maoist ideal; it now is – for better or worse – subject to the forces and flows of the world economic system.

Conclusion: Dropping the reins

It has thus been demonstrated that China has had a tight grip on its currency pricing, but that such a grip is no longer possible going forward, as China experiences increased capital flow exposure and finite intervention capabilities through the process of finanicialization. As explained above, trying to retain a fixed exchange rate has already cost China $700 Billion USD in the early part of 2016; even China's vast foreign currency reserves are not infinite and thus cannot maintain such a pace indefinitely.

Moreover, China's integrative moves have allowed for increased capital flows – which, as seen above in Tobin's description of the Asian currency crises of 2008, offer vulnerabilities when currency devaluation is expected. Now, as "export-led growth is no longer a viable strategy for a large emerging market because Europe and North America cannot sustain the domestic demand required to import so much," China will find the RMB under downward pressure.[54] As currency markets sense that devaluation is inevitable, it costs increasing amounts to maintain a fixed rate, escalating until the point of unsustainability.[55] Ergo, China has already lost the ability to exercise the control over RMB valuation that it previously enjoyed, both in economic and IR terms described above, as if it does not move RMB valuation to true market value, the market pressure will do it for them. Thus, herein China sees the eventual result of financialisation.

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[52] Epstein, Gerald, "Financialization, Rentier Interests, and Central Bank Policy", Paper prepared for PERI Conference on "Financialization of the World Economy", December 7-8, 2001, University of Massachusetts, Amherst, http://citeseerx.ist.psu.edu/viewdoc/download?doi=10.1.1.372.2039&rep=rep1&type=pdf

[53] Streeck, Wolfgang, "How Will Capitalism End?", *from* New Left Review 87, May-June 2014, London, and

Mair, Peter, Ruling the Void: The Hollowing of Western Democracy, Verso Books, London, 2013

[54] King, p. 362

[55] Tobin, p.351