

# Newsletter



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## The Outlook for the Tri-polar World and the Japan-China Relationship<sup>1</sup>

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With the coming of the 21<sup>st</sup> century, the global paradigm is shifting dramatically, and it is high time for Japan to plan for the future based on a long-term perspective.

### **1. Changes in the US uni-polar Structure**

We had experienced a bi-polar structure during the Cold War, split between, so to say, a Soviet sphere of planned economy, and the US sphere of democracy and market economy. When the Berlin Wall fell in 1989 and the Soviet Union collapsed in 1991, the bipolar structure changed into a uni-polar world. The collapse of the Soviet Union can be described as a victory of democracy and market economy over centralized, planned economy, which meant the establishment of an American hegemon. In the 1990s, the US truly held a hegemonic position in a huge range of areas from economy, military power, foreign policy, technology to popular culture. This uni-polar global structure is still the underlying order today.

However, needless to say, changes are occurring even in this uni-polar world. The most significant development among them is the evolution of the EU. The original objective of the EU was to bring Germany and France together and avoid further wars in Europe but the concern that Europe might sink between the two superpowers soon became an added incentive. It was a

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reflection of a European survival instinct, to find a way to avoid being sunk into a ditch. The project took a concrete form with the creation of the European Coal and Steel Community (ECSC) in 1952, the European Economic Community (EEC) in 1958, then the European Community (EC) in 1968, and finally the European Union (EU) in 1993. Half a century into the project, Europe at last adopted a single currency, the euro, which has been successfully in operation for the last five years.

The EU has also developed geographically, admitting ten new members in May 2004, most of them former Communist countries in Central Europe, and is now a group of 25. Though it is still an uni-polar world, the EU has achieved a significant development and has strengthened its voice in the international community.

The second notable change is the growth of Asia, especially East Asia. From the end of the Second World War until about 1990, Japan had achieved notable economic growth, becoming the second largest economy in the world. This development stimulated the region, and with Japan leading the pack, NIES countries flew off to a start, so to say, in a geese-flying formation. Although Asia was hit with an economic crisis in 1997, the regional economy had expanded dramatically until then. China is following the course and under the open reform policy, it is showing remarkable progress. India could be next in line. These developments in Asia, especially in East Asia, are the another change that has been occurring in the current global structure.

In view of these developments, the global economy is now often described as tri-polar; the US, the EU and East Asia. But the gap between the first, the US, and the second, the EU, and that between the second and the third, East Asia, are still very wide and this fact must not be overlooked. Let us observe how this tri-polar world will operate say in the next quarter of a century, until about 2030.

To come to the conclusion first, I believe the relative predominance of the United States and the NAFTA region will not change. One of the reasons is that NAFTA will maintain youthful demographics. Looking at the US and Mexico, population as a whole is growing and the working population will increase. The United States by itself is calculated to have a population of over 400 million by 2030. Added to this population projection, the innovative strength of the market with

its flexibility, and free and rigorous competition is likely to continue. If so, the relative predominance of the US should almost be intact after a quarter of a century.

## **2. Challenges facing the Tri-polar World**

On the other hand, however, various difficulties are likely to develop in a tri-polar world which may not have existed in a uni-polar world. Since the terrorist attacks of September 11, 2001, the Islamic world has become a significant influence in the international community. Islam and terrorism should not be confused, but it is true that since the terrorist attacks, the Islamic community, which had not been influential before, has become a force to be recognized. At least from the view of the Islamic world, the United States is the current opponent. The antagonism of not only the Muslim world but of the international community towards the uni-polar rule of the US is becoming ever more serious over the war in Iraq and the post-war management. Although the United States is still the hegemon in the areas of economy, military power and technology, its position as the unchallenged leader of the world seems to be weakening. Though it has power, it is losing the credibility to lead. This means that although the United States may maintain its relative predominance, its leadership position may weaken in the future.

On the other hand, the EU, which is creating friction with the US over dealings with the Islamic world, is likely to continue its expansion and will eventually reach the Central and Eastern Europe as well as part of the Muslim countries such as Turkey. There is a strong desire within Europe to expand the area into Eurasia, even including Russia and the former CIS countries in Central Asia. But when it comes to whether Europe will become the force to replace the United States as the leader of the world, that is questionable.

First, the EU does not have an integrated military. As the Europeans themselves admit, when it comes to military power, the US power is far beyond the European reach. Even if Europe expands to the east, it is most unlikely to have a military power that would enable Europe to be an integrated pole. Second, the more the EU expands, the more likely their various internal differences will not be solved. Even now, although most members have adopted the euro, and there is a single monetary policy and a single market, there is still no single fiscal policy. There are other important unsolved issues on markets, especially labor market regulations, and other areas that create considerable obstacles to a truly single economy.

The EU does have a larger population than the United States and the total sum of the economy is equivalent to the size of the US. The euro-denominated bond market is growing rapidly and in some areas the euro market has overtaken the dollar market. The key question is: when will Europe recognize that it constitutes a pole in the world and have the will to play a leadership role. The EU does not have that recognition now. Its attention is concentrated on expansion and deepening of integration, and it lacks the kind of awareness of a leadership responsibility that the US has. It is a huge question as to whether Europe will come to have that kind of will and desire in the future, such as in the next 25 years. I think it would be very difficult for Europe to have such a clear awareness, one that the United States does have. In the first place, Europe needs to be politically integrated in order to have such a leadership capability but such political integration will not progress easily and it would be even more difficult as Europe expands. And even if Europe integrates politically and adopts a federal system, I doubt that it would develop the awareness of a leader.

Will the issue of dealing with Islam create an antagonistic relationship between the US and Europe? I think that unlikely because there is a blood relationship between the US and Western Europe, the center of the EU. Europe at least shares the belief in the paradigm based on democracy and market economy just as it did during the Cold War. This will not change even if Russia and the Central Asian countries join the EU. In other words democracy and market economy will not change to something else with the expansion of the EU. That is why I believe the US and Europe will not become opposing poles. Economically, with the further enhancement of globalization, mutual dependence in such areas as trade and investment will strengthen, creating a competitive relationship but not an antagonistic one. Concerning the role of the dollar and the euro, the big question is when Europe will have the clear policy objective of replacing the dollar with the euro as the global key currency. For the time being Europe will not have such a clear desire. I think that for quite a long time Europe will concentrate on strengthening internal coherence and integration.

But there will be global problems where Europe will be involved, including those with the Muslim world, though much depends on where that world heads for. There is also the question of the relationship with China. There will continue to be frictions between the US and Europe on such global relations and issues. Opinions could be even more sharply divided in the future.

This means that although the American hegemonic system will continue, the global situation under that system may likely become more and more unstable.

### **3. Where is Asia heading ?**

So where will Asia, the third pole, go? To concentrate on East Asia, intra-regional economic activities have increased tremendously in the last 10-20 years and this tendency for active exchange in the real economy will continue. There are currently energetic developments towards integration such as the creation of free trade areas and this tendency is likely to continue in the future. The financial mutual support network is developing as is seen in the Chiang Mai Initiative.

Will such deepening of intra-regional relationships in the real economy lead to political integration? If not political integration, when will the region move to a more fundamental economic integration, such as adopting a single currency? Compared to North America or Europe, East Asia has many more hurdles on the way to that goal. For example, NAFTA has the United States as a strong core and the other countries are like satellites in its orbit. In Europe, although the situation has been changing with expansion, it is basically a group of comparable countries led mainly by Germany and France. There is a clear pattern of a vertical integration structure in North America and a horizontal one in Europe.

However, in Asia, it is difficult to have either a horizontal or a vertical pattern. Still, the critical factor in portraying the future is the kind of relationship that will be formed between Japan and China, the two largest countries in Asia, and the balance of power between these two countries and ASEAN, which is a group of medium to small countries. Integration of a region cannot be achieved without a distinctive leader. There is the US in NAFTA, and Germany and France in the EU. Germany and France were once enemies for a century but now have a strong bond, and they share a clear will to lead Europe to closer integration. Unless there is a country or a group of countries that is willing to be the core of integration, it is very difficult to integrate a region. It is no use hoping that countries will integrate naturally.

The economic ties between Japan and China are strengthening in both trade and investment, and the overall bilateral relations are deepening. Some hope that such relations will grow further but

when we think about the future of Asia, it is difficult to see the development of this relationship in terms of the real economy and extended exchange can be the decisive factor for integration in Asia.

#### **4. Who will be the leader in Asia in 2030?**

This naturally leads to the question of who will become the leader of Asia in 2030. The majority of people in the world, except in Japan, do not seem to doubt that China, not Japan, will be the leader by 2020. This question has hardly been asked outright in Japan. I should say that there is a tendency not to want to face this question in Japan. The impressive economic growth of China in recent years is the main reason why most people think that China will be the leader of Asia by 2020. As is often quoted, if the Chinese economy continues to grow at 9% annually, it would overtake Japan in 20 years. In the following ten years, it could even match the American economy. Quite often the future is argued on the basis of such simplistic notions of economic size.

I believe that the possibility that the Chinese economy will overtake the Japanese economy in 20 years' time is 50-50. First, it is doubtful whether China can maintain present high annual economic growth for the next 20 years. It is also well-known fact that the Chinese economy faces many problems. Then even if it grows at that pace in size, per capita income will be only about one tenth of that of Japan because China has about ten times more population than Japan. For all these reasons, the possibility that the Chinese economy will lead Asia is certainly not 100%, but somewhere around 50%.

In addition, a country cannot be a leader just from its economic power. It must at least have international influence through foreign policy and military power. From that point of view, China has already surpassed Japan. I suspect that many people in the world have already placed a heavy weight on China judging that its influence will grow in various areas beyond economy where there is a strong probability that the Chinese economy will grow faster than that of Japan. Japan's biggest problem is the population projection. If, as it is said, the Japanese population ages rapidly and the number decreases with low fertility, there is no question that China will increasingly gain ascendancy while Japan will face a relative decline.

With this background in mind, what kind of leadership structure will there be in Asia around 2030? One possibility is China as the leader. The other possibility is Japan putting up a good fight to remain so. But neither can unequivocally be the leader. This means that we must think

of the possibility of a joint leadership. Is such an arrangement a real possibility? For example, can Japan and China have a similar relationship to German and France, or the United States and Great Britain? Both China and Japan must seriously contemplate the possibility, but I believe it would be extremely difficult. China is now on the rising tide of history and the underlying sense of nationalism is extremely strong. Some say that this is a pure form of nationalism based on its tradition, history and imperialism. I agree with that assessment. If this is correct, then there is no way that China will accept a dual leadership with Japan following the German-French or US-UK pattern. This means that even if the Chinese do not say it out loud, China's national objective must be to become the leader of Asia.

##### **5. How should Japan deal with China?**

What is the choice for Japan? Even if we want to tell the Chinese that we will not let them be the sole leader of Asia, what can Japan actually do to maintain its current leadership role? What Japan can actually do is questionable when we consider the population projection, productivity increase and market size.

Japan, consequently, has to think hard whether it can accept China's leadership in Asia, and if it does what the bilateral relations will be, or to be more precise, what Japan wants to do about it. These questions cannot be avoided to address.

Of course, when we talk about leadership in Asia whether it will be China or Japan that plays the role or whether it would be a joint leadership, we must also bring ASEAN and Korea into the picture. There is a possibility that the two Koreas will integrate in the next 25 years, becoming the third largest force in Asia. But China and Japan will still be the key players. The ASEAN countries have a keen interest in how the relationship between the two heavy weights in Asia will develop. As a group, they may want to be the balancing power between the two big powers. So when Japan and China seek the leadership role, they must take into consideration the relationship with ASEAN and with South Korea.

In view of these circumstances, it is hard to imagine that a definitive structure will be created in the next quarter of a century. Instability in some form will continue and in some instances, instability will deepen. On the other hand, mutual economic dependency is likely to increase and, as is already the case, the survival instinct of the region sandwiched between NAFTA and the EU

may serve to be the integrating force. But even when these factors are brought into the overall picture, I believe that stability in Asia will be hard to achieve unless Japan-China relations are somehow defined. From the economic perspective, even though dependency will increase, one cannot ignore the areas of competition. The most serious of these is energy. When we look back, one of the key reasons for World War II and especially the war in the Pacific, was natural resources-- the Japanese need to secure oil and iron ore. Depending on the kind of balance among China, a united Korea, Japan and furthermore possibly India in securing the energy resources, it could be a source of serious instability.

I cannot be too optimistic about the future of Asia for all these reasons. For Japan, the biggest challenge is the relationship with China, not just the furtherance of economic exchanges but how to construct a relationship while focusing on the leadership role in Asia. This is an immediate problem to be tackled. I am deeply concerned that Japan is putting its head in the sand hoping that this question will somehow go away.

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