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Deglobalization and China's Reaction to the Process in the Light of the Ukrainian War

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Abstract

The paper attempts to answer the question of how China is responding to the current deglobalization trends that seem to be accelerating in recent months following the outbreak of war in Ukraine. At the same time, we point out that this process may have already started after the Global Financial Crisis (2008-2009). In the first section, the author describes the current deglobalization process, its origins, and elements. The next section revisits the concept of the developmental state and also demonstrates why the concept is critical to understanding and interpreting China's behavior and responses to deglobalization. In the third section, entitled "In the Age of Parallel Worlds", we examine the hypothesis that implies the emergence of parallel worlds and the possible implications of this scenario for the policy choices of the main actors—the United States, China, the European Union, and Russia. The two aspects we have chosen for closer examination are finance and supply chains. The paper concludes that the process of deglobalization could continue in the coming years, but that the fundamental interests of the main players will still save us from the worst scenario, the emergence of a bipolar world. At the same time, it was also pointed out that the United States might be more interested in "splitting up" the world economy and separating a part in which American dominance can be maintained, while China might play a different game, more concerned with accelerating the globalization process and maintaining state intervention capabilities.

Keywords: *China, Ukrainian war, deglobalization, economic blocs*

1. Deglobalization

As of 2016, the Trump administration's withdrawal policy has not supported economic globalization in the world. In addition, the trade war with China, the deliberate decoupling from the Chinese economy, efforts to "bring manufacturing home", and the Brexit reinforced deglobalization. At this point, China had the opportunity to successfully launch new institutions and initiatives (Belt and Road Initiative, China-CEE cooperation, etc.), some of which reordered the global order and some of which showed that initiatives could come not only from the West but also from the East.

The sanctions against Russia in 2014 and 2022 reinforced the trend toward deglobalization that was already present in the system. But what is the connection between deglobalization and China's economic development? We need to understand is that China's intentions are best understood by looking at the country as a particular version of the Asian developmental model (see Section 2). One of the main features of the developmental state model is export-led growth. The basic idea behind the Belt and Road Initiative (BRI) is to open markets for Chinese goods by building the necessary infrastructure to get the products to the target markets. As the EU is China's most important trade and investment partner on the Eurasian continent, the EU is the most important region of the BRI. The need for such infrastructure is evident in the vast Central Asian and Eastern European regions that link China and Western Europe, the two hubs of global trade. If there is one country in the world economy that needs more globalization and can benefit from globalization, it is China. The problem, however, is that since the 2010s, there have been several factors that, intentionally or unintentionally, have promoted deglobalization: (1) China's economic success, (2) populist movements, (3) efforts to decouple China from the rest of the world, (4) the 2020-2021 global pandemic, (5) economic sanctions against Russia, and (6) the establishment of parallel international institutions.

1. *China's economic success* challenges the existing world order. The success and size of its economy has meant that its very existence challenges current global multilateral trade and investment institutions. To protect the global order, Western countries restricted China's access to this institutional framework and impeded China's economic integration. (At the same time, we must add that China's reforms also stalled after it joined the WTO in 2001.)
2. Since the 2010s, *populist movements* in power have actively helped create barriers to international trade and capital flows. The withdrawal of the United States from several international commitments (in 2017 from the Trans-Pacific Partnership and the Paris Agreement, in 2020 from the World Health Organization), the introduction of a screening mechanism for foreign direct investment (FDI) in EU member states has exacerbated these problems. Although the Biden administration reversed these withdrawals, the genie was out of the bottle, and the institutions of the global order were challenged, beginning the process of redesign.

3. U.S. efforts to *decouple China* from the global economy have been clear since Trump launched the trade war in 2016. Although the original goal of pushing China back in international trade and reducing the U.S. trade deficit has not been achieved, the policy has helped to re-shift trade routes. But we must understand in this context that geopolitics only distorts market conditions and we, the consumers, end up with more expensive products and services. Moreover, we can add that a bipolar world means bipolar markets and the inability to achieve the optimal scale of production necessary to lower the cost per unit of output.

4. Deglobalization received a new impetus from the *global pandemic* that broke out in early 2020. Not only did the lockdowns restrict economic activity and cause a collapse in global trade and a decline in GDP, but they also prompted countries to focus on supply chain security and to revise these policies to rely less on economic cooperation and to prioritize (at least regional) self-sufficiency, although it remains to be seen whether that is a reasonable and feasible policy. Although the restrictions were relaxed in 2021 and 2022, the fear remained and changed the economic policy decisions. We should add that China's continuation of the zero-COVID policy has the same effect whether it is intended or not.

5. The Biden administration's *economic sanctions* during the Ukraine war support deglobalization. Intentional and forced decoupling from Russia (and Russian energy and raw materials) may be an effective foreign policy, but it will create trading blocs in the global economy unless the policy is reversed after the war.

6. The decoupling of Russia and China drives these two countries together, whether they want to deepen economic integration or not and it also encourages *the establishment of parallel international*

> *institutions*. And there is another aspect: the economic sanctions against Russia have shown the world how vulnerable it can be when it relies on the financial and economic infrastructure built and managed by the United States after World War II. The temptation to create and participate in parallel international institutions is growing, ultimately leading to a breakdown of the world order in terms of trade, investment, technology, and financial infrastructure. The Belt and Road Initiative does not include the US, Canada, Australia, and New Zealand. The BRIC bank (New Development Bank), the Asian Infrastructure Investment Bank (AIIB) provide countries with alternative financing opportunities while the International Monetary Fund, the World Bank and the Asian Development are mainly dominated by the U.S. and its allies.

All these factors have led to a slowdown and possibly a reversal of globalization. Between 2008 and 2022, this situation created a power vacuum in Central European countries that was not filled by any country. The war with Ukraine showed that Russia wanted to fill this vacuum but did not have the power to do so, while the U.S. had the political, economic and military power but did not want to fill this vacuum—at least not until the war in Ukraine. Later we will see if it is capable in the long run to stand by the European Union, which was apparently not prepared for any kind of geopolitical, let alone military, conflict in the region.[1] Although there are more positive voices on this issue, we do not believe that the EU's assertive response to the war would show Europe's awakening to its superpower potential. German Lopez elaborates on this idea and summarizes the possible consequences of this awakening as follows, "One way this could play out is through Europe more aggressively protecting itself. That could help free up American resources now devoted to European security, which would in turn allow the US to embark on a long-promised refocus on Asia to help counter China.” (Lopez, 2022) Another possible consequence of the war is that the militarily threatened and economically weakened EU—as an unintended consequence of sanctions against Russia—will be more likely to pursue a foreign policy that serves U.S. interests in the region and globally. Indeed, one of the consequences of the war could be a Europe that is more hostile to China.

Ironically, what China wants from the region is trade—the flow of investment and technology in both directions. China has neither the need, nor the will, nor the power (political or military) to act as a major power in the European region. Rather, what China needs is to open up new markets and internationalize its economy.

2. The “Developmental State” Narrative and the Link to Globalization

The reason why I touch upon the “developmental state”[2] narrative is that China can be viewed as a special version of the original development state model. This way China’s behavior and future strategies can be more easily forecast and interpreted. One of the features developmental states share, is the focus on export-driven growth.[3] Export-focused growth requires an open global economy, where trade and investment do not face serious impediments. Chinese efforts to further open up the world economy have inevitable consequences, at the same time, Chinese attempts to maintain reaction capability in the macroeconomy are also integral part of the Chinese development strategy.

China’s further development needs more globalization in order to maintain the speed of the catch-up with the West. That being said despite Chinese efforts to focus more on private consumption, as engine of GDP growth. The dual circulation strategy[4] which is often interpreted as an inward-looking economy policy[5] did not bring the wanted results in the sense that China's growth would come more from domestic sources, the rise of China's share in world exports in merchandise good could not be stopped, while this figure—based on Statista database—was 12 percent in 2019, it increased to 15 percent in 2021.

The debate about the "developmental state" has been forgotten in academia because it has been argued that globalization has rendered states weak and powerless, and thus the days of the intervening state are over. Yet today, after the Covid 19 pandemic, states appear stronger than ever. Interventions in every segment of the economy have been shown to be possible, and economic activities are being regulated to a degree that no one thought possible. Questions have been raised about who can and cannot provide technology-intensive services. Instead of the attraction of FDI, the rules of FDI screening are being debated. Bringing home global supply chains is fiercely debated. All this requires clear and strong interventions, and these interventions are also part of the economic development strategy. But we have to understand that strongly intervening state in the economy does lead necessarily lead to protectionism as it was often the case in earlier decades—see the example of Argentina in the 1970s—but intervention can go in hand with export-driven growth, the efforts to open other markets and the will to more globalization.

This narrative of China broadens the picture and brings us closer to the core content. In this understanding, the real question is what China is as a country in the modern world, how we define its political and economic structures, and whether we can find similar models in the world. The two focal points are the changing role and power of the state in a globalized world and the question of a model or parallels in the world that might give us clues about what to expect in the later stages of China's development.

It has often been argued that the main reason for cooperation with China is the changing nature of the global order, in which globalization, the argument goes, would have changed the attitudes of the main actors, the states. Jiang Ye, a professor at the Humanity College at China's Shanghai Normal University, claims that China seems more willing to cooperate than the established powers: "But for all the strength of states as the principal actors in the international system, the dominance of states as the focus of political authority is declining with the impact of globalization on the international system since the end of the Cold War." (Ye, 2002) In the light of the war in Ukraine, the US-China trade war, we can raise doubts that the nature of the global order would have changed the attitude of states, moreover, what we can witness now, it the return of the geopolitics, balance of power games.

The Chinese economic model is unique due to the size[6] of the country and its historical development, although it bears a strong resemblance to the original developmental state model followed by other advanced Asian economies. The model can be used efficiently as a lens through which to view the Chinese economy, and the resemblance is even more striking when one considers how much the global economy has changed over the decades. Therefore, in our understanding, the Chinese economy can be viewed as a special case of the developmental state in the 21st century. The differences between China and the three original models of the developmental state would not be outstanding if one did not consider the freedom of maneuvering room for economic policy which comes from the size of the economy.

Why is the developmental state model important when it comes to understanding China's responses to the war in Ukraine, and its efforts to maintain globalization? It provides us with a model in which strong state intervention with export-driven growth are extremely important explanatory factors. The developmental state model can also help us understand why the absence of democratic institutions may not necessarily impede China's development, but rather has the potential to fast-track it.

Having reviewed the main points of this model, let us next examine how conditions would change if one of the extreme scenarios, a bipolar world, emerges!

3. In the Age of Parallel Worlds?

The hypothesis of this section is that Russia and China as a consequence of Western economic sanctions could form an economic bloc, the Eastern bloc, while EU member states, the United States, the United Kingdom, Australia and Japan could build an antipode and form an Eu-American bloc or Western bloc.

According to our hypothesis, the passage between the two economic and technological blocs would remain, but not only trade in goods and services would the self-sufficiency withing the blocs include but parallel financial worlds, infrastructures, and tech-eco-system would rise due to geopolitical considerations. A closer look at the blocs in our hypothesis shows that there are four similarities in the relationships of the players to each other.

— Both blocs are built on the cooperation of a stronger and a significantly weaker player. The EU is the weaker partner in the Western bloc and Russian in the Eastern bloc, while China and the U.S. are the significantly stronger partners in the blocs.

— The other similarity is that Russia and the EU are supported by the cooperating other player in the area, where these are extremely weak.

China support Russia economically, while the United States offer security guarantees to the European partners.

— The third similarity is the weaker partner pays for the support. The costs of war in Ukraine weighs heavily on the European economy and European countries face a very deep recession in the coming months, Russia also pays for the support by opening its market for Chinese companies who have substantially increased their market share in Russia.

— The fourth similarity is the dominant player in both cases uses the current situation to extend its leverage. The United States seems to grab the opportunity to increase its geopolitical clout in Europe and China uses the war for gains in the Russian market.

3.1. Dilemmas in This Scenario

What are the direct consequences of this hypothesized geopolitical situation for the foreign policy strategies of China, the United States, and Russia?

1. *United States*. The United States will most likely have to change its "all fronts strategy." The term "all fronts strategy" means that since 1990, the country has been able to conduct foreign policy in the belief that it has sufficient financial and military resources to intervene and act in virtually any conflict in which its interests were affected. That is no longer the case. The question is in what cases and conflicts does the United States need to engage other countries—and do so with a multilateral approach—and what issues are still so important that the country seeks to influence events unilaterally.

The United States plays a global "Go" (围棋) game, its strategy of recent months was the strategy of isolation of Russia and China. Behind this strategy, the vision is that the United States might not be able to stop the rise of China, therefore it seems to be reasonable to assign a circle of interference for both super powers. This way, China might be contained and hindered from being part of the global institutional frameworks and the country cannot "hack" the system from within and become global leader. This can happen by featuring China as a "villain" and an irresponsible, amoral player, even if occurs at the cost for giving up certain regions.

Slowly declining American economic power gives rationale to this thinking and strategy. Global American military presence is the strongest in the world, however, the capability of simultaneously being engaged in every region and conflict is not present anymore.

This negations process between China and the United States is easier to be described by the question of which regions the United most likely will not fight for. These regions might be Central Asia, Mongolia, several other countries in South and East Asia; such as Laos, Cambodia, Iran. This region happens to overlap with the countries of Shanghai Cooperation Organization more or less.

This strategy is however built upon a flawed interpretation of Chinese strategy. China is not playing the game of "Go" by carving out spheres of influence but is trying to achieve the idealism hidden in the concept of *tianxia* (天下), which envisions a world in which stability and security can be achieved and guaranteed for every actor. At the same time, China sees itself as the center of the harmonious, peaceful world and seeks to ensure the sustainability of China's development. And Chinese strategists are aware that this can be achieved only if the world economy remains open. In other words, China has a vested interest in maintaining international order, while the United States—at least at this geopolitical moment—does not have the same interest.

2. When it comes to *China*, the country needs a thorough cost-benefit analysis, because the Chinese economy can benefit from the isolation of the Russian economy, but the Russian market is not enough for China; economic relations with the United States and the European Union are much more important. For example, China exports ten times more to the United States than to Russia. China is also much less dependent on Russia for resources than Europe. 16 percent of its imported oil, 15 percent of its coal, and 10 percent of its natural gas comes from Russia. In other words, the main supplier is not Russia. (Downs, 2022) The only scenario in which China would commit to Russia in the long term would be if China were also subject to Western sanctions and the West tried to make China a pariah of international relations and the world economy.

3. *Russia*. While we concluded above that Russian foreign strategy is consistent in its opposition to the expansion of NATO and its commitment to building a multilateral global order, the steps of Russian foreign policy are less predictable because Russia may also reach a certain point where it must or can end the war. Either because the Russian economy has suffered enough, the political regime is undergoing internal change, or Russia has achieved its foreign policy goals. In any case, the Europe is facing a new world in which Russian influence in the region will be weakened. The region will not be able to return to pre-war conditions.

4. *The European Union*. The player who would be probably in the worst situation if parallel world emerge, is the European Union. The EU is militarily weak, it needs the protection of the United States, it does

> not have energy sources, it basically relies on external sources, regardless of whether they come from Russia, the United States, the Middle East or the Caucasus region, it depends on other regions. It dismantled its manufacturing it is also dependent on China in terms of manufactured goods. It is a trading giant, which needs global markets and needs globalization. If the bipolar would emerge, the EU's position would significantly worsen and would not have the chance to compete with other player, not to mention the EU's desire to establish itself as "strategically autonomous" (Damen, 2022).

In the next sub-section, we look for evidence of the bipolar world in two sectors, in finances and supply chains. Obviously, we could have chosen other topics, such deglobalization in international trade or the emerge of independent technological eco-system, but finances, supply chains are also related to trade, and independent financing is not possible anymore without self-reliant tech-eco-systems.

3.2. Pieces of a Puzzle: Parallel Financial World

The seeds to a parallel financial world were already planted before the war erupted in Ukraine. Moreover, we could add that sanctions on Russia did not trigger the process, but it speeded up the clear wish of Russia and China to be more independent from the U.S. dominated international financial system.

Under current conditions, the United States dominates the global financial system. Not only is the U.S. dollar the key currency for central bank reserves, foreign exchange, and international trade transactions, but the U.S. can also impose sanctions on countries that do not comply. The vehicle for sanctions is the Society for Worldwide Interbank Financial Telecommunications (SWIFT), the world's largest clearinghouse for cross-border payments, which is dominated by the United States.

One need only look at the case of Russia to see how this works. When sanctions are imposed on a country, it is extremely difficult for that country to trade with the rest of the world.

— According to the latest IMF data (2022Q1), 54.7 percent of global central bank reserves are held in US$, while the Chinese yuan accounts for 2.7 percent of reserves.
— The U.S. dominated currency trading with 88.3 percent in 2019. (National Bank of Canada, 2021)
— According to Rajesh Bansal and Somya Singh, U.S. financial institutions are involved in at least one leg of the trading transactions conducted globally. (Bansal and Singh, 2021: 3)

In a world where political tensions between the U.S. and China are increasing, it is a logical step for Beijing to reduce the influence of the United States on China in this area. It is not only the challenge of the US dollar, but also the internationalization of the yuan that are important aspects for China. We can also raise the question of why China is bound to challenge the existing global financial system.

— First, there is a stark discrepancy between China's role in trade and the role of its currency in global foreign reserves. While China is the world's largest trading nation, the yuan's role as a global reserve is almost nonexistent.
— Second, China will always be in an unfavorable position in a trade war as long as it relies on the U.S. dollar for transactions.
— Third, the U.S. can impose sanctions on countries that do not comply. The SWIFT system can be used to achieve this goal. The list

of sanctioned countries is relatively long. More importantly, most sanctions are imposed unilaterally by the United States, meaning it does not need the support of other major economies to have leverage. This is not new, but the use of SWIFT first took clear shape when the United States sought to choke off funds from terrorist organizations after the 2001 attack on the World Trade Center, and since then sanctions have become a regular tool of U.S. foreign policy.

— Fourth, attempts to meet needs in emerging markets serve as pull factors for new solutions.

The case of Russia shows us that replacing the dollar is not an impossible challenge. The share of the Chinese yuan in bilateral trade between China and Russia has increased from 3.1 percent in 2014 to 17.5 percent in 2020. (Chinese Ambassador to Russia Zhang Hanhui, cited by *Global Times*, 30th July 2021)

Prior to 2022, there were Russian steps too that want to achieve more independence from U.S.-dominated global financial order, see some examples below:

— Expressing concern about the dominance of the dollar in international trade, Russian Deputy Foreign Minister Sergei Ryabkov said in 2017, "We will of course intensify work related to import substitution, reduction of dependence on U.S. payment systems, on the dollar as a settling currency and so on. It is becoming a vital need, ..." (Sergei Ryabkov, quoted by *RFE/RL*, 8th August 2017)

— After the annexation of the Crimean Peninsula, Russia began to implement the System for Transfer of Financial Messages, which can replace the globally accepted SWIFT. The system has been in operation since 2017 and includes 399 banks to date.

— Since 2019, the Russian Central Bank has significantly reduced its U.S. dollar reserves and its holdings of U.S. bonds. Prior to the invasion of Ukraine (January 2022), 11 percent of Russia's foreign reserves were held in U.S. dollars, down from 21 percent in January 2021. (*NIKKEI Asia*, 14th April 2022)

— Meanwhile, Russia increased its yuan reserves from 4 percent to 17 percent. Gold accounts for 22 percent of reserves and the euro accounts for 34 percent of Russia's foreign exchange reserves. (*ibid.*)

— The growing cooperation between Russia and China is also reflected in the distribution of Russian reserves. China is the largest custodian of Russian foreign exchange reserves, at 17 percent. (Germany: 16 percent, France: 10 percent, U.S.: 6 percent.) The largest portion of this, 22 percent, is apparently gold stored in physical form in Russia. (*ibid.*)

— In May 2022, Russia set the price of 5,000 rubles for a gram of gold, making the ruble a gold-backed currency. The former president of Commerce Bank in Chicago responded as follows: "It forces people to go to the Russian central bank and pay gold to get rubles to make the transactions. .... Now the ruble basically recovered, trading 80 rubles to the dollar. And it's because of the way they pegged the ruble to gold." (Jack Bouroudjian, quoted by *Forbes*, 2nd May 2022)

— In the summer of 2021, Russia announced that it would completely remove U.S. dollar assets from the National Wealth Fund. (*CNBC*, 3rd June 2021).

— While 97.1 percent of Russian exports to China were denominated in USD in 2014, this share declined to 22.7 percent by 2020, while the share of the euro (0.8 percent in 2014, 65.3 percent in 2020) and the yuan (0.7 percent in 2014 and 6.3 percent in 2020) increased sharply. (Bhusari and Nikoladze, 2022)

The question is how other countries might respond to the emergence of blocs in terms of financial infrastructure. Wu Xinbo, the dean of the Institute of International Studies at Fudan University concludes that, "The global game around the Russia-Ukraine conflict has sent the following signal: international relations, which used to be dominated by the ideas of cooperation and seeking consensus, are increasingly splitting the world into two confrontational camps and a neutral one. Countries in the neutral camp don't want to take sides. They instead prefer to adopt a pragmatic attitude to decide their positions according to specific matters." (Wu, 2022)

Wu's conclusion may be satisfactory when it comes to African and Latin American countries that can form a neutral bloc. However, the conclusion may be flawed when it comes to European countries, as geographic proximity to Russia pushes these countries into a Western orbit. At the same time, cooperation with China in financing would be more attractive if the yuan's role as an international currency reserve were stronger.

A look at the U.S. dollar shows what the yuan lacks at the moment. In addition to convertibility, China must have a negative current account balance, which means that more money (yuan) is leaving the country than is coming in. And why? This is the only way foreign central banks can accumulate yuan on a significant scale. While the U.S. has run a current account deficit since the mid-1970s, China's balance has been positive since China began its reforms in the late 1970s. This is the point where cooperation between China and the CE region can develop, but we definitely do not see this potential in cooperation between Russia and

Central European countries. And we should add that the international role of the Chinese yuan cannot be strengthened without full convertibility of the currency. IMF Chief Economist Gita Gopinath summarized the requirements this way, “If a country is aspiring to be a global currency, then in that case, you would need to have, you know, basically fully and freely mobile capital, full capital account liberalization, full convertibility of exchange rate, which is not the case right now in China, right now...” (Gita Gopinath, quoted by Reuters, 26th April 2022).

3.3. Pieces of a Puzzle: Parallel Brands, and Supply Chains

At this point it is worth looking at a historical analogy. In interwar periods (1918 and 1938), the internationalization of companies has historically slowed down due to the newly created borders and customs systems. At the same time, the internationalization of companies has continued, and thus international companies with parallel structures emerged. This basically means that companies established subsidiaries in other countries and set up a “mirror company” that manufactured the same products in the target country. This way, they did not have to pay the additional high tariffs. In the case of China, this parallel development of companies existed even before the Ukraine war. Obviously, this development was not due to high tariffs, but to the planned economic development, while this kind of development gained momentum in Russia after the imposition of economic sanctions against Russia.

The above-mentioned historical analogy has strong limitations:

— In the recent case, the parallel company is not established by the parent company, but Russian and Chinese companies establish companies with similar product lines to meet domestic demand and reduce dependence on foreign capital and technology.

— In our case, the development is also driven from two sides, as the U.S. and Western European sanctions or "voluntary" withdrawal from Russia also create free space for Russian and Chinese companies.

— Another limitation is that clustered production makes it difficult to copy product lines. The difficulty lies in the complex vertical integration of today's companies.

— The rise of parallel brands and supply chains could also be limited by the lack of necessary technology. China is much better in the technological realm, while in the case of Russia, this could be the most important factor limiting Russia's room to maneuver.

3.4. Pro and Contra Arguments: The "Bipolar World" Concept

Looking at the figures, some support the "bipolar world" concept:

— Chinese Ambassador to Russia said: "In the first 11 months of this year, the total volume of Sino-Russian trade reached $172.41 billion, up 32% year-on-year, already surpassing last year's annual figure of $146.87 billion and undoubtedly set to reach a new record high." (*UrduPoint*, 22,nd December 2022)

— Before the war, 0.5 percent of trade in the exchange market was nominated in yuan, this figure is 20 percent today. (Prokopenko, 2022)

— The Chinese share in the Russian market of smartphones is up from 50 percent to 70 percent today. (Reuters, 29th June 2022)

— The Chinese share in the Russian car market was 9.5 percent before the war, the ratio is 31.1 percent now. (*Asia Financial*, 8th December 2022)

From all the above factors and the role of Russia, the trends point to the formation of economic blocs. In principle, it would make sense to maintain compatibility of European countries with both blocs. But the possibly of compatibility is different between sectors:

1. When it comes to *trade blocs, parallel brands and supply chains*, this seems to be a difficult task, as the European Union's single market is the decisive factor (e.g., Central European countries cannot import Chinese cars if they do not comply with EU regulations).

2. When it comes to *technological cooperation or parallel financial infrastructures*, the potential seems great, but in any case, cooperation with China rather than Russia has greater potential for the European region. Russia's importance to the region is in energy and raw materials imports. The EU is trying to cut off supply routes from Russia and replace Russia with other countries (Israel, Turkey and Azerbaijan) and boost renewable energy production. Adjusting to this new reality is painful, as it not only requires time and financial resources, but it is coming at a time when it is clear that the world is starving for energy.

However, we also have figures that run counter the "bipolar world" concept. Let us have a look at them:

— Russia is not a super power in economy, its GDP (US$1.5 trillions) is less than the GDP of Guangdong province (US$1.8 trillion). China needs more for its modernization and catch-up process than Russia.

(Chiang, 2022)

— Russia only accounts circa 2 percent in China's total trade, while the U.S and the EU account for 26 percent of China's trade. Russia is not alternative to the EU and the U.S. (*ibid.*)

— Even if the trade between China and Russia would double or triple due to sanctions, this trade would be dwarfed by China-U.S.-EU trade.

— Despite strong development, the Chinese yuan is still far away from offering a full alternative to American dollar.

— China companies and bank are cautious in their dealings, businesses with Russian companies, especially those who can be hit by American sanctions.

- ○ According to Bloomberg, offshore subsidiaries of the Industrial and Commercial Bank of China stopped "issuing U.S. dollar-denominated letters of credit for purchases of physical Russian commodities ready for export", in other words they restricted financing for Russian commodities. (Bloomberg, 25th February 2022)
- ○ In early March 2022, Chinese traders reduced coal import from Russia because financing became more difficult because of Chinese state-owned bank worrying about potential American sanctions. (Downs, 2022)
- ○ The Sinopec paused Russia project because of potential sanctions from American side in March 2022. (Reuters, 25th March 2022)

4. Summary

This paper has been able to show the clash of two different strategies. We have argued that the United States is playing the game of "Go", which is more about dominating certain sectors of the board rather than controlling the entire board, while China seems to be more interested in continuing the globalization that has greatly helped the country in its modernization and catch-up process. The U.S. strategy may be motivated by the belief that the U.S. can no longer dominate the entire board because of its dwindling economic power, so it makes more sense to carve out strategic points that are usually in the middle of the board. We have also shown that China can benefit from greater cooperation with Russia. However, it cannot do without the United States and the European Union as economic partners, so some kind of balance can be found in its responses at different levels (state—business). While the Chinese state seems to put more emphasis on relations with Russia, the "no limits" formulation of cooperation with Russia may cause more headaches for Chinese companies, which are extremely cautious in doing business with Russia. China's multi-faceted reaction shows that its policy decisions may be motivated by the logic of *tianxia*, which would place China at the center of the world order, but it is also willing to "bide its time" in the spirit of Deng Xiaoping. While this conclusion contradicts mainstream thinking, which assumes more assertive behavior by Chinese diplomacy, long-term economic interests will bring Chinese diplomacy back on the old tracks. This does not mean that China's long-term strategy would be abandoned, but a "stop and go" approach will be taken.

Notes

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1. Even before 2022, the reluctance to enlarge the EU to include the Balkans showed that the EU was not prepared to act as a political and economic superpower.
2. Chalmers Johnson coined the term "developmental state" in the 1980s. He tried to show the significant differences between capitalist countries by focusing on Japan. As he put it, "One of my purposes in introducing of the "capitalist developmental state" into a history of modern Japanese industrial policy was to go beyond the contrast between the American and Soviet economies" (Johnson, 1999: 32). He emphasized that the competent and far-sighted bureaucracy greatly contributed to the Japanese economic miracle. Later, the concept "developmental state" became popular, and major contributions were made by Alice Amsden (1989), Robert Wade (1990), and others. Emphasis was put on other elements too: investment and various policy instruments (savings and credit schemes, foreign investment, export processing zones, government interventions to spread technology, etc.), history and culture.
3. Other common features of the model are: (1) *Strong economic planning tools*. Economic planning tools are stronger in China than in the original development states/economies (i.e., Japan, South Korea, Taiwan). Not only

do state-owned enterprises have a larger role in the economy, but the Chinese government still has a double-track price-setting system that distorts market prices while at the same time it helps guide such enterprises into new sectors. Similar systems existed in the 1950s and 1960s in Japan, South Korea, and Taiwan. A special and often noted tool is a devaluation policy that ensures more competitiveness to the domestic companies (Johnson, 1999: 32-60). In the case of China too, the devaluation policy was featured by the United States as currency manipulation. (2) *Cheap labor*. Although academic papers have already pointed out that wages and salaries are rising, the Chinese economy is still dominated by cheap labor. Despite growing wages and salaries, there is still a backlog of cheap labor in China's rural sector. According to the World Bank, agricultural employment accounted for 24.73 percent of total employment in 2020. In advanced countries, this figure is usually less than 5 percent. In addition, the relevance of this factor in competition will decrease as more companies will use robots in manufacturing. (3) *Export-orientation*. It is strong in each developmental state, although the Chinese market is less open than other Asian markets, which is understandable given China's size and different historical development path. Learning from the bad experiences of the 1930s and before, China has always been wary of opening its economy too quickly to foreign capital, while establishing the first special economic zones in Guangdong and Fujian and later expanding this model to other areas of China. (4) *Land reform* as the starting point of economic reform and take-off. Land reform was crucial in each case, as Japan, Taiwan, and South Korea began their respective industrialization processes with comprehensive land reforms completed in the 1950s and 1960s. Although the Chinese have taken steps to modernize the agricultural sector in recent years, the process is far from complete. (5) The question of *bureaucracy and the rule of law*. The connection between democratic institutions and growth rate is not present absent in the case of China, but this connection is not a critical component of the developmental state model. The rule of law and the relative independence of the state bureaucracy, as well as meritocratic, merit-based selection, are more important inherent elements of the developmental state model. However, China's performance in these areas is weak, with corruption in particular currently overly prominent.

4. The “dual circulation” strategy has become a key priority in the government’s 14th Five-Year Plan (2021-2025). The concept of dual circulation was launched by Chinese President Xi Jinping in May 2020. When Xi visited Shenzhen on the occasion of the 40th anniversary of the special economic zone, the “dual circulation” development strategy was once again brought to the center of political discourse. We do not yet know the details, but the emphasis is much more on the domestic rather than the external loop, which could lead to more limited economic activity, including direct investment, worldwide. The move towards self-sufficiency in semiconductors will most likely also lead to a more domestic-oriented innovation strategy. Ken Moak explains the key elements of the development strategy this way: “Key to the ‘internal circulation’ was innovative manufacturing and increased private consumption. The former was to be realized through a massive spending of 1.4 trillion U.S. dollars over the next five years on innovation to climb the manufacturing value chain and become self-sufficient in advanced semiconductors and other technologies. The latter was to be attained by boosting household income through urbanization, turning migrant workers into city dwellers and enlarging the around 500 million middle-class population.” (Moak, 2020) The move mirrors the attitude and the conclusions of Western countries in the wake of the Covid 19 pandemic. The global pandemic drew the attention of political elites to the vulnerability of global supply chains and external shocks such as a global pandemic. Discussion about the “dual circulation strategy” is growing among analysts, as it does not mean much

to the observer and can be seen as a mere description of the economy in which the domestic economy (the second circulation) is linked to the global economy (the first circulation) (Reuters, 15th September 2020). This is the simplest general description of all modern open economies in the world, not a Chinese special case. The *CGTN*'s guidance on this concept emphasizes that internal circulation refers to domestic economic activities and external circulation refers to China's economic links with the outside world. It also concludes that the concept signals China's intention to reduce the role of international trade in the Chinese economy and also to strengthen its domestic economy (*CGTN*, 25th October 2020).

5. Alicia García-Herrero puts this opinion this way: "Dual circulation may sound like a buzzword without much relevance, but it is not. It actually enshrines China's long-standing ambition to become self-sufficient. Such an ambition was made known to the world in 2015 after the launch of China's industrial policy masterplan, Made in China 2025, even though the world at the time was still in full engagement with China." (García Herrero, 2021)
6. The paradigm of the developmental state is not the only attempt to frame and interpret the Chinese model. The term "Beijing Consensus"—a clear reference to the Washington Consensus—was invented by Joshua Ramo, which emphasized three crucial elements of Chinese success: the value of innovation, the rejection of the GDP-per-capita approach, and self-determination (Ramo, 2004: 11-12). Although the term became popular for a short time, it failed to reflect many other characteristics of Chinese economic development and contrast the Chinese experience with the example of Japan, South Korea, Taiwan and Singapore.

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Postscript