China assumes lead on world economy

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By Geoff Dyer in London
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The meeting yesterday between Barack Obama and Hu Jintao, his Chinese counterpart, on the sidelines of the G20 summit had been described by some as "the G2" and marked the first encounter between the two men.

During the meeting Mr Hu stressed China's commitment to strengthen macro-economic control and expand domestic demand, the White House said.

The two leaders agreed to work together to renew world economic growth, strengthen the financial system and establish a "strategic and economic dialogue" group that would first meet in Washington later this year.

The White House also announced that Mr Obama would visit China in the second half of the year.

But with China demonstrating that it now wants to play a much more decisive role in international economic affairs, their meeting may have also set the tone for the rest of the London summit.

While talk of an emerging "G2" ignores the increasingly multilateral basis of financial diplomacy, it does reflect the reality that on a growing range of international issues, little can happen without agreement between the US and China.

For much of the build-up to the G20 summit, China was a quiet participant. However, in recent days China has launched a series of initiatives which demonstrates a desire to move centre-stage. Zhou Xiaochuan, Chinese central bank president, called last week for the eventual replacement of the US dollar as the global reserve currency.

Meanwhile, ahead of the summit, China has established Rmb650bn ($95bn, €72bn, £66bn) worth of currency swaps with Indonesia, Belarus, Malaysia, Argentina, Hong Kong and South Korea - all of which indicate a more confident diplomacy and a larger future role in international finance for the Chinese currency.

The more assertive stance also reflects anger building in China about criticism that its large current account surplus and reserves helped create the crisis and the realisation that its huge holdings of US bonds give it little direct leverage over US policy.

"In my 16 years of covering China I have never seen the country approach an international forum in such a proactive way," says Dong Tao, economist at Credit Suisse. "China has traditionally been passive on the international stage, being a listener rather than an opinion leader, but this time it's different. China wants to make sure [its] voice is being heard."

On the IMF issue, China has been under pressure from the US and the UK to make a substantial contribution to boosting the Fund's coffers, similar to the $100bn already pledged by Japan and the European Union.

China initially pushed back strongly against the idea, arguing that it was still a poor country. Yet over the past two weeks the Chinese line has softened somewhat, prompting speculation that it will inject substantial new funding.

However, Chinese officials have also made clear that their condition is accelerated reform of the IMF to boost China's voting rights. More-over, Hu Xiaolian, deputy governor of the central bank, said last week that a quicker way for the IMF to raise new funds might be for it to issue bonds that China and other countries would buy.

"Having made these points forcefully, the Chinese now realise they would gain a tremendous moral advantage by appearing flexible and providing more resources to the IMF at a critical time for the institution and the world economy," says Eswar Prasad, a professor at Cornell University and former head of the IMF's China division.

Observers had been watching closely the conversation about China's ideas for a new global reserve currency using an IMF currency basket. But the issue was not raised in yesterday's meeting.

Although the same idea is being pushed by Russia and has support from other developing economies, some observers do not believe that China will lobby too hard at the summit for the proposal.

Additional reporting by Jamil Anderlini