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U.S.–CHINA RELATIONS: MAXIMIZING THE EFFECTIVENESS OF THE STRATEGIC AND ECONOMIC DIALOGUE

HEARING

BEFORE THE

SUBCOMMITTEE ON ASIA, THE PACIFIC AND THE GLOBAL ENVIRONMENT

OF THE

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U.S.–CHINA RELATIONS: MAXIMIZING THE EFFECTIVENESS OF THE STRATEGIC AND ECONOMIC DIALOGUE

THURSDAY, SEPTEMBER 10, 2009

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON ASIA, THE PACIFIC
AND THE GLOBAL ENVIRONMENT,
COMMITTEE ON FOREIGN AFFAIRS,
Washington, DC.

The subcommittee met, pursuant to notice, at 1:09 p.m. in room 2172, Rayburn House Office Building, Hon. Eni F.H. Faleomavaega (chairman of the subcommittee) presiding.

Mr. FALEOMAVAEGA. The subcommittee hearing will come to order. This is a hearing by the Foreign Affairs Subcommittee on Asia, Pacific and the Global Environment. The general theme of our discussion this afternoon is "U.S.-China Relations: Maximizing the Effectiveness of the Strategic and Economic Dialogue."

I will get to introducing some of our fantastic witnesses that we have today for this afternoon's hearing. In place of our ranking member, the gentleman from Illinois, Mr. Manzullo, we have one of our senior members of not only the subcommittee, but the full committee, my good friend, the Congressman from California, Mr. Rohrabacher, as acting ranking member this afternoon.

I will begin with my opening statement and then give time for the ranking member for his opening statement. There may be other members who will be coming in, and I will give them the opportunity to do the same. After that I will introduce our witnesses.

At a bilateral meeting on the sidelines of the G–20 Financial Summit in London in April of this year, President Obama and Chinese President Hu agreed that the United States and China would work together to build a positive, cooperative and comprehensive U.S.-China relationship for the twenty-first century.

Central to building that relationship would be the United States-China Strategic and Economic Dialogue, or S&ED, composed of a strategic track led by Secretary of State Hillary Clinton and Chinese State Councilor Dai Bingguo and an economic track led by Secretary of the Treasury Timothy Geithner and Chinese Vice Premier Wang Qishan.

The S&ED would aim to deepen mutually beneficial cooperation on a range of bilateral, regional and global matters from economics, trade and the global financial system to law enforcement, science and technology, education, culture and health.

In addition, the S&ED would bring together senior officials to work cooperatively in settling conflicts and reducing tensions contributing to regional and global instability, including the nuclear programs of North Korea and Iran, problems in Afghanistan and Pakistan and humanitarian issues in other parts of the world.

Finally, President Obama and President Hu agreed that the new dialogue would intensify cooperation on energy, the environment and climate change, with a specific focus on energy efficiency, renewable and clean energy technologies and the achievement of a successful international climate change agreement.

The broad scope of topics to be covered by the S&ED was to be matched by a wide breadth of participation across government agencies. The S&ED was thus an expansion of the strategic economic dialogue initiated by the previous administration and organized under the Department of the Treasury, which had focused primarily on economic and environmental matters.

The S&ED would also provide a comprehensive framework for the more than 50 ongoing United States-China governmental dialogues and working groups that covered issues ranging from aviation and nonproliferation to food safety.

The first round of the S&ED was held in July of this year in Washington, DC, and included senior officials from the State Department, the Treasury, the White House and 12 other departments and agencies of the U.S. Government, as well as senior counterparts from 15 Chinese Government agencies.

President Obama opened the meeting by noting that, and I quote, "The relationship between the United States and China will shape the twenty-first century, which makes it as important as any bilateral relationship in the world."

The Chinese clearly viewed the initial meeting of the S&ED as a great success. In meetings I participated in last month in Beijing, a number of senior Chinese officials all gave very positive assessments of the first dialogue. Vice Premier Wang Qishan said the meeting allowed the two sides to better define further steps they needed to take in responding to the global financial crisis. He called it a huge success.

Mr. Wu Bangguo, the chairman of the Standing Committee of the National People's Congress, noted the unprecedented depth, scope and representation on the two sides, and said the positive work of the first S&ED would allow China and the United States to move forward more effectively on a wide range of issues.

Our Secretary of State, Hillary Clinton, also pointed to a number of positive achievements resulting from the S&ED. In her closing remarks at the Dialogue she noted the United States and China agreed to promote stability in northeast Asia, resume the Six-Party Talks and implement U.N. Security Resolution 1874, address ongoing threats of violent extremism and nuclear proliferation, encourage Iran to live up to its international obligations and work toward peace and stability in Afghanistan, Pakistan and the Middle East.

Secretary Clinton also noted that as a result of the S&ED, bilateral talks on counterterrorism would be held, military-to-military relations would be expanded, and progress was made on a global nuclear summit that President Obama plans to convene early next year.

In addition, the two countries signed an MOU to enhance cooperation on climate change, energy and the environment, which commits both sides to achieving a successful international climate change agreement, cooperating on adaptation strategies and developing practical solutions for both countries.

On the economic track, Secretary Geithner announced agreement on a framework for cooperation on macroeconomic and structural policies designed to ensure more balanced and sustainable global growth, the building of more resilient financial and regulatory systems, the reaffirmation of the two countries' commitment to an open, rules-based trade and investment regime and a pledge to work together in ensuring that international financial institutions are provided the necessary tools and resources to respond adequately to international financial challenges.

Beyond the issues themselves, the Congressional Research Service notes that the S&ED is one of the few venues in which the Chinese Ministers interact with one another across departmental jurisdictions, which is a major benefit. Chinese Government bureaucracies traditionally have been stove piped, with little interdepartmental interaction or coordination.

The interdepartmental nature of the S&ED is important as China's own policy making process has become more complicated now that the bureaucracy does not speak with a single voice and the government must take some account of the views of the media and the public.

Clearly the Strategic and Economic Dialogue covers an impressive array of issues and challenges, and it now stands at the very center of the bilateral relationship.

The United States is now the world's largest economy, while China will soon be second. We are the world's two biggest trading nations and the two leading emitters of greenhouses gases. China is the top surplus country, while the United States, unfortunately, is the largest deficit country. We thus represent the opposite sides of the global imbalances that contributed significantly to the worst financial crisis in generations.

While our two countries may have differences, including a petty dispute over tire imports from China, I believe that Washington and Beijing share interests on most of the important regional and global issues. More to the point, there is no problem in the world that can be addressed adequately without bilateral cooperation, whether it be achieving lasting economic recovery and financial stability or overcoming the substantial threat of climate change and achieving a clean and secure energy future. These are the problems we must address cooperatively.

Fortunately, the bilateral relationship today is in excellent shape. In my view, the first meeting of the S&ED has laid the groundwork for the sort of positive, cooperative and comprehensive relationship both sides seek, and from which both countries, as well as the region and the whole world, will benefit.

Maintaining open channels of dialogue between the United States and China, which the S&ED does, is essential. At the same time, since the S&ED covers such a wide range of topics and involves so many government agencies, unless the process is well managed, it may fail to achieve its promise.

The purpose of today's hearing is to review the results of the first meeting of the S&ED and to examine how the Dialogue can best achieve its worthy goals on the many issues that are currently under discussion between the United States and China.

I would like to turn the time now to my colleague for his opening statement, Mr. Rohrabacher.

[The prepared statement of Mr. Faleomavaega follows:]

COMMITTEE ON FOREIGN AFFAIRS
U.S. HOUSE OF REPRESENTATIVES

STATEMENT OF
THE HONORABLE ENI F.H. FALEOMAVAEGA
CHAIRMAN

before the
SUBCOMMITTEE ON ASIA, THE PACIFIC AND THE GLOBAL ENVIRONMENT

U.S.-China Relations: Maximizing the Effectiveness of the Strategic and Economic Dialogue

September 10, 2009

At a bilateral meeting on the sidelines of the G-20 Financial Summit in London on April 1, 2009, President Obama and Chinese President Hu agreed that the United States and China would "work together to build a positive, cooperative and comprehensive U.S.-China relationship for the 21st century."

Central to building that relationship would be the U.S.-China Strategic and Economic Dialogue, or S&ED, composed of a Strategic Track led by Secretary of State Hillary Clinton and Chinese State Councillor Dai Bingguo, and an Economic Track led by Secretary of the Treasury Timothy Geithner and Chinese Vice Premier Wang Qishan. S&ED would aim to deepen mutually beneficial cooperation on a range of bilateral, regional and global matters, from economics, trade and the global financial system to law enforcement, science and technology, education, culture and health.

In addition, S&ED would bring together senior officials to work cooperatively in settling conflicts and reducing tensions contributing to regional and global instability, including the nuclear programs of North Korea and Iran, the problems in Afghanistan and Pakistan, and humanitarian issues in other parts of the world.

Finally, Presidents Obama and Hu agreed that the new Dialogue would intensify cooperation on energy, the environment and climate change, with a specific focus on energy efficiency, renewable and clean energy technologies, and the achievement of a successful international climate change agreement.

The broad scope of topics to be covered by the S&ED was to be matched by a wide breadth of participation across governmental agencies. The S&ED was thus an expansion of the Strategic Economic Dialogue initiated by the previous Administration

and organized under the Treasury, which had focused primarily on economic and environmental matters. The S&ED would also provide a comprehensive framework for the more than 50 ongoing U.S.-China governmental dialogues and working groups that covered issues ranging from aviation and non-proliferation to food safety.

The first round of the S&ED was held on July 27-28, 2009 in Washington and included senior officials from the State Department, Treasury, the White House and twelve other departments and agencies of the U.S. government, as well as senior counterparts from fifteen Chinese government entities.

President Obama opened the meeting by noting that, "The relationship between the United States and China will shape the 21st century, which makes it as important as any bilateral relationship in the world."

The Chinese clearly view the initial meeting of the S&ED as a great success. In meetings I participated in last month in Beijing with a number of senior Chinese officials, all gave very positive assessments of the first Dialogue. Wang Qishan, Vice Premier and Chair of the Economic Track for China, said the meeting allowed the two sides to better define further steps they needed to take in responding to the global financial crisis. He called it a "huge success." Wu Bangguo, Chairman of the Standing Committee of the National People's Congress, noted the unprecedented depth, scope and representation on the two sides, and said that the positive work at the first S&ED would allow China and the United States to move forward more effectively on a range of issues.

Secretary Clinton also pointed to a number of positive developments resulting from the S&ED. In her closing remarks at the Dialogue, she noted that United States and China agreed to "promote stability in Northeast Asia, resume the Six-Party Talks, and implement UN Security Resolution 1874, to address ongoing threats of violent extremism and nuclear proliferation, to encourage Iran to live up to its international obligations, and to work toward peace and stability in Afghanistan, Pakistan and the Middle East."

She also stated that as a result of the S&ED, bilateral talks on counterterrorism would be held, military-to-military relations would be expanded and progress was made on a global nuclear security summit that President Obama plans to convene early next year. In addition, the two countries signed a "Memorandum of Understanding to Enhance Cooperation on Climate Change, Energy and the Environment," which commits both sides to achieving a successful international climate change agreement, cooperating on adaptation strategies, and developing practical solutions for both countries' transitions to low-carbon economies.

On the Economic Track, Secretary Geithner announced agreement on a framework for cooperation on macroeconomic and structural policies designed to ensure more balanced and sustainable global growth, the building of more resilient financial and regulatory systems, a reaffirmation of the two countries' commitment to an open and rules-based trade and investment regime, and a pledge to work together in ensuring that

international financial institutions are provided the necessary tools and resources to respond adequately to international financial challenges.

Beyond the issues themselves, as the Congressional Research Service has noted, the S&ED, "is one of the few venues in which PRC ministers interact… with each other across departmental jurisdictions," which is a major benefit as China's "government bureaucracies traditionally have been 'stove-piped' with little inter-departmental interaction or coordination." The interdepartmental nature of S&ED is important as China's own policymaking process has become more complicated now that the bureaucracy does not speak with a single voice, and the government must take some account of the views of the media and public.

Clearly, the Strategic and Economic Dialogue covers an impressive array of issues and challenges, and it now stands at the very center of the bilateral relationship. After all, the United States and China are more dependent upon one another than ever before as trade, investment and mutual exchange have skyrocketed since normalization 30 years ago.

The United States is now the world's largest economy while China will soon be second. We are the world's two biggest trading nations and the two leading emitters of greenhouse gases. China is the top surplus country while the United States, unfortunately, is the largest deficit country. We thus represent the opposite sides of the global imbalances that contributed significantly to the worst financial crisis in generations.

While our two countries may have differences – including a pending dispute over tire imports from China – I believe that Washington and Beijing share interests on most of the important regional and global issues. More to the point, there is no major problem in the world that can be addressed adequately without bilateral cooperation, whether it be achieving lasting economic recovery and financial stability, overcoming the existential threat of climate change and achieving a clean and secure energy future.

These are the problems we must address cooperatively. Fortunately, the bilateral relationship is today in excellent shape. And in my view, the first meeting of the S&ED has laid the groundwork for the sort of positive, cooperative and comprehensive relationship both sides seek, and from which both countries – as well as the region and the whole world – will benefit.

Maintaining open channels of dialogue between the United States and China, which the S&ED does, is essential. At the same time, since the S&ED covers such a vast range of topics, and involves so many government agencies, unless the process is well managed, it may fail to achieve its promise. The purpose of today's hearing is to review the results of first meeting of the S&ED, and to examine how the Dialogue can best achieve its worthy goals on the many issues it covers.

Mr. ROHRABACHER. Thank you very much, Mr. Chairman. Before I move forward, let me just note that I believe that the people of China are America's greatest hope for a better world and the comments that I have about the government that controls them has nothing to do with the people of China.

The people of China, we need to see those people as our very important allies against the authoritarian government that controls them, which I believe that government, the dictatorship in Beijing, represents the greatest threat to America and to the western democracy's security and prosperity in the future.

Mr. Chairman, China is playing a rogue's role in the world. It has become the ally of criminal governments and criminal gangs that control various controls on various parts of the planet, whether we are talking about Burma, whether we are talking about Sudan, Cambodia or any list of the other rogue states of the world.

They are all buddies of China, and you will find that the Chinese are arming their friends and they are robbing the resources of people like the people of Burma where they are letting that regime destroy and dissipate the natural resources in exchange for weapons that are then used to suppress the people, and the profits from those natural resource rip offs are going into the pockets of a very corrupt few.

This is a pattern throughout the world, whether it is Sudan or Cambodia or Burma. It shows that the Chinese Government does not reflect the values that we would expect from a country that would have a place that we would talk to them as equals among nations.

China continues to be the world's greatest human rights abuser, whether we are talking about suppression of the Uighurs and this slow motion genocide that the Chinese have put in place to try to destroy the Uighur nation or whether it is the people of Tibet, the same slow motion genocide operation against the people of Tibet.

Or whether we are talking about the Falun Gong who are still being arrested by the hundreds at times, perhaps at times by the thousands, and thrown into prison with no due process. People just disappear and, worse, we find that the prisons which they are thrown into have an unexplainable source of body parts and which they are then selling to western buyers.

This ghoulish regime needs to be recognized for what it is and not be given the status that some people would like to give it simply because it is powerful and simply because it is a force to be reckoned with. No, that does not mean you give someone who runs the government like that, you don't give gangsters, just because they are powerful, the same respect that you would pay to democratic nations.

We need to look at China as potentially America's worst enemy. It is not an enemy today, it is an adversary, but it is building itself to the point where it could be the most threatening enemy that we have ever faced.

First of all, when we look at the economic relationship that has been established with China it has been a disaster for the people of the United States and a boon for those people who control the levers of power in Beijing. What we have had is an unfair trade relationship that we have winked and nodded and permitted, a

partnership between America's corporate elite and the gangsters that run China for the benefit of our corporate elite and the benefit of those gangsters, to the detriment of the American people.

The American people have lost millions upon millions of jobs, of manufacturing jobs, that have been sent off to China in order to be done by slave labor by people who have no right to form a union and people who would be thrown in jail or murdered if they tried to form a union in the company, not to mention the environmental things that you have mentioned today.

China, of course, there is no democratic process in which the people of China will try through their government to limit the exploitation of the environment, unlike in other democratic societies, so the gangsters who run that country can simply do what they please in terms of the environment. We have had a one-way free trade policy with them, which again has cost us millions.

We have the theft of American intellectual property rights on a huge scale being conducted by the Chinese Government. They are using our own technology to put us out of work and put America into a position where our safety and security is being jeopardized. We now see that in the expansion of the Chinese military and we see that in the expansion of the Chinese military's insistence on building rockets and missiles which are demonstrably aimed at taking out America's satellites.

Mr. Chairman, what we need to do is face reality when it comes to this potential threat and this potential enemy in Beijing and we must side—we must make sure that the people of China know that in their endeavors against this tyranny the American people are on their side and that those corporate leaders in the United States who have made their alliance do not represent the values and the policies of the people of the United States.

Thank you very much.

Mr. FALEOMAVAEGA. I just want to make sure that it is corrected in the record for my good friend from California. You don't mean small business owners. It is the big, corporate multinationals that are the ones.

Mr. ROHRABACHER. Certainly. If I said small business owners I meant big, corporate nationals.

Mr. FALEOMAVAEGA. Okay. Very good. I thank the gentleman from California for his statement. This is what makes America such a beautiful democracy where you can openly dissent or disagree on any given issues that you want.

Mr. ROHRABACHER. Unlike in China where they will throw you in jail.

Mr. FALEOMAVAEGA. I do thank the gentleman nevertheless.

We have two distinguished members representing the administration at our hearing this afternoon. Mr. David Shear is currently the deputy assistant secretary for East Asia and Pacific affairs at the Department of State. He formerly worked as director of Chinese and Mongolian affairs in the East Asia and Pacific Affairs Bureau, has been a Foreign Service officer since 1982, and served in postings in Tokyo, Beijing, Kuala Lumpur and Sapporo, Japan.

Mr. Shear was also deputy chief of mission at our Embassy in Kuala Lumpur. He was a minister counselor at our Embassy in Tokyo and deputy director of Korean affairs. An excellent gen-

tleman by career. He is fluent in both Chinese and Japanese. I only wish I could be as well.

We also have with us Mr. David Loevinger. He is currently the executive secretary and senior coordinator for China Affairs and the Strategic and Economic Dialogue at the United States Treasury Department. Previous to that Mr. Loevinger served as a U.S. minister counselor for financial affairs to the People's Republic of China.

Also at the Treasury Department, he was the first permanent representative in China. He was responsible for deepening United States-China engagement on financial and macroeconomic issues, including monetary, fiscal and exchange rate policies.

He played a leading role in the establishment of the United States-China strategic economic dialogue, the precursor of the current U.S.-China Strategic and Economic Dialogue. This is all semantics it seems to me. He worked closely with Chinese regulators to open new markets for United States financial service firms. The list goes on.

Prior to his service in Beijing the gentleman was also deputy assistant secretary at the Treasury for Africa, Middle East and Asia where he advised the Secretary of the Treasury and other senior Treasury officials on United States policies regarding the IMF, the World Bank and regional development banks.

Prior to that position he served as a staff economist, including also as a special assistant. My gosh. The list goes on forever on this guy. Mr. Loevinger, we are indeed very happy that you are able to come and join us. He worked with the IMF and is a graduate of Dartmouth University. He completed his master's at Harvard in public policy at the Kennedy School.

Very, very distinguished careers for both of these gentlemen. I look forward to hearing your testimony. Mr. Shear?

STATEMENT OF MR. DAVID SHEAR, DEPUTY ASSISTANT SECRETARY, BUREAU OF EAST ASIAN AND PACIFIC AFFAIRS, U.S. DEPARTMENT OF STATE

Mr. SHEAR. Thank you very much for the nice introduction, Mr. Chairman, and thank you, Mr. Rohrabacher, and thank you also for inviting me today to appear before you to discuss the first United States-China Strategic and Economic Dialogue held at the end of July.

I would like to provide an overview of the role of the S&ED as we call it in our bilateral relations with China, the primary goals of the first S&ED and the issues discussed in the S&ED strategic track, which was chaired by Secretary Clinton.

My colleague from the Treasury Department, David Loevinger, will speak to the economic track, and my colleague from the State Department Bureau of Oceans, Environment and Science, Jeff Miotke, will be prepared to take questions regarding the Memorandum of Understanding (MOU) on climate change discussed during the S&ED.

The Strategic and Economic Dialogue establishes the framework for the United States-China relationship under the Obama administration. We recognize the importance of engaging China as an important partner in addressing complicated global challenges, in-

cluding the recent economic crisis, climate change and threats to international security. It is critical that China meets its responsibilities as a global stakeholder and contributes to the solution to these problems.

The S&ED brings together top United States and Chinese political and economic leaders to outline opportunities for cooperation and engage in frank discussions of priorities for our bilateral relationship. The dialogue enables us to work together to build trust, strengthen cooperation and resolve our differences. And we have no illusions about our differences; all of these activities serve our common interests.

The S&ED is not the beginning of a G–2 structure. Both countries recognize that we can't solve the world's problems bilaterally. What the Dialogue does is provide a framework for the United States and China to deal with these challenges as responsible global cooperators and open up paths of communication on global issues of common concern.

We had three primary goals for the first S&ED, all of which I think we achieved. First, the S&ED served as a prime opportunity for our senior officials to get to know their Chinese counterparts, a necessary first meeting that will lay the foundation for effective cooperation for the next 4 years.

The first dialogue allowed face-to-face interaction among not only the four co-chairs—Secretary Clinton, Secretary Geithner, Vice Premier Wang Qishan and State Councilor Dai Bingguo, but also over 20 officials of cabinet rank from each side. We held frank discussions on a variety of issues, including those sensitive to the Chinese such as human rights, Xinjiang and Tibet.

Secondly, by mobilizing the whole of government on each side, the S&ED enabled discussions on issues that cut across agencies, including the full range of economic, regional, global and environmental challenges

Third, the S&ED set the agenda for our future engagement with China by giving our senior officials the opportunity to convey priorities of the Obama administration. The S&ED set the tone and framework for our major bilateral initiative with China, including a number of subdialogues.

With regard to the strategic track, it basically consisted of four areas. We discussed bilateral relations; international security issues such as nonproliferation and counterterrorism; global issues, including health, development, energy and global institutions; and regional security issues in North Korea, Afghanistan, Pakistan and Iran. Climate change, clean energy and the environment were addressed in separate special sessions.

Some of the key highlights of the strategic track include first, the climate change, energy and environment MOU which elevates the importance of climate change in our bilateral relationship.

Second, both sides agreed to enhance efforts in promoting regional stability. On North Korea, we affirmed the importance of the Six-Party talks and continuing efforts to achieve denuclearization of the Korean Peninsula. On Afghanistan and Pakistan, the two sides pledged to increase coordination to jointly promote stability and development in the region. On Sudan, both sides expressed our willingness to increase coordination and consultation to jointly seek

an early and enduring comprehensive political settlement of the Darfur issue and promote the north/south peace process.

In discussions on international security issues, both sides noted their shared opposition to terrorism and agreed to hold the next counterterrorism subdialogue this week actually, September 14 and 15. We discussed the upcoming 2010 Nuclear Nonproliferation Treaty Review Conference and the Conference on Disarmament and exchanged views on the Global Nuclear Security Summit proposed by the United States for March of next year.

On other global issues of common concern, both sides agreed to further dialogue in cooperation on promoting global sustainable development, including strengthening global institutions and government, addressing public health challenges and future discussion of cooperation on poverty alleviation around the world.

The two sides held frank discussions on human rights. Secretary Clinton raised U.S. concerns about recent violence in Xinjiang and discussed ways to enhance mutual understanding and positive cooperation on human rights issues. Both sides agreed to reconvene the U.S.-China legal experts dialogue and will seek to hold the next human rights dialogue before the end of the year.

We have no illusions about how the Chinese treat their people. We have a strong interest in improvement of human rights in China, and we make our views crystal clear—absolutely clear—to the Chinese at every possible opportunity, and we took that opportunity during the S&ED to do so this time around and will do so in the future as well.

On bilateral military-to-military relations, the two sides welcomed recent improvements in military-to-military relations and agreed that the two militaries would expand exchanges at all levels.

Over the next year, U.S. senior officials will take full advantage of a packed bilateral political calendar to follow through on S&ED objectives. High level bilateral engagements over the next few months include the President's visit to Beijing in November, several energy and environment meetings leading up to Copenhagen and technical consultations on counterterrorism and human rights.

The Strategic and Economic Dialogue has created both a strategic guideline and a catalyst for the United States and China to address complex global challenges. I would like to conclude my remarks here, Mr. Chairman, and thank you again for the opportunity to testify today on this important topic.

[The prepared statement of Mr. Shear follows:]

DAVID B. SHEAR
DEPUTY ASSISTANT SECRETARY
BUREAU OF EAST ASIAN AND PACIFIC AFFAIRS
U.S. DEPARTMENT OF STATE

BEFORE THE
HOUSE COMMITTEE ON FOREIGN AFFAIRS
SUBCOMMITTEE ON ASIA, THE PACIFIC AND THE GLOBAL ENVIRONMENT

SEPTEMBER 10, 2009

U.S.-CHINA RELATIONS: MAXIMIZING THE EFFECTIVENESS OF THE STRATEGIC AND ECONOMIC DIALOGUE

Chairman Faleomavaega, Mr. Manzullo, and Members of the Subcommittee, thank you for inviting me to appear before you today to discuss the first U.S.-China Strategic and Economic Dialogue (S&ED) held in Washington on July 27and 28. I will provide an overview of the role of the S&ED in our bilateral relations with China, the primary goals of the first S&ED, the issues discussed and achievements of the S&ED Strategic Track, and next steps. Dave Loevinger, Treasury's Executive Secretary and Senior Coordinator for China and the S&ED will speak to the Economic Track. I am also joined by State Department Deputy Assistant Secretary Jeff Miotke, who is prepared to take questions regarding the Memorandum of Understanding on climate change signed during the S&ED.

The Role of the S&ED

The Strategic and Economic Dialogue establishes the framework for the U.S.-China relationship under the new Administration. We recognize the importance of engaging China as an important partner in meeting the complex global challenges our two countries face. It is critical that we reinforce the message to China that with its increased influence comes increased responsibility. China must meet its responsibilities as a global stakeholder and contribute to the solutions to global challenges, such as the recent economic crisis, climate change, and threats to international security--challenges that cannot be met without cooperation between our two countries. During a discussion of U.S.-China relations and global issues of common interest at a bilateral meeting in April, President Barack Obama and President Hu Jintao agreed to work toward a positive,

cooperative, and comprehensive U.S.-China relationship for the 21st century. They established the U.S.-China Strategic and Economic Dialogue as the mechanism to advance that relationship.

The S&ED brings together top political and economic leaders from both sides to outline opportunities for cooperation and engage in frank discussions of priorities for our bilateral relationship. Our two countries are already cooperating in a number of areas by promoting global economic recovery and international financial reforms, combating piracy in the Gulf of Aden, working to curb nuclear proliferation by North Korea and Iran, seeking clean energy solutions that can curb CO2 emissions, and cooperating on regional stability in South Asia. While we will not always agree on all issues, the Dialogue enables us to work together to resolve our differences, to build trust, and to strengthen cooperation, all of which serves our common interest.

I would like to emphasize at the outset that the S&ED is not the beginning of a G2 structure. Both countries recognize that we cannot solve the world's problems bilaterally. What the Strategic and Economic Dialogue does is to provide a framework for the U.S. and China to deal with these challenges as responsible global stakeholders and open up paths of communication on global issues of common concern.

Goals of the S&ED

We had three primary goals for the first S&ED, all of which were accomplished:

First, the S&ED served as a prime opportunity for our senior officials to get to know their Chinese counterparts, a necessary first meeting that allows for more effective engagement on issues over the next four years. Having our Chinese counterparts understand the Administration's positions and priorities was one of the most valuable results of the Dialogue. The presence of President Obama at the opening and in the leaders' meetings further highlighted to the Chinese the significance of the Strategic and Economic Dialogue for the new Administration. The first Dialogue also provided an opportunity not only for the four co-chairs, Secretary of State Clinton and Secretary of the Treasury Geithner, Vice Premier Wang Qishan, and State Councilor Dai, but also for over 20 officials of cabinet-rank from each side to meet face-to-face and to discuss a range of substantive

issues. By bringing these senior officials together in one location in both formal and informal settings, the S&ED enabled frank and candid discussions on a number of issues, including those sensitive to the Chinese such as human rights and Xinjiang.

Second, the Strategic and Economic Dialogue mobilized the whole of government on each side by incorporating the full range of economic, regional, global, and environmental challenges that require action by both countries in order to attain progress. By employing a whole-of-government approach, the S&ED allowed us to discuss with Chinese officials issues that cut across agencies, such as climate change and international security. With the right people at the table, discussions at the S&ED served to energize sub-dialogues by bringing issues to the attention of senior officials from multiple agencies.

The Strategic and Economic Dialogue complements and adds additional force to the many existing bilateral dialogues that we have with China. The S&ED sets the tone and framework for these sub-dialogues, which incorporate the priorities developed at the S&ED. It was designed to meet once a year to give room for these sub-dialogues to grow. Also, holding the S&ED once a year allows us to get away from an event-planning mentality and move toward building a regular process of robust engagement and consideration of broader topics of long-term, strategic concern.

Third, the S&ED set the agenda for our future engagement with China by giving our senior officials the opportunity to voice the priorities of the new Administration. Climate change, for example, was addressed at a senior level unprecedented in U.S.-China discussions and resulted in the signing of an MOU that lays a solid foundation for cooperation on climate change as we move toward Copenhagen.

Overview and Achievements of the Strategic Track

The Strategic Track of the S&ED consists of four pillars: 1) bilateral relations (people-to-people exchanges); 2) international security issues (non-proliferation, counterterrorism); 3) global issues (health, development, energy, global institutions); and 4) regional security and stability issues (Afghanistan/Pakistan, Iran, DPRK). As part of the Strategic Track, we also discussed climate change, clean energy, and the environment in separate special

sessions. The Joint Press Release on the U.S.-China Strategic and Economic Dialogue documents the wide range of issues discussed and is located on the State Department website at *www.state.gov*.

Some key highlights from the Strategic Track include:

- *Climate Change, Energy, and Environment MOU.* The Memorandum of Understanding (MOU) signed during the S&ED elevates the importance of climate change in our bilateral relationship, recommits the United States and China to reach a successful international agreement, and expands cooperation to accelerate the transition to a sustainable low-carbon global economy. The MOU establishes an ongoing dialogue on what both countries are doing to reduce emissions and to advance international climate negotiations ahead of the UN climate change conference in Copenhagen. In addition, the MOU expands and enhances cooperation between the United States and China on clean and efficient energy and environmental protection. Discussion of specific emissions reduction targets are not a part of this agreement, nor were they meant to be. In the MOU the U.S. and China commit to respond vigorously to the challenges of energy security, climate change and environmental protection through ambitious domestic action and international cooperation.

- *North Korea.* The two sides affirmed the importance of the Six-Party Talks and continuing efforts to achieve denuclearization of the Korean Peninsula. They emphasized the importance of implementing UN Security Council Resolution 1874 and resolving the nuclear issue on the Peninsula through peaceful means. Both sides agreed to increase their efforts for the early realization of these goals.

- *South Asia.* The two sides pledged to increase coordination to jointly promote stability and development in Afghanistan and Pakistan.

- *Sudan.* The two sides expressed their willingness to increase coordination and consultation on the issue of Sudan to jointly seek an early and enduring comprehensive political settlement of the Darfur issue and promote the peace process between the north and the south of Sudan.

- *Counter-Terrorism*. Both sides noted their shared opposition to terrorism. The United States proposed dates to hold the next round of the U.S.-China Counter-Terrorism Sub-Dialogue this year, and China expressed interest in holding the Sub-Dialogue in that timeframe. The Sub-Dialogue has been scheduled for September 14-15, 2009.

- *Non-Proliferation*. The two sides pledged to work collaboratively to strengthen global non-proliferation and arms control regimes. They discussed the upcoming 2010 Nuclear Nonproliferation Treaty (NPT) Review Conference and the Conference on Disarmament (CD) and exchanged views on the Global Nuclear Security Summit proposed by the United States.

- *Military-to-Military Relations*. The two sides welcomed recent improvements in military-to-military relations and agreed that the two militaries would expand exchanges at all levels. The dialogue included the participation of a People's Liberation Army (PLA) representative who, on behalf of PLA General Xu Caihou, Vice Chairman of the Central Military Commission, accepted Secretary of Defense Gates' invitation to visit the United States during the last week of October. There is a set of official military-to-military exchanges that is separate from the S&ED.

- *Human Rights*. The two sides also discussed ways to enhance mutual understanding and positive cooperation on human rights issues through our Human Rights Dialogue and other initiatives on the basis of equality and mutual respect. In light of the importance of the rule of law to our two countries, the United States and China decided to reconvene the U.S.-China Legal Experts Dialogue and will seek to hold the next Human Rights Dialogue before the end of the year.

- *Energy Security*. We agreed to future dialogue on strategic petroleum reserve cooperation and increased transparency in energy markets.

- *Global Issues*. The two sides agreed to further dialogue and cooperation on promoting global sustainable development, including strengthening global institutions and governance, addressing public health challenges, and future discussion of cooperation on poverty alleviation around the world.

Next Steps

Over the next year, we will be working on priority issues identified at the S&ED in our various bilateral initiatives with China, including several sub-dialogues and meetings between cabinet and sub-cabinet level officials. The results of these meetings will feed into the planning for the second S&ED next year in Beijing. High-level bilateral engagements over the next few months including the President's visit to Beijing in November, several energy and environment meetings leading up to Copenhagen, a sub-dialogue on counterterrorism, and a human rights dialogue. The messages and priorities from the S&ED will help to guide these interactions, and vice versa.

Thank you, again, for the opportunity to testify today on this important topic. I welcome your questions.

Mr. FALEOMAVAEGA. Thank you, Mr. Shear.

Mr. Loevinger, for your testimony?

STATEMENT OF MR. DAVID LOEVINGER, EXECUTIVE SECRETARY AND SENIOR COORDINATOR FOR CHINA AFFAIRS, AND THE STRATEGIC AND ECONOMIC DIALOGUE, U.S. DEPARTMENT OF TREASURY

Mr. LOEVINGER. Thank you, Mr. Chairman, Congressman Rohrabacher. I want to thank you for the invitation to come and speak to you today about the United States-China Strategic and Economic Dialogue and more broadly our bilateral economic relationship.

The S&ED that President Obama and President Hu initiated in April recognizes that cooperation between China and the United States is vital not only for the well being and prosperity of our two nations, but also for the health and stability of the global economy.

Given that my colleague, David Shear, has talked about the strategic dialogue, I am going to focus my remarks on the economic track of the S&ED. The economic track provides a framework for promoting productive bilateral economic engagement in core U.S. interests. As Secretary Geithner told the Chinese at the S&ED, the United States and China may not always agree on economic issues, but the S&ED provides a platform for narrowing our differences and reinforcing our common interests, both bilaterally and in setting the multilateral economic agenda.

The first meeting of the economic track of the S&ED was one of the largest delegations from any foreign country in the history of our foreign relations, involving 12 United States cabinet officials and agency heads and 15 Chinese ministers, vice ministers and agency heads. Both sides agreed on a framework for cooperation on economic issues based on four pillars: First, promoting a strong recovery and achieving more sustainable and balanced growth; second, promoting more resilient, open and market oriented financial

systems; third, strengthening trade and investment; and, fourth, strengthening the international financial architecture.

On the first item, promoting a strong recovery and achieving more sustainable and balanced growth, both sides agreed to undertake macroeconomic and structural policies to ensure a more sustainable and balanced trajectory of global growth.

China committed to policies to adjust its demand and relative prices that will lead to more balanced trade and growth. To achieve this, it will promote more domestic demand led growth and pursue policies to increase the share of consumption in its GDP. It also committed to greater development of its services sector, which will reduce its dependence on exports in heavy industry and support its transition to a greener economy.

Second, we focused on building more resilient and market oriented financial and regulatory systems. China agreed to a range of measures, including promoting consumer finance, allowing foreigners to invest more in China's capital markets, increasing the number of foreign joint venture securities companies and allowing foreign banks incorporated in China to underwrite corporate bonds on China's interbank bond market.

This will not only create market opportunities for United States financial services firms, but by creating a more developed and market oriented financial system it will boost the incomes of Chinese households and contribute to more consumption led growth.

The two sides also agreed to strengthen their cooperation on anti-money laundering and countering the financing of terrorism, and we will continue to encourage the Chinese to strengthen their efforts to counter the threat of North Korea and Iran's nuclear weapons programs through their financial sector.

The third item was strengthening trade and investment, and the United States and China each reaffirmed their commitment to open and rules-based trade and investment. China committed to a range of measures that over time will create new opportunities for United States firms and workers.

This includes further opening of its services markets to private investment, decentralizing its foreign investment reviews, and China also clarified that products produced in China by foreign invested enterprises will be treated the same under China's Government procurement regulations as products produced by Chinese producers. China also agreed to intensify its effort to join the WTO Government Procurement Code.

Lastly, the United States and China recognized the critical role that the international financial institutions play in preventing and responding to crises and ensuring more balanced global growth. The global economy has changed fundamentally since the historic gathering of Bretton Woods and so too must the global architecture that bears its name.

Both sides committed to work together to ensure that the international financial institutions have the requisite resources and tools to address today's challenges, and we will work together with China to ensure China's full engagement and representation in the design of key multilateral arrangements and groupings, including the G–20, the Financial Stability Board and the international financial institutions.

As Mr. Shear said, while the S&ED is going to meet annually, having agreed on priorities and broad policy commitments, the word of the S&ED is going to continue throughout the year. On the economic side we will work closely with our colleagues at Commerce and USTR on the Joint Committee on Commerce and Trade and through a range of other deputy level and staff level groupings.

Throughout the year we intend to consult with and seek the advice of Congress, including members of this committee and your staff, U.S. businesses, labor and other groups affected by United States-China relations. Thank you.

[The prepared statement of Mr. Loevinger follows:]

"U.S.-China Relations: Maximizing the Effectiveness of the Strategic and Economic Dialogue"

Prepared Statement of
David Loevinger
Executive Secretary and Senior Coordinator for China Affairs &
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U.S. Department of Treasury
House Foreign Affairs Committee,
Subcommittee on Asia, the Pacific and the Global Environment
September 10, 2009

Chairman Faleomavaega, Ranking Member Manzullo, thank you for the invitation to speak to you today about the U.S.-China Strategic and Economic Dialogue, and the United States economic relationship with China.

Framework for the U.S.-China Economic Relationship

Building upon President Obama's call for a positive, cooperative, and comprehensive relationship, the U.S.-China Strategic and Economic Dialogue (S&ED) that President Obama and President Hu initiated in April recognizes that cooperation between China and the United States is vital not only to the well being of our two nations but also the health of the global economy. Today I will speak mainly about the Economic Track of the S&D and leave discussion of the Strategic Track to my colleague, David Shear.

In my testimony, I will provide a brief overview of the Economic Track of the S&ED, its objectives and achievements, and discuss how the S&ED fits into the overall management of U.S.-China economic relations.

S&ED Economic Track Overview

In the last few years the frequency, intensity, and importance of U.S.-China economic engagements have multiplied. China and the United States individually, and together, are important enough in the global economy that what we do has a direct impact on the stability and strength of the international economic system. Both nations have an obligation to ensure that our policies and actions promote balanced, sustainable global growth going forward.

The Economic Track of the S&ED provides a framework for promoting productive bilateral economic engagement and core U.S. interests. As Secretary Geithner said to the Chinese at the S&ED, "the United States and China may not always agree on economic issues, but the S&ED provides a platform for narrowing our differences and reinforcing our common interests, both bilaterally and in setting the multilateral economic agenda."

I'd like to discuss the first meeting of the Economic Track of the U.S.-China Strategic and Economic Dialogue, held on July 27 and 28, in which one of the largest delegations in the history of our bilateral relations met for two days, involving twelve U.S. economic Cabinet officials and agency heads and 15 Chinese Ministers, Vice Ministers and agency heads.

Both sides agreed on a framework for cooperation on economic issues based on four pillars: i) promoting a strong recovery and achieving more sustainable, balanced growth, ii) promoting more resilient, open, and market-oriented financial systems, iii) strengthening trade and investment, and iv) strengthening the international financial architecture.

Promoting a Strong Recovery and Achieving More Sustainable, Balanced Growth

First, we will undertake macroeconomic and structural policies to ensure a more sustainable and balanced trajectory of global growth.

In the United States, the current account has fallen and private savings rates have risen to historical average levels, and we will take steps to sustain and reinforce these trends. President Obama has committed to lowering the federal deficit to sustainable levels once recovery is firmly established. The Administration is committed to investments in energy, education and health care that will rebuild the American economy on a firmer foundation going forward.

China will rebalance towards domestic demand-led growth and increase the share of consumption in GDP. Policies to enable adjustment of demand and relative prices will lead to more balanced trade and growth. Greater development of China's services sector and the shift away from dependence on exports and heavy industry will have a powerful effect not only on rebalancing but also supporting the transition to a green economy.

Promoting More Resilient, Open, and Market Oriented Financial Systems

Second, we focused on the importance of building more resilient and market-oriented financial and regulatory systems. The United States underlined its commitment to stronger regulation and supervision of the financial system. China agreed to undertake specific measures, including promoting consumer finance; allowing foreigners to invest more in China's capital markets; increasing the number of foreign joint-venture securities companies that can participate in brokerage, proprietary trading and advisory services; allowing foreign banks incorporated in China to underwrite corporate bonds on China's inter-bank market on the same basis as Chinese banks; and allowing qualified overseas companies to list on Chinese stock markets and promote the listing of Chinese companies on U.S. stock markets.

This will not only create market opportunities for U.S. financial services firms, but creating a more developed and market-oriented Chinese financial sector through such measures as liberalizing interest rates and creating a wider variety of financial products and services, will

help boost the incomes of Chinese households and contribute to more consumption-led growth.

The two sides also agreed to strengthen their cooperation on anti-money laundering and countering the financing of terrorism, and we will continue to encourage the Chinese to strengthen efforts to counter the threat of North Korea and Iran's nuclear weapons program.

Strengthening Trade and Investment

Third, the U.S. and China each reaffirmed their commitment to open and rules-based trade and investment. China committed to a range of measures that over time will create new opportunities for U.S. firms and workers through increased trade and investment. China announced its intention to further open its service markets to private investment, and decentralize its foreign investment reviews, including by raising the dollar threshold of foreign investments that requires central government review. Chinese authorities also clarified that products produced in China by foreign-invested enterprises will be treated the same under China's government procurement regulations as products produced by Chinese producers, and also agreed to intensify efforts to join the WTO Government Procurement Agreement.

Strengthening the International Financial Architecture

Fourth, the United States and China recognized the critical role of the international financial institutions in preventing and responding to crisis and ensuring balanced global growth. The global economy has fundamentally changed since the historic gathering at Bretton Woods and so too must the global architecture that bears its name. We committed to work together to ensure the international financial institutions have the requisite resources and tools to address today's challenges. We will work together to ensure China's full engagement and representation in the design of key multilateral agreements and groupings, such as the G20, the Financial Stability Board, and the international financial institutions.

How the S&ED Fits into the Management of U.S.-China Economic Relations

While the S&ED will meet annually, having agreed on priorities and broad policy commitments, the work of the S&ED will continue throughout the year, through coordination with other bilateral economic fora such as the JCCT and Deputy and staff led working-groups. Treasury will lead efforts to promote reforms of macroeconomic and financial policies, and the international financial institutions, through the Joint Economic Committee (JEC) and the Financial Stability Working Group (FSWG). The Investment Forum, co-led by Treasury, State, Commerce, and USTR, will promote open investment policies. Frequent and constructive interactions with Chinese finance and economic officials in multilateral settings such as the G20, IMF and World Bank annual meetings, and Asia Pacific Economic Cooperation (APEC) meetings, provide further opportunities to enhance our cooperation. At the S&ED, the U.S. and China also agreed to continue a range of other bilateral economic dialogue mechanisms on banking

supervision, transportation, communications, postal reform, health, agriculture and labor issues.

And throughout the year we intend to consult with and seek the advice of Congress, including members of this Committee and your staffs, U.S. businesses, labor, and other groups affected by U.S.-China relations.

Thank you again for the opportunity to appear before you on this important topic and I would be happy to take any questions you have.

Mr. FALEOMAVAEGA. Thank you, Mr. Loevinger.

We are joined this afternoon also by one of our distinguished members, Mr. Inglis. I wanted to ask him if he has an opening statement he would like to share with us?

All right. We are going to open now with questions, and I will defer to my good friend, the gentleman from California. At a later time I will ask my series of questions.

Mr. ROHRABACHER. Thank you very much, Mr. Chairman.

Mr. Shear, and I appreciate your addressing my specific points on human rights in your opening statement, and you seemed rather adamant about that we are actually serious about human rights in the complaints we make to China. Can you tell me what consequences the regime in Beijing suffers?

What have we put forward to say you know, these are human rights abuses and because you are doing that you are paying this consequence for it? What have we offered them as a suggestion that we really are serious about it rather than just using words?

Mr. SHEAR. Thank you, Congressman. We made it clear to the Chinese that, for example, in the case with regard to religious freedom that all modern, civilized countries implement religious freedom vigorously and that countries that do not suffer in terms of openness and the vitality of their society and their economies as well.

We have made it clear to the Chinese that the restriction of information on the internet, for example, not only results in a society which is less well informed, but in an economy that is less efficient.

Mr. ROHRABACHER. But we haven't said there is no direct correlation between the Chinese regime continuing to commit these human rights abuses and any specific policy of the United States Government. There is no correlation there at all. Is that correct?

Mr. SHEAR. My understanding, Congressman, is that, for example, the Chinese still remain under the Tiananmen Sanctions Act, which limits a variety of exchanges with the Chinese, including some exports of United States law enforcement equipment and commercial space cooperation as well, so in that regard the Chinese have seen some consequences with regard to their treatment of human rights.

On the general question——

Mr. ROHRABACHER. Right.

Mr. SHEAR [continuing]. We are very strong in making representations on these subjects to the Chinese. I think that we have achieved some successes.

Mr. ROHRABACHER. Pardon me. I only have a very short period of time to ask questions, and I have to go to——

Mr. SHEAR. Understood.

Mr. ROHRABACHER. I would suggest that talking strong and not following up with a specific consequence has exactly the opposite impact that diplomats would like us to believe.

Unless there is something that backs up somebody's words, if we continue to talk tough but there are no further consequences other than what happened right after Tiananmen Square and at the same time Americans are stumbling over themselves to invest capital in and build an economy in China, don't you think that basically gives the Chinese the opposite impression that really Ameri-

cans are just using a bunch of words when in reality all they care about is making money?

Mr. SHEAR. We don't let up on the Chinese on human rights issues, Congressman. The Chinese understand very clearly what we think on these issues, and I think our exchanges with them on this subject have had positive effects.

I think Chinese rule of law has improved over the past several decades. They have a long way to go in this regard.

Mr. ROHRABACHER. Right. Are there any opposition parties in China?

Mr. SHEAR. There are no legitimate opposition parties.

Mr. ROHRABACHER. Is there a free press in China?

Mr. SHEAR. The press is highly restricted.

Mr. ROHRABACHER. Okay. Is the Falun Gong free to have their organization without having their members thrown in jail?

Mr. SHEAR. No, it is not.

Mr. ROHRABACHER. All right. So I don't think we have seen very much, and yet at the same time we have seen massive increases and exchanges of money, of people investing money from the United States in building a manufacturing base which puts our people out of work and enriches that regime. That is kind of a bigger message than all the words we can use.

Let me ask you about that. The President last night said that we have been losing 750,000 jobs a month in our current economic situation. How many of those jobs have been going to China?

Mr. SHEAR. I can't answer that question, Congressman, but I know that the $73 billion in exports we sent to China last year also accounted for thousands of American jobs.

Mr. ROHRABACHER. Sure. And what was the offset there? It was $73 billion or $43 billion we are exporting, and how much is it we importing?

Mr. SHEAR. I think we imported $256 billion in Chinese goods last year.

Mr. ROHRABACHER. All right. And you think that didn't cost any American jobs? Well, I think that we could suggest that.

Why is it that they have gotten away with that so long? Why is it that for so long we have had a one-way free trade policy that has permitted, from what you just described, a five to one ratio—it may be even more than that—of exports or imports to exports?

Mr. SHEAR. Just a general point, Congressman, and then I would like to turn the microphone over to Mr. Loevinger, but this administration is committed to doing everything we can to foster American industry and help the American worker.

We have taken action both within the WTO and bilaterally on trade issues with China, and, as I say, we have had some successes.

Mr. ROHRABACHER. You will have my support at that point. My last question——

Mr. FALEOMAVAEGA. Will the gentleman yield?

Mr. ROHRABACHER. Certainly.

Mr. FALEOMAVAEGA. I recall that it was in 2007 China exported to the United States over $340 billion worth of goods.

And I am curious. Mr. Loevinger will help us. Out of those goods that were manufactured in China, how many United States multi-

nationals were involved in the manufacturing process in terms of the number of jobs that were sent overseas, sponsored heavily by our own multinationals?

I am curious. Of that $340 billion of Chinese imports, how much was that percentage produced by our own American corporate entities that are doing business in China because of cheap labor and all this other stuff that comes with it?

Mr. LOEVINGER. Thank you, Mr. Chairman. Roughly about 60 percent of China's exports are produced by multinational corporations. My impression is the biggest foreign investors are from Taiwan, Japan and Korea, but also the United States is a very important foreign investor in China.

But more broadly to the point you made and the point that Congressman Rohrabacher made, we are concerned about these very big trade imbalances, and this was the focus of the economic track of the S&ED. The message to China is that its growth model is going to have to change because there are changes going on in the United States.

U.S. households are changing their savings behavior—we have seen savings going up—and that if China wants to grow it is not going to be able to depend on the United States consumer in the way it has in the past. It is going to have to produce its own home grown growth model. Very simply, China is going to have to consume more and save less because the United States consumer is saving more.

So how are we going to bring that about? The S&ED talked about, and it wasn't just talk. We got commitments from China over the course of the next several years. That was our intent going in was to build a framework for engagement for the rest of the administration on ways China can bring down its very large trade imbalances.

The exchange rate is an important part of that equation, and we had serious and frank discussions on the exchange rate, but the exchange rate is only one tool. We also talked about things China can do in the financial sector creating what we call a social safety net.

China has to establish its own health care reform, its own unemployment insurance, its own way of financing education so Chinese households feel more secure so they can save less and consume more.

Mr. ROHRABACHER. I am very happy to hear that we have had so much talk, and I would hope that the administration, unlike the past administration and the administration before that and the administration before that who also talked about many of the very same issues, will decide to do something specific in which the Chinese will feel a consequence if they are not, for example, giving us the type of reform on currency reform that we are talking about and the same type of trade restrictions that we face and they themselves are engaged, the government itself is engaged.

Let me ask that as a basic question. Is not the Chinese Government engaged in a great effort in the United States to steal American technology? We are talking about espionage, economic espionage. I mean, I understand there have been about 50 such situations in the last few years that we have uncovered from China where you have——

Mr. FALEOMAVAEGA. The gentleman has one more question.

Mr. ROHRABACHER. Am I incorrect in that?

Mr. LOEVINGER. Okay. What I can tell you is we had frank discussions. There are policies that we have concerns about in China. There are issues that the Chinese raise with us.

They think our export control policies are too tough. They think our Sisyphus process is too tough, and we were very frank with them that in Sisyphus we are going to protect our national security. In our export control policies that are implemented both by the Commerce Department and by the State Department we are going to ensure that militarily critical technologies and dual use technologies are protected.

Mr. ROHRABACHER. Well, to the degree that you guys are doing that more than talking you will have my support. I wish you luck, and we will be watching real closely, won't we, Mr. Chairman?

Mr. FALEOMAVAEGA. Yes. I find it somewhat ironic that here we have a country that is basically Socialist Marxist ideology in applying free market systems since Deng Xiaoping made that announcement in 1978, and yet somehow they do a better job in working their economy in a free market system when we are supposed to be the better ones to understand how capitalism, how a free market, should work in such a way that we find ourselves in a worse situation than the Chinese.

Am I missing something here? Because it seems that the Chinese are telling us how to properly implement a free market system because, apparently, despite all this world crisis, economic crisis, China's economy seems to be the most stable. Yet it is a not a capitalistic society. Could you help me reconcile this irony?

Mr. LOEVINGER. I would be happy to. Without a doubt the growth that China has achieved since Deng Xiaoping instituted the reforms 30 years ago has been one of the most notable economic success stories in history. Without a doubt, the Chinese people, their lot has been improving. More people now are richer in China than they have ever been.

At the same time, I respectfully disagree that I don't think when you compare the United States to China we have to give anything to the Chinese. The big imbalances we see in China are as much an indication of their weaknesses that Chinese households can't consume. They feel they have to save because they don't have the whole set of systems that we have set up in the U.S.

Mr. FALEOMAVAEGA. What I meant, Mr. Loevinger, is that I am not an economist, but the financial crisis that we find ourselves in, something happened on Wall Street. The derivatives and all this came about, lack of regulatory authority on the part of government to enforce what was supposed to be to keep an eye on greed, if that is a better way of saying it. I suppose the extreme of capitalism, you become greedy and you forget the rules and that is how we ended up where we are.

Now, I may be wrong in my laymen's terms of defining that. I mean, you have to give some credit to the Chinese for their success in doing whatever they have done in making their economy now second or near second now only to our economy, so that is what I am trying to say here.

They seem to have done a better job in not only controlling the economic situation with the annual growth rate now at 8 percent, and we are suffering right now in terms of all the jobs lost, the recession and all of that, so I was just trying to dig into that.

Mr. LOEVINGER. Yes. Let me make three quick points.

Mr. FALEOMAVAEGA. Yes.

Mr. LOEVINGER. Obviously a lot of mistakes were made in the U.S. and Secretary Geithner is going to work very closely with Congress on reforming our financial supervision and regulation to make sure those mistakes don't happen again.

Secondly, China did not have the financial crisis, but part of the reason is China's financial sector is much less developed than ours, and that has its own problems for Chinese households. It is much harder to go to a store and pay with a credit card. It is much harder to get a loan to buy a home or finance schooling in China than it is in the United States.

Mr. FALEOMAVAEGA. I think that is understandable. I think our overall GDP right now is about $19 trillion to China's what, $3 trillion or $4 trillion, so understandably, our economy is still number one in the world.

On the S&ED, it sounded more like a G–2 that we are taking all the world's issues it seems. Are you sensing any sense of resentment maybe from some of our closest allies? Do they ask, "How come we are not part of the team?"

Is there a sense of exclusivity involved here where now only China and the United States are solving the world's problems and without consultations with our allies or the other forums that may have similar problems?

Are we taking too much into this or are we streamlining it better, defining our priorities? Not just for China. We are talking about regional issues. We are talking about world issues. Shouldn't others also be active participants in the process?

Mr. SHEAR. Mr. Chairman?

Mr. FALEOMAVAEGA. Mr. Shear?

Mr. SHEAR. Secretary Clinton has said that we are not in a multipolar world now; we are in a multipartner world. And China, as one of the world's great powers, one of the world's great trading nations, is one of those essential partners in our efforts to address issues like climate and the global financial crisis.

But it is not the only partner. We will be working together closely particularly with our allies in Europe and in East Asia to address these issues as well. In East Asia we will be working closely with our Japanese, our South Korean and our other allies, particularly as the new Japanese Government comes in.

We will be consulting with them closely. We will be cooperating with them intensively, and we will be keeping them fully informed of what we are doing with our other partners, including China.

Mr. FALEOMAVAEGA. I was in Korea recently, and I noticed with interest the fact that there is no other country that has more influence on the situation in North Korea than China. There is no other country in the world that has more influence on the situation in South Korea than the United States.

So my question: Where does it say in the Bible that there must be Six-Party Talks? Why not just China and the United States and

two Koreas? Where does Russia have an interest in the process? Japan now is introducing a collateral issue that has nothing to do with denuclearization, which to me kind of puts a puncture there on the process of Six-Party Talks. Do you care to comment on that?

Mr. SHEAR. All members of the Six-Party Talks——

Mr. FALEOMAVAEGA. And by the way, how do you denuclearize a country that already has in its possession 10 nuclear bombs like North Korea? Did we do that to Pakistan? Did we do that to India? Why are we singling out North Korea to denuclearize when it already has the nuclear bomb, may I ask?

Mr. SHEAR. On your first question with regard to Six-Party Talks, we think that all parties with a vital interest in peace and stability and denuclearization on the Korean Peninsula should be involved in this process. The six parties are the countries closest to the Korean Peninsula and with the strongest interest in these issues.

I think we have worked closely through the Six-Party process. We want the Six-Party process to continue. The Chinese do as well. The Chinese have a variety of interests on the Korean Peninsula, including the denuclearization of North Korea, but also including stability and avoiding a large flow of North Korean refugees across the border.

We have addressed all these issues within the context of the Six-Party process. We hope the North Koreans will come back to the Six-Party table as soon as possible as we rigorously implement the sanctions under Security Council Resolution 1874.

Mr. FALEOMAVAEGA. My apologies. My time is up.

Mr. Royce?

Mr. ROYCE. Thank you, Mr. Chairman. Let us stick on that issue for a minute with respect to North Korea because China is North Korea's gateway to the outside world, right? I mean, China props up North Korea. That is the reality.

Now, you say that China recognizes the latest U.N. Security Council resolution. I am trying to figure out what that means. Does that mean that China is giving us adequate assistance on North Korean financial activity? Because it doesn't look that way.

Mr. SHEAR. I will defer to Mr. Loevinger on the subject of financial activity, but in general terms China worked with us in the Security Council to produce one of the strongest sanctions resolutions on North Korea yet. That is the result of lengthy cooperation and consultation with the Chinese within the Security Council on a succession of Security Council resolutions on this subject.

With regard to implementation, we have consulted closely with the Chinese on this. We have urged them to implement the sanctions vigorously. I think the Chinese have done that, and we are working with them on other measures they can take.

Mr. ROYCE. They are with us right up to pulling back on economic support and propping up North Korea.

Mr. SHEAR. The Chinese have restricted energy to North Korea in the past.

Mr. ROYCE. But for very short periods of time, and we had some success for a very short period of time in terms of the Banco Delta Asia. That was an example of how you get North Korea's attention, but that requires the cooperation of China.

The only point I am going to make is that your report was light in terms of how we have tried to leverage China on North Korea. What I would suggest to you is you spent a lot of time on these issues with China, a whole host of them. I think we are missing the big picture right now, which is proliferation. Once it reaches the Euphrates River and North Korea is building reactors in Syria we have a proliferation problem. China is sort of the linchpin of this.

But that takes me to another concern that I have, and I will go to David's testimony here. Mr. Loevinger, you said in your testimony that China and the United States each reaffirmed their commitment to open and rule-based trade in investment. That seems to me a stretch because I don't see China—I can see them reaffirming its commitment. I just don't see any practice of it.

One of the reasons I say that, I am from California and have met with many Chinese, Vietnamese-American, American investors, people all over the map who are trying to do business in China, and it is always the same story about corruption.

So after so many of these cases and reading so many of them in the press as well, it is clear that American investors get used and abused in China and you have officially sanctioned corruption there. So what is the United States going to do about that? We have got American investors basically being piñatas, you know, and Chinese corruption just takes a whack at them.

And what is more bothersome is that the U.S. Government, more specifically, the Commerce Department, very deceptively promotes China. I can't tell you how many complaints I get from investors. So you go to one of the many conferences they hold, and you would think China was nirvana as they pitch this, an investor's paradise. That it is ripe for the picking.

These conferences are a real shame because they give disinformation, and our commercial advocacy at the embassies and the consulates, which are then absolutely necessary once anybody invests, that is very, very feeble. For those of us who have worked on constituents' cases to try to get any justice done, you and I know there is no justice in that system.

So I would like to hear from you what this trade and investment dialogue was like with the Chinese, given the fact that some of us know what the process is really like for those involved in trade and investment. You know, did it deal with the reality that thousands of American investors are getting wronged in China, or was it just happy talk, or what happened during that dialogue?

Mr. LOEVINGER. Thank you, Congressman Royce. Frankly, you bring up a lot of good points.

I just spent 3½ years at the embassy in Beijing, and every week I heard from U.S. companies, a lot of U.S. financial services firms, talking about how tough it is to do business, so I can tell you it is no nirvana. On the other hand, frankly, as you guys mentioned, there is a lot of United States investment going into China because even though it is not a nirvana businesses are making money and they are growing their business.

When we say we want to promote rule-based investment in trade and we want a Chinese commitment to rule-based investment in trade, we are going to start with the WTO. You have seen this ad-

ministration and the previous administration bring several WTO cases to China, and we have won several WTO cases and we are going to continue to bring cases to the WTO when China is not adhering to its commitment.

Secondly, we want to expand the international commitments on trading investment that China is part of, so we spent a lot of time talking about the WTO government procurement agreement and how it didn't matter in the 1980s when the agreement was signed whether China was in or out because who cared because China was a small purchaser and a small supplier. Now it matters a lot.

And we also talked about when the administration finishes its review of policies toward bilateral investment treaties moving forward on a bilateral investment treaty with China again to put our trade and investment relations under more of a rule-based framework.

Mr. ROYCE. Thank you, Mr. Chairman.

Mr. FALEOMAVAEGA. Thank you. I wondered if the gentleman from California desires to do a second round. We have another panel pending.

Mr. ROHRABACHER. No.

Mr. FALEOMAVAEGA. Okay. I do want to say thank you both, gentlemen, for coming. My subcommittee looks forward to working with you both in the coming weeks and months as we try to unravel a lot of the fundamental issues affecting the Asia-Pacific region, over which it has jurisdiction. I sincerely want to thank you both for being here this afternoon.

Mr. SHEAR. Thank you, Mr. Chairman.

Mr. FALEOMAVAEGA. Thank you.

We have in our next panel my dear friend, a distinguished gentleman in his own right, Mr. John Podesta. Here with us also are Mr. Fred Bergsten and Mr. Randall Schriver.

Mr. Podesta is currently president and CEO of the Center for American Progress. Under his leadership, the Center has become a notable leader in development of and advocacy for progressive policies. In 2003, Mr. Podesta served as White House chief of staff to President Bill Clinton and served on the President's Cabinet and was a principal on the National Security Council. While in the White House, he also served as both assistant to the President and deputy chief of staff.

Recently, Mr. Podesta served as co-chair of President Obama's transition team, where he coordinated the priorities of the incoming administration, oversaw the development of policy and spearheaded the appointment of major Cabinet secretaries.

Additionally, he has held numerous positions on Capitol Hill as an aide to the former Democratic leader, Senator Thomas Daschle, and as counsel to the Senate Agriculture Committee and Judiciary Committee.

A Chicago native and a graduate of Knox College and Georgetown Law School, he currently is a visiting professor of law, authored several books, and the list goes on and on. John, welcome. Very glad to have you.

Mr. PODESTA. Thank you, Mr. Chairman.

Mr. FALEOMAVAEGA. Dr. Fred Bergsten is currently the director of the Peterson Institute of International Economics, formerly

known as the Institute for International Economics in its creation in 1981. The Institute is the only major research institution in the United States devoted solely to international economic issues.

It has been called the most influential think tank on the planet. The first comprehensive survey of some 5,465 think tanks around the world recently concluded that the Peterson Institute was tied for top-rated think tank in the world with the Brookings Institution, I understand. It has a staff of about 60 and has moved to an award winning new building right now. Dr. Bergsten was the most widely quoted think tank economist in the world in 1997 and 2005, and his tremendous work continues on.

Also he was assistant secretary for international affairs at the U.S. Department of Treasury from 1977 to 1981, also as a major economic assistant to Dr. Henry Kissinger at the National Security Council. Dr. Bergsten has authored, co-authored and edited over 40 books and hundreds of articles. My gosh, the list goes on and on. I could spend the whole day here listening to this gentleman.

Dr. Bergsten received his doctorate and his master's from the Fletcher School of Law and Diplomacy and graduated magna cum laude from Central Methodist College. He has contributed tremendously to U.S. and international economic policy, analyses of a wide range of global economic issues, and provided a vision for a G–2, now known as the Strategic and Economic Dialogue.

Mr. Randall Schriver is one of the founding partners of Armitage International, a consulting firm that specializes in international business development and strategies. Mr. Schriver served as deputy assistant secretary of State for East Asia and Pacific affairs where he was responsible for the People's Republic of China, Taiwan, Mongolia, Hong Kong, Australia, New Zealand and the Pacific Islands.

Prior to that, he served as chief of staff and policy advisor to then Deputy Secretary of State Richard Armitage. He formerly served for 4 years in the Office of the Secretary of Defense, was an active Naval intelligence officer for 3 years, foreign policy advisor on the McCain Campaign for President last year and was on the Bush-Cheney defense transition team.

Mr. Schriver has won numerous military and civilian awards. He hails from the state of Oregon. He holds a master's degree from Harvard and a bachelor's from Williams College.

Gentlemen, this committee is truly honored to have all three of you for taking your precious time to come and testify before the subcommittee on this issue, which I think is very, very important not only to me, but also to my colleagues on the Foreign Affairs Committee.

I would like to start with Mr. Podesta, if you would, and see where we can go from there.

STATEMENT OF MR. JOHN PODESTA, PRESIDENT AND CHIEF EXECUTIVE OFFICER, CENTER FOR AMERICAN PROGRESS

Mr. PODESTA. Thank you, Mr. Chairman. You have an extensive written statement, so let me try to summarize.

Mr. FALEOMAVAEGA. Without objection. All your statements will be made part of the record, as well as any other materials you want to add.

Mr. PODESTA. I will just try to hit some key points. I am honored to be here with you, Mr. Chairman, Mr. Rohrabacher. I just returned from China where I led a high level delegation that included former leader of the Senate, Tom Daschle, John Deutch and former Ambassador Wendy Sherman, and I just came back last week so my observations are at least fresh, if not accurate, but they are at least fresh.

Our conversations with very senior members of the Chinese Government convinced me that the relations between China and the United States are on a solid footing. For example, State Councilor Dai Bingguo told us that the government hoped President Obama's visit in November would rival the significance of President Nixon's visit and introduce an era in which the United States and China could build a positive, cooperative and comprehensive relationship, which you quoted in your opening statement, Mr. Chairman.

Look, I am not naive about China. I understand the human rights issues, the issues around support for states like Sudan and Burma, but I think that we don't have the luxury of either ignoring or not getting along with China at this moment in history.

We have pressing global challenges that need to be addressed with China, so I think it is time to move beyond what has been usually referred to as engaging in hedge framework of China policy and take an approach that is openly premised on a strategy that maximizes opportunity and tries to manage the risk.

The new format of the Strategic and Economic Dialogue will be instrumental to shaping our relationships going forward, as well as making progress on a number of global challenges. I thought I might comment based on again our conversations recently in China on some aspects of the national security relationship and then talk a little bit about climate change and clean energy.

On North Korea, you may know, Mr Chairman, I recently accompanied President Clinton to Pyongyang, making me I guess one of the few Americans who have been there in recent years, and our discussion in Beijing I think suggests that China remains committed to a denuclearized Korean Peninsula, and they will work to reengage the DPRK in multiparty communications.

China's recent enforcement, as Mr. Royce was suggesting, of U.N. sanctions against Pyongyang I think is actually an encouraging sign of their position. They view this as a strategic I think threat in the region, and I think they are being cooperative on that question.

On Iran, China has acknowledged that Iran should not possess nuclear capabilities, but it has declined to use its leverage on the issue. The United States Government I think needs to continue to press China on Iran, given our mutual interest in avoiding a regional arms race and promoting long-term stability. I think in that regard, the Chinese investments, particularly with respect to developing the Iranian capacity to develop gasoline, I think are troubling. I think we need to keep pressing on that front.

With respect to military cooperation, we met with General Ma, who is the vice chairman of their Joint Chiefs. Cooperation and confidence between China and the United States militaries I think has lagged behind that of other state apparatuses. I think both

sides view this as being marked by a kind of stop/start/restart quality that has not always been helpful to either side.

I think both sides actually, both the United States military and the Chinese military, are looking to bring cooperation and confidence to levels consistent with other areas of the United States-China relations, and senior leaders of our two militaries need to continue to engage in regular and candid dialogue on issues of mutual concern.

The resumption of our formal bilateral defense dialogue is an important first step, and there are a number of other activities I think that could follow on. For example, our ships are battling pirates side-by-side right now off the coast of Somalia, and I think that is symbolic of the way we can develop a stronger mil-to-mil relationship.

We also discussed pandemics. I think China learned its lesson from SARS and are actively cooperating with the World Health Organization particularly with respect to H1N1. While they have made some mistakes in that regard, I think they are basically in a cooperative mode and a positive mode.

Let me just say a word about climate change. During our meetings in Beijing, we were assured that China will do its part with respect to addressing its skyrocketing emissions rates. As my testimony goes over, they have very, very significant investments in clean energy, very major investments in solar and wind, developing the clean energy technologies and industries of the future. I think they will be a competitive player in that regard. In fact, I think we are at risk of falling behind.

The MOU that was referenced in the first panel I think is a significant movement whereby we can begin to understand and move forward to demonstrate that their energy policy will indeed result in emissions reductions capabilities in a measurable, reportable and verifiable way, so I think it is a very important part of the Dialogue and has been made central under this administration to the Dialogue.

We, along with the Asia Society, have developed a kind of road map on how we can cooperate on CCS, carbon capture and sequestration, which I think they are quite interested in, our own Government is quite interested in, and it may be a way of carrying out demonstration of that vital technology to both countries in a way that is cost effective and will result in reduced emissions again in both countries.

My time is up, and I will turn back the microphone.

[The prepared statement of Mr. Podesta follows:]

Written Testimony for the
Subcommittee on Asia, the Pacific, and the Global Environment
Eni F. H. Faleomavaega (D- American Samoa), Chairman

on

"The Strategic and Economic Dialogue: Setting the Agenda, Achieving Results"

by

John D. Podesta
President and CEO
The Center for American Progress

1:00pm, September 10, 2009

Mr. Chairman and members of the committee, thank you for inviting me to testify before you this afternoon. I am very pleased to have this time to share my thoughts on U.S.-China relations and the Strategic and Economic Dialogue, along with some specific ideas for increasing cooperation between the U.S. and China.

This opportunity comes at a timely moment. I returned from China last Thursday, where I led a small American delegation that included Senator Tom Daschle, Ambassador Wendy Sherman, Professor John Deutch, former Deputy Secretary of Defense Rudy deLeon, and SEIU President Andy Stern to Beijing. Our group spent three full days speaking with some of the senior-most government officials, leading

academics, and members of the financial industry about a range of issues of utmost importance between our two countries.

On the whole, our conversations convinced me that relations between China and the U.S. are on solid footing. Although many areas of difference remain – lead among them those that touch on China's sense of territorial integrity – the Chinese seem eager to keep bilateral relations on an upward trajectory. They demonstrated a willingness to increase cooperation with the United States on a range of pressing global problems, spanning national security, economic, and environmental challenges.

Dai Bingguo, China's State Councilor, expressed his support for closer ties in extremely strong terms that I'm sure this committee will appreciate: he told us the government hoped President Obama's upcoming visit in November would rival the historical significance of President Nixon's 1972 visit. Just as Nixon's groundbreaking visit to China marked the beginning of normalization, the Chinese hope that President Obama's trip will introduce an era in which the United States and China can build a "positive, cooperative, and comprehensive relationship." This was the description that Presidents Obama and Hu agreed upon when they met in April at the G20 summit, and we heard it repeated like a mantra during our three days of meetings.

Indeed, we no longer have the luxury of not getting along with China. We cannot meet today's most pressing global challenges, be they climate change, nuclear

proliferation, grinding poverty or deadly viruses, without its pivotal participation—not only in implementing solutions, but also in devising them. We should move beyond the "engage and hedge" framework for China policy – an approach openly premised on mistrust and suspicion – to a strategy that maximizes opportunity but also manages risk. Building a relationship will accelerate China's development into a responsible stakeholder and increase our ability to solve today's most difficult global problems. The touchstone for a successful U.S.-China relationship should be effective collaboration against global challenges and strengthening the global architectures we need to battle them.

We are off to a positive start. Despite initial apprehension among Chinese leaders about President Obama's position towards China given their lack of familiarity with him, they seem reassured by what they see to be an unusually smooth transition with clearly stated policy priorities, even though strong points of difference cut across a range of issues. The restructuring of the Strategic and Economic Dialogue, and the fact that the first full meeting under the new format was held after President Obama had been in office only six months, played a large role in dispelling the uncertainty that has marked previous transitions and could have hindered progress on a number of issues critical to U.S. interests. Continuing to engage in frequent dialogue is integral to maintaining a relationship with China that encourages their constructive participation in the international system.

Today, I would like to offer my impressions on two broad aspects of our relationship: national security and climate change. Both areas contain major challenges, but both also present unique opportunities to move bilateral relations in a stable, constructive direction. The new format of the S&ED, which now includes a security track led by the State Department alongside the existing economic track led by Treasury, will be instrumental to progress in these areas.

On the national security front, China's active engagement continues to be necessary to constrain North Korea's nuclear ambitions. Our discussions in Beijing suggest that China remains firmly committed to a denuclearized Korean peninsula and will work to reengage the DPRK in multiparty communication. China's recent enforcement of UN sanctions against Pyongyang is a new and encouraging sign of their position.

Iran's nuclear program is another major national security concern that requires China's cooperation. Here, however, we have a longer and rockier road ahead. China has acknowledged that Iran should not possess nuclear weapons, and has been engaged in the diplomatic process to find a solution. However, Beijing has declined to use its leverage on this issue. And while the international community has been trying to increase the pressure on Tehran, China's energy companies continue to sign multibillion dollar contracts with the regime. China, like the U.S., has a profound interest in ensuring Iran does not achieve nuclear armament, which could trigger a regional arms

race. This is an issue that the U.S. government should continue to press with China, given our mutual interest in promoting long-term regional stability.

In order to improve cooperation on issues of mutual concern as well as to discourage any potential tensions or misunderstandings between our two countries in the future, we need to improve our military to military ties with China. Historically, our militaries have generally comprised the most conservative elements of state policy. U.S.-China military to military relations have been marked by a start-stop-restart quality that has not always been helpful.

To bring cooperation and confidence to levels consistent with other areas of U.S.-China relations, senior leaders of our two militaries should continue to engage in a regular and candid dialogue on issues of mutual concern. The resumption of our formal bilateral defense dialogue is an important first step. There are a number of other activities that could follow: additional exchange among senior levels of military leadership, including continued coordination on maritime operational procedures, or jointly addressing security issues in weak or failing states. These could provide valuable opportunities for strengthening U.S.-China military to military relations. Our ships that are battling pirates side by side off the coast of Somalia are symbolic of how American and Chinese national security interests are not a zero sum game.

Let me just say a few words on the swine flu pandemic, which is also a national security issue. China has learned its lesson from SARS and is actively cooperating with the World Health Organization. In fact, the WHO is now under the leadership of Dr. Margaret Chan, a Chinese national, and China held a major international conference last August to discuss strategies for fighting the virus. While some Chinese officials have been overzealous in quarantining potential victims, including American visitors who were not sick, overall China is showing real responsibility in this area.

I would like to use the rest of my time to discuss the Strategic and Economic Dialogue in the context of clean energy and climate change, issues that have the greatest potential both to drive and to benefit from a new kind of U.S.-China relationship. Although it is still uncertain what steps China will take in advance of the UN Summit in Copenhagen this December (as it is still unclear what steps the United States will take over the next few months), last week we were told by China's top climate negotiator, Xie Zhenhua, that we would find China's commitments in the next Five Year Plan positively surprising. As expected, the Chinese government is not likely to abandon its self-understanding as a developing country that requires assistance to catch up to OECD countries, but we were assured at every stage that China will "do its part" to address its skyrocketing emissions rates.

Although China was originally slow to acknowledge the threat of climate change, it is now moving quickly to capitalize on the economic advantages a robust clean energy

industry offers. While debate over climate legislation rages in the United States, Beijing is keenly aware that investing in the building blocks of a low-carbon economy will drive job growth and innovation in the years to come. China's leaders frame the development of clean energy as an opportunity to stimulate consumption, increase investments, achieve stable export opportunities, and adjust their energy structure, all while increasing international economic competitiveness.

A rapid change in policy priorities has accompanied Beijing's change in attitude. China has ramped up national targets for energy efficiency and renewable energy development, and its recent stimulus package spends around 3 percent of China's annual GDP in 2009 and 2010 on clean energy investments – considerably more than U.S. clean energy stimulus funding as a percentage of our respective economies. These measures have driven China's leadership in solar and wind component manufacturing, grid transmission technology, and electric vehicles, and helped Chinese clean energy companies leapfrog competitors within only a few years.

As Beijing forges ahead with its aggressive clean energy agenda, U.S.-China climate developments have also been on an upward tick. At the inaugural Strategic and Economic Dialogue in July, China and the U.S. signed a new "Memorandum of Understanding" to improve cooperation on climate change, energy and the environment. The MOU sets up a platform for cooperation between our two countries while opening the door to the initial steps of a solution to one of the main obstacles to a

global climate change agreement: uneven acceptance among developing countries that their emissions reductions should be "measurable, reportable, and verifiable." China, despite large investments in clean energy over the last several years, ambitious targets for energy intensity, and new efficiency standards, does not currently quantify resultant emissions reductions in a way that is measurable, reportable, and verifiable within the international climate change framework.

The Chinese are anxious to move beyond broad guidelines for cooperation to initiate joint clean energy projects with the United States, and the MOU establishes a format whereby such projects must demonstrate their emissions reductions capabilities in a measurable, reportable, and verifiable way. Implementation of renewable energy or smart grid technologies, for example, only works if we can actually see the results and make sure these technologies achieve the emissions reductions they are designed to do. By holding discussions regarding technology cooperation and emissions reductions with China, as opposed to working with the entire block of developing countries at once, we now have a pragmatic forum in which measuring, reporting, and verifying emissions reductions in China can be initiated. In short, this MOU has moved us from the principles laid out in the 2007 Bali Action Plan at 30,000 feet down to an approach position where we can enter Chinese airspace and see the runway.

Given the influence China and the U.S. have over the success or failure of the UN climate summit in Copenhagen, there is little time to waste in making the most of recent

climate progress between our two countries. To capitalize on the opportunities the MOU facilitates, the Center for American Progress has recently partnered with the Asia Society's Center on U.S.-China Relations to propose a series of programs to advance U.S.-China cooperation, focusing on carbon capture and sequestration (CCS) technology.

The U.S. and China's continued reliance on coal-fired power for electricity generation – 50 percent and 80 percent, respectively – must be addressed in any comprehensive climate change policy. CCS offers a potential pathway for achieving swift and sustained reductions in global greenhouse gas emissions from coal-fired power generation, and should be part of a portfolio that includes dramatic gains in efficiency, conservation, and renewable generation. But before we commit ourselves to this technological pathway, it is critical to conduct more CCS demonstration projects to generate accurate cost and environmental safety assessments, develop accepted practices and standards for sequestration, and establish a market for private sector investment. The Center for American Progress and the Asia Society's proposal identifies opportunities for immediate collaboration that will produce quick results, while simultaneously focusing on the longer term goals of retrofitting existing plants and developing financing infrastructure.

First, the proposal lays out a blueprint for rapid cooperation on large demonstrations of geological sequestration of available pure CO2 streams that exist today in China. China has installed over 100 coal gasifiers that produce pure ("pre-

captured") CO2 streams that currently vent into the atmosphere from a variety of heavy industrial plants, such as chemical and cement facilities. We recommend a set of large projects at multiple sites within China with substantial U.S. contributions in practice, equipment, and science. Such collaborations could serve as templates to not only test various sequestration technologies, which we will eventually want to deploy in the U.S., but also to build regulatory and financial infrastructures at less cost than would be possible with unilateral development in the U.S. (We estimate $50-100 million for each project with a U.S. contribution of $20-30 million.) Such a project is highly likely to succeed and, in addition to providing assistance to the Chinese in an area where they lack capacity and opening a new market to U.S. suppliers, would build confidence for future cooperation.

The proposal also provides a framework for enabling collaborative research, development, and demonstration of CCS technology (such as post-combustion capture) to retrofit existing coal-fired plants over short, medium and long-term timeframes. This would first and foremost identify plants in both countries for large-scale retrofit demonstrations and establish commitments for doing so. It would also test new technologies to improve effectiveness and lower costs, along with outlining a long-term strategy for retrofitting coal-fired power plants in both the U.S. and China that respects the political, industrial and financial dispositions of each. Retrofitting older coal-fired plants is a key component to a low-carbon future if, and only if, the technology can be

demonstrated. Most public investments in the U.S., such as the Futuregen project, are aimed at building new integrated "pre-combustion" plants. But even if this technology succeeds, it will be difficult to encourage power generators from giving up older plants that may be more profitable. Attending to these older coal-fired plants is essential to avoiding a global rise in temperature of more than 2 degrees Celsius.

Additionally, the report discusses the creation of a global capital fund designed to distribute funds to private actors that innovate or invest in CCS endeavors and the development of public finance structures (price guarantees or other market value substitutions) such as those proposed in the American Clean Energy and Security Act to provide guaranteed returns in the short term.

In sum, both the United States and China stand to gain more through collaboration than through independent pursuit of CCS technology. Furthermore, by conducting sequestration projects in China, rather than in the U.S., both sides benefit from lower costs and faster execution. The experience gained by cooperating with China will accelerate the deployment of CCS facilities in the U.S., with benefits to job growth, utility and energy companies, and technology firms. We estimate that cooperation with China on this suite of programs could accelerate large-scale deployment of CCS technology in the U.S. by 5 to 10 years. Our initial assessment is that this could result in billions of dollars in savings if we can accelerate full scale deployment of CCS before the anticipated execution date of 2030. Just as important, in a few years,

nearly 10 million tons of CO2 that would otherwise have entered the atmosphere will instead be stored indefinitely.

If we are to achieve a best-case climate scenario, the U.S. and China must turn the seeds of good will into genuine cooperation. This holds true not only for climate change, but also for many other tough global challenges. In many cases, genuine strategic collaboration with China will be necessary, which won't always be easy for the U.S. It will take some adjusting on our part to work toward solutions that are not always entirely of our crafting. But while the U.S. and China do not constitute a "G2," as some have said—we need a whole community of nations working together to address the serious problems that plague us—both countries' commitment to solving global threats is pivotal. The Strategic and Economic Dialogue, therefore, is a critical framework for facilitating deeper understanding and cooperation between our two countries. The U.S. and China should move forward with efforts to build the "positive, cooperative, and comprehensive" relationship that our presidents have called for.

Mr. FALEOMAVAEGA. Thank you, Mr. Podesta.
Dr. Bergsten?

STATEMENT OF MR. FRED BERGSTEN, DIRECTOR, PETERSON INSTITUTE FOR INTERNATIONAL ECONOMICS

Mr. BERGSTEN. Thank you, Mr. Chairman. I appreciate the opportunity to testify. I will make five basic points and try to do so quickly.

First, as you have already indicated, the United States and China are clearly the two most important national economies in the world. It is therefore clear that effective international policy coordination requires the closest possible cooperation between the United States and China.

The two countries do not have to agree on every issue, let alone pursue identical policies, but they must be willing and able to work constructively together if enough agreement is to ensue to permit progress across the entire range of crucial international issues ranging from recovery from the current crisis to creating a new global regime to counter global warming.

The punch line of that dual leadership is that the United States-China relationship must focus increasingly in the future on the wide range of global economic issues rather than the narrow bilateral frictions that we have traditionally emphasized in the past.

Second, in anticipation of those conditions, and as you indicated, I proposed 5 years ago that the United States and China work toward creating an informal G–2 that could provide effective leadership of the world economy. The idea is to develop a close working relationship that would supplement, not supplant, the other Gs—G–7, G–20—and the IMF and WTO.

Somebody mentioned that other countries are miffed that the United States and China might be working on these issues together. If the U.S. plays it right, all the other countries will be consolidated and engaged too, and if the United States and China can agree, and they have to agree to make progress, the outcomes will be superior and the other countries ought to welcome it. The idea is not to supplant but to supplement and make the system work better. And without these two, whether we like it or not, there has to be agreement or we won't get much progress.

My assessment of the initial meeting of the Strategic and Economic Dialogue and its future prospects is governed largely by an assessment of whether it is helping to create such a G–2. I think it is moving clearly in that direction, despite the denials of the Secretary of State earlier on, and holds considerable promise for so doing. I thus strongly endorse the initiative, praise the Chinese for participating so actively in it, and offer a few suggestions for how it can best proceed.

Third, to create and sustain an effective G–2, and to have an S&ED that works, the United States and China have to engage in a wide ranging and continuing conversation on their respective roles in the world economy and the global economic system.

As you mentioned, Mr. Chairman, they weren't even in it until 30 years ago. The whole system was created before they were even engaged. They were not present at the creation. They had nothing to do with the rules and institutions. So it is not a shock that as

they become the second largest economy in the world they might raise some questions about what they are getting into.

Therefore, we have to talk with them very seriously on world views about the global economy, the same way my old boss, Henry Kissinger, and President Nixon talked to Zhou Enlai and Mao Zedong back almost 30 years ago in opening up the United States-China relationship. And in a way that is even more important in the economic sphere because, as I say, they weren't involved in the system when it was created and developed, yet it is critically important to bring them into it.

So that would be point 3. The S&ED, by providing a full day or two of intensive interaction between key ministers of the two countries, can and should play an active role in that process.

Point 4. Heads of government and top officials will become impatient with lengthy discussions of world views and such unless there are some deliverables on issues of immediate concern. And I think it is therefore imperative the S&ED tackle the media topics. There are at least two issues where I think they did so effectively, and you heard about it early from the government representatives.

On the world economy, China and the United States have led the global recovery with fiscal and monetary stimulus. China in fact grew at an annual rate of 15 percent in the second quarter of this year, clearly was the first country to recover, clearly is leading the global recovery. The U.S. has not bottomed out. Our recovery has probably begun, and so I think we are on the way to a joint leadership of the recovery process.

What is critically important, however, and David Loevinger from Treasury emphasized it, is not only recovery of growth, but reshaping the composition of that growth and therefore the direction of both countries' strategies. China has been running huge, and in my view, unacceptable and unsustainably large trade surpluses, over 10 percent of its GDP. They have manipulated the exchange rate.

Mr. Rohrabacher didn't even mention that one, which I think is the most important problem. The Chinese have manipulated their exchange rate aggressively and massively. That has given them a huge competitive advantage and built up these trade surpluses. That just can't continue.

As Loevinger said, you have to put that in the context of a restructured growth strategy. Already, and this is not widely realized, China's trade surplus this year will be cut in half from where it was just 2 years ago.

The U.S. trade deficit is already cut in half from where it was 3 years ago so there is good progress, but the issue is to keep that going, build on it, use the S&ED and other devices in order to restructure the growth pattern in the way that Loevinger was discussing. I can elaborate on that if you wish.

The other big issue is global warming, and I do believe that this Memorandum of Understanding, which was the most tangible result from this S&ED meeting 6 weeks ago, could turn out to be a breakthrough in terms of United States-China cooperation and China's commitment to deal with that global problem.

Fifth and finally, there are some things they did not do and have to do in the future. China has expressed great anxiety about its dollar holdings. Well, they didn't really talk about that. The United

States is very concerned, rightly, about a seeming revival of industrial policy initiatives in China. I am not aware that they talked about that very much either, and the Chinese have this very aggressive policy of keeping the exchange rate undervalued. That boosts their trade surpluses and enhances their competitiveness unfairly.

Loevinger said they had long talks about it, but the truth is both Treasury and the IMF have backed away from any effective counter to that Chinese policy, which is very adverse not just to our economic interest, but to the stability of the whole global system.

So I think the S&ED is a good step down the line toward a G–2 to talk about global issues, and they made good progress on two of the big ones. But there are several others that remain to be addressed so they have a big agenda for the future that I hope they will continue to address.

[The prepared statement of Mr. Bergsten follows:]

THE UNITED STATES – CHINA ECONOMIC RELATIONSHIP AND THE STRATEGIC AND ECONOMIC DIALOGUE

C. Fred Bergsten[1]
Director, Peterson Institute for International Economics

before the
Subcommittee on Asia, the Pacific and the Global Environment
Committee on Foreign Affairs
US House of Representatives

September 10, 2009

The Policy Context

The United States and China are the two most important national economies in the world:

- China will shortly pass Japan to become the world's second largest economy behind the United States;
- the two together accounted for almost one half of all global growth during the four-year boom prior to the crisis;
- they are the two largest trading nations;
- they are the two largest polluters;
- they are on opposite ends of the world's largest trade and financial imbalance: the United States is the largest deficit and debtor country while China is the largest surplus country and holder of dollar reserves; and
- they are the leaders of the two groups, the high-income industrialized countries and the emerging markets/developing nations, that each now account for about one half of global output.

It is clear that effective international policy coordination requires the closest possible cooperation between the United States and China. The two countries do not have to agree on every issue let alone pursue identical policies. But they must be willing and able to work

[1] C. Fred Bergsten has been Director of the Peterson Institute for International Economics since its creation in 1981. He was formerly Assistant Secretary of the Treasury for International Affairs (1977-81) and Assistant for International Economic Affairs to the National Security Council (1969-71). His 40 books include *The Long-Term International Economic Position of the United States* (2009), *China's Rise: Challenges and Opportunities* (2008), *China: The Balance Sheet - What the World Needs to Know Now about the Emerging Superpower* (2006), and *The Dilemmas of the Dollar: The Economics and Politics of United States International Monetary Policy* (2nd edition, 1996).

constructively together, in terms of the domestic politics of each as well as their direct diplomatic contacts, if enough agreement is to ensue to permit progress across the entire spectrum of crucial international economic issues – ranging from recovery from the current crisis to creating a new global regime to counter global warming. Their relationship must therefore focus increasingly on the wide range of global economic issues for which they bear systemic responsibility rather than the bilateral frictions that have traditionally been its centerpiece.

In anticipation of these conditions, I proposed five years ago that the United States and China work toward the creation of an informal G-2 that could provide effective joint leadership of the world economy.[2] The idea was, and is, to develop a close working relationship between them that would supplement (not supplant) the existing steering committees, including the G-7/8 and the newly dominant G-20, and the multilateral institutions (notably the IMF and WTO). The overriding goal is to make those institutions function more effectively and thus strengthen the world economy.

My assessment of the initial meeting of the Strategic and Economic Dialogue (S&ED), and of its future prospects, is thus governed largely by an assessment of whether it is helping to create such a G-2. Viewed as a further extension of the earlier Senior Dialogue and Strategic Economic Dialogue (SED), I believe that the S&ED is indeed moving in that direction and holds considerable promise for continuing to do so. I thus strongly endorse the Administration's initiative, and praise the Chinese for their active participation in the process, and would offer a few suggestions for how it can best be used to achieve the desired outcome.

The Conceptual Framework

To create and sustain an effective G-2, the United States and China must carry on a wide-ranging and continuing conversation on their respective views of the world economy and the global economic system. They must do so in the same way that Richard Nixon and, especially, Henry Kissinger discussed their global geopolitical concepts at great length and depth with Mao Zedong and Zhou Enlai in re-opening relations between the two countries in the early 1970s. Such exchanges are perhaps even more important in the economic sphere because China is a late-comer to today's global arrangements and institutions, having opened to the world only in 1978 after the postwar rules and architecture had already been in place for three decades.

As a new economic superpower, along with the United States and the European Union (which, however, speaks with a single voice on only a few issues and thus cannot form a G-3 with the other two), China understandably asks why it should conform to a set of rules and institutional arrangements that it had no role in creating. This is of course the historical problem of the powerful newcomer crashing the (sometimes cozy) club of incumbent systemic leaders, which has had disastrous effects on some occasions – Germany in the late 19th century and again

[2] C. Fred Bergsten. 2005. A New Foreign Economic Policy for the United States. In *The United States and the World Economy: Foreign Economic Policy for the Next Decade*, eds. C. Fred Bergsten and the Institute for International Economics. Washington: Institute for International Economics. I developed the idea further in C. Fred Bergsten, Charles Freeman, Nicholas R. Lardy, and Derek J. Mitchell. *China's Rise: Challenges and Opportunities*. Washington: Institute for International Economics, 2008 and C. Fred Bergsten. 2008. A Partnership of Equals: How Washington Should Respond to China's Economic Challenge. *Foreign Affairs* 97, no. 4 (July/August): 57-69.

in the interwar period, Japan as well in the latter – though has been handled relatively smoothly in others (the United States in the late 19th century, Germany and Japan after the Second World War).

A central goal of the S&ED must therefore be to encourage the countries to seriously discuss their worldviews, at least on economic issues. It is of course difficult to do so with dozens of people sitting around a table in a formal setting so the Dialogue should provide maximum scope for smaller subgroups, particularly for the top officials, to carry on more informal and candid conversations. Those conversations can of course also take place during bilateral events, as when President Obama visits Beijing in November, and on the margins of the many multilateral meetings where leaders and top officials of the two countries frequently come together (G-20, G-7/8 "outreach sessions," UN General Assembly, APEC, etc.), and the evolution of the G-2 relationship of course occurs through these interactions as well as the S&ED. By providing a full day or two of intensive interaction between key ministers of the two governments, however, the S&ED can and should play an important role in this process.

The Current Agenda and Deliverables

Heads of government and top officials, however, will become impatient with lengthy meetings of this type if they do not also address issues of current concern and deliver results that will attract support at home. Thus it is imperative that the S&ED tackle topics of immediate salience and at least set broad policy directions that will help resolve them. There are at least three such issues on the global, and hence the United States – China, agenda at present:

- recovery from the global economic and financial crisis;
- reform of the international economic architecture, to help prevent future crises but also for long-standing structural reasons; and
- creation of a new international regime to save the planet from global warming.

I believe that the S&ED, building on the last year or so of the previous SED, has made substantial progress on at least the first and third of these topics.

On the world economy, China and the United States have led the way on fiscal and monetary stimulus. As a result, China recorded growth at an astounding annual rate of 15 percent in the second quarter to lead the global recovery. The US recession has bottomed out and renewed expansion, perhaps at a more robust rate than most forecasters now expect, has probably already begun.[3]

Surplus China and deficit America also seem to have reached a meeting of the minds on the shape of the recovery and future growth patterns. They appear to recognize that it would be a huge mistake, and indeed again unsustainable, for China to resume its reliance on export-led

[3] Michael Mussa. "Global Economic Prospects as of September 2009: Onward to Global Recovery." Paper to be presented at Sixteenth Semi-Annual Meeting on Global Economic Prospects at the Peterson Institute for International Economics, Washington, DC, September 17, 2009.

growth and ever-rising trade surpluses or for the United States to again become the "global consumer of last resort" and run huge current account deficits. Instead, China must expand domestic (especially consumer) demand and the United States must re-orient toward exports and productive investment.

It is too soon to judge whether the public pronouncements of the two governments in the direction of achieving these restructured growth paths will be fully realized. The early signs are promising, however:

- the US external deficit in 2009 will be about half its peak in 2006, and improvements in the real trade balance kept the economy growing through much of 2008 and sharply reduced the depth of the recession in the first half of 2009;

- China's rapid growth in the second quarter occurred despite a sharp fall in its external surplus, and my colleague and top China expert Nicholas Lardy forecasts that surplus will decline to 5-6 percent of China's GDP this year from its peak of 11 percent in 2007 (though that is at least partly due to their early and strong recovery from recession and could be reversed as their exports again expand when the rest of the world picks up).

The two governments will need to take further policy steps to sustain and build on this progress even as the recovery is still taking place. In particular, China has blocked further appreciation of its exchange rate against the dollar over the past year and indeed intervened in the currency markets at record levels in the second quarter to keep the renminbi from rising.[4] For its part, the United States must substantially reduce its budget deficits as soon as the recovery permits if it is to avoid a renewed escalation of its external imbalances.[5] If it can foster these additional measures, the G-2 will have been highly successful in correcting one of the major global economic problems of recent years and indeed an important cause of the current crisis. That could mark a major achievement for the S&ED.

The G-2 must likewise lead on global warming and there is similar evidence that the latest S&ED may have taken an important step down that road. The most tangible result of the July 2009 meeting was in fact a Memorandum of Understanding (MOU) that, while wholly procedural, committed the two governments to work intensively together toward the installation of national energy and environmental policies that will significantly cut their carbon emissions.[6] Two experts on US-China relations, Banning Garrett and Jonathan Adams, believe that this agreement has potentially game-changing implications and "could catalyze a global transition to low-carbon sustainable economic development"[7]:

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[4]Goldstein, Morris, and Nicholas R. Lardy. *The Future of China's Exchange Rate Policy*. Policy Analyses in International Economics 87. Washington: Peterson Institute for International Economics, July 2009.

[5] Bergsten, C. Fred, ed. *The Long-Term International Economic Position of the United States*. Special Report 20. Washington: Peterson Institute for International Economics, May 2009.

[6] The two meetings of the former SED in 2008 had already agreed on a Ten Year Energy and Environment Cooperation Framework that provided a foundation for the new MOU.

[7] Banning Garrett and Jonathan Adams. "Do We Know Change When We See It?" chinadialogue.net. August 27, 2009. Available at: http://www.chinadialogue.net/article/show/single/en/3231-Do-we-know-change-when-we-see-it

- the leadership of the two countries at the highest level now endorse climate-change science and take climate change seriously as a strategic threat to both nations and the world;

- the two are committed to scaled-up domestic actions to implement policies aimed at transitioning their economies to clean-energy systems and low-carbon development; and

- the strong and public commitments by the two leaders to both meet the climate-change challenge and to engage in unprecedented US-China cooperation is a new and essential ingredient to energize the two governments at all levels and the two business communities to vastly scale up their collaboration as well as national efforts.

Here too serious and sustained follow-through will be essential to realize the potential payoff. But there is now a common understanding of the strategic threat faced by the two countries, and agreement on both the essentiality and feasibility of China-US cooperation. Garrett and Adams conclude that the "humble MOU may be pointed to as a historic turning point that marked a strategic shift as important in its global impact as the US-China opening nearly 40 years ago."

The Future Agenda

Hence there is substantial evidence that the initial S&ED, building on other United States – China contacts and its own predecessor forums, has made an important contribution to resolving two of the central problems now confronting the world economy. Future meetings of the group will obviously need to expand this cooperation further but the startup has been impressive and deserves strong support.

There is much less indication that the two countries have been able to use the S&ED to address some of the other systemic issues that confront them. China has expressed great anxiety over the stability of its huge official dollar holdings (probably now above $1.5 trillion). It worries about possible restrictions on its future direct investments in the United States, as in the infamous CNOOC case and more recent instances involving Huawei and others.[8] The United States is concerned that China is resuming an industrial policy strategy that encompasses selection of "national champions" and wide-ranging subsidies for preferred sectors, as well as maintaining its currency intervention policy to preserve a substantially undervalued exchange rate for the renminbi.

There are additional important opportunities for G-2 leadership on key global economic issues. China and the United States need to get together on the related topics of stronger IMF

The underlying analysis is in *A Roadmap for US-China Cooperation on Energy and Climate Change*, a January 2009 report prepared by the Pew Partnership on Global Climate Change and The Asia Society.

[8] Daniel H. Rosen. 2009. *China's Changing Outbound Foreign Direct Investment Profile: Drivers and Policy Implications*. Peterson Institute for International Economics Policy Brief 09-14. Washington: Peterson Institute for International Economics.

surveillance of national economic policies (which China needs to embrace) and reform of the governance of the international financial institutions (where the United States needs to give up its veto over major decisions in both the IMF and World Bank and its "right" to select the President of the Bank). Both countries have a major(and frequently articulated) interest in preserving an open global trading system but they still appear at loggerheads over the Doha Round in the WTO, which their frontal disagreement brought to a screeching halt over a year ago. They have barked at each other's discrimination against foreign suppliers under their respective fiscal stimulus programs rather than joining together to renounce all such protectionism themselves and leading the way toward a new compact on government procurement policies that would proscribe such behavior everywhere.

It is particularly important that the two countries' new understanding on common strategic priorities to collaboratively address climate change be followed by sustained, scaled-up efforts. To be effective, the MOU's statement of common strategic interests must be translated to real projects on the ground. Tangible projects with clearly articulated goals must include a wide range of players in the public and private sectors. This collaboration will make it possible to create stronger constituencies which both contribute toward stated goals on climate change and foster greater transparency of domestic action and policies.

The United States and China will of course continue to have bilateral problems that must be addressed along with these systemic topics. Any two countries with such a large and growing volume of trade and investment will inevitably encounter periodic disputes; the largest number of trade conflicts arises between the United States and Canada, or sometimes the United States and the European Union, simply because they enjoy such extensive commercial ties. Even these more traditional problems will be easier to resolve constructively, however, in a G-2 context in which the United States and China have developed much more far-reaching mutual understandings and can place those issues in a broader systemic framework. [9]

The S&ED, at this early stage of its evolution, has both a positive record of achievement and a rich agenda for future action at both the broad conceptual and very practical policy levels. The two governments should be encouraged to continue, broaden and deepen the approach over the months and years ahead. I hope that the Congress will continue to monitor the process to make sure that it realizes its full potential.

[9] In this trade policy context, it is also important that President Obama reject the ITC recommendation to erect new barriers to import of tires from China. The low-grade tires that we import from China are no longer made in the United States, and are not going to be made in the United States, so the imposition of controls on imports from China would simply shift the sourcing of those imports to other countries rather than increase production and employment in the United States. Such a step just prior to the upcoming G-20 meeting would also be a major setback to its efforts to resist the spread of protectionism.

Mr. FALEOMAVAEGA. Thank you very much, Dr. Bergsten.
Mr. Schriver?

STATEMENT OF MR. RANDALL G. SCHRIVER, PARTNER, ARMITAGE INTERNATIONAL, L.C. (FORMER DEPUTY ASSISTANT SECRETARY FOR EAST ASIAN AND PACIFIC AFFAIRS, U.S. DEPARTMENT OF STATE)

Mr. SCHRIVER. Thank you very much, Mr. Chairman. Thank you for the invitation and thank you also for seating me along side people I respect and admire so much. I know we are somewhat judged by the company we keep, and I know my reputation is enhanced today. Thank you for giving me that opportunity.

Talking about a particular format or dialogue, I think it is important that we ground this in our impressions of the overall relationship because even the best modalities won't produce results if the fundamentals aren't there in the relationship. And the reverse is true as well. If the fundamentals are in place the form of dialogue will only marginally affect the outcomes.

I guess I would take a bit more of I don't want to be pessimistic, but maybe in my view at least a sober minded view of where things stand. I think although it is undeniable that our interests are converging in many ways, there are still very profound differences between the United States and China. Many of those issues have already been mentioned—human rights, the security of Taiwan, proliferation and so forth.

So I think even if we are extremely creative and come up with the best modalities, I think these profound differences will mean that the outcomes and the deliverables and the products I think will necessarily be modest, and I think that was frankly borne out in the first round of the S&ED. That doesn't mean the Dialogue shouldn't take place, but we should think carefully about how we characterize this dialogue and what our expectations are.

In fact, when the Chinese raised the prospects of holding a strategic dialogue, my boss at the time, then Deputy Secretary Armitage, agreed to a senior dialogue only. He said we reserve strategic dialogue for allies and people who share our views and share our interests, and I think that is an important point to keep in mind.

I think many of the advantages of this forum have already been discussed. I would underscore several of them. I do think it is useful to the interagencies on both sides. People have noted the Chinese interagencies are stove piped. I might hasten to add that is a problem on our side as well at times, and this format with so many cross-cutting issues does help interagencies on both sides interact and deal constructively on a range of these issues.

Obviously having a flagship dialogue of this magnitude can be an important action forcing event that can incentivize governments into action, and obviously having a format of this nature when things are said they are almost by definition authentic, authoritative and it is a great platform for communicating clear messages.

I think between the United States and China that single goal of clear communication to the extent it helps us avoid differences and conflicts and miscommunications, that in and of itself is important, but let me focus on what I think are a few of the potential

downsides, and I do so at the risk of sounding overly negative, but I want to use the time to be constructive and talk about what I think some of the potential pitfalls are.

Number one, I think we have inadvertently placed China in a place of priority or predominance that they haven't quite earned. I would note that Japan still has the second largest economy in the world. We have other major trading partners in Asia.

We have trading partners around the world who are more closely aligned to the United States, share our values, share our views, but yet, as was noted earlier, there has never been anything like this in terms of high level engagement with any of these countries, so I think inadvertently we have given the impression that China has a place of priority, which I don't think they quite frankly have earned through their actions and through their policies.

I think that segues into a second concern I have. We often place value differently on the outcomes of dialogues of this nature. China often judges success or failure based on symbolism, status. People say face in Asia. I think we run the risk sometimes of loading six or seven Cabinet secretaries on a plane, touching doing in Beijing, and the Chinese have already accomplished their objectives in the meeting without having to actually produce.

If they perceive they are already the great strategic partner of the United States, my feeling and based on my experience of interacting with China, that may actually decrease the possibilities that they will engage in constructive cooperation, and in fact there are a range of things we can and should be doing with our allies that are not only the right things to do with respect to those relationships and for our United States interests, but also is the smart thing to do in terms of engaging China.

I mentioned that it is a useful action forcing event, but the reverse could also be true. China often holds in abeyance initiatives and deliverables and outcomes until the next round of a major dialogue, so I think there is a potential downside of this diluting many of the other interactions we have; for example, the so-called JCCT, the Joint Commission on Commerce and Trade.

Another downfall and potential downside I would note is a lack of priority and a very unwieldy agenda in the S&ED format. I have noted what the representatives of the administration have said about prioritization. I take them at their word. I have a great deal of respect for both of them, but it is, very frankly, hard to see from the outside that there were clear U.S. priorities being conveyed in the S&ED. I think that that has the potential to dilute the possibility of achieving outcomes on what are truly the most important and strategic issues for the United States.

Finally, I worry a little bit about a sense of complacency; that we have so many ministers, so many Cabinet secretaries that we will be under the impression we are talking to all the right people and we have a vehicle that is sufficient for all the work that needs to be done in the United States-China relationship.

And in this regard it certainly underscores something Mr. Podesta said about the military-to-military relationship. I think if we could get PLA operators into a room to talk about safety on the high seas, that in and of itself would be just about equal value to

what we are getting with all these Cabinet secretaries and ministers.

I know my time is running very short. Let me just quickly conclude with some recommendations. I don't want to only cast aspersions. I think high level dialogue, senior dialogue, with China is important. I think it can be improved.

Number one, I think we should step up our cooperation with our allies. I think we should conclude CORUS, I think we should enhance our TIFA talks with Taiwan, and I think we should really take advantage of this fiftieth anniversary of the U.S.-Japan alliance coming up for a robust security declaration. Again, the right thing to do, but I think it actually helps us to engage China.

Number two, I think we need much greater clarity on the agenda for the S&ED so that we can really work on issues of true priority and the number of Cabinet secretaries and ministers adjusted accordingly if we are able to do that and focus on a more concrete and specific agenda.

Again, number three, other fora. We shouldn't be complacent about this S&ED as being all the right people, all the right issues. I do think military-to-military is extremely important.

And then finally, I do think we have created an impression, and I will only say that, that human rights is lower on the agenda than I feel it should be with China. I take the administration and Mr. Shear, again who I respect greatly. I take him at his word about the vigor with which these issues are pursued, but I did note China coming out of the S&ED almost thanking the United States for not raising the Uighurs and Xinjiang with greater intensity and forcefulness.

I don't take that as a good sign when we are being congratulated for things like that, and so I think some things should be done to re-energize those issues in the United States-China relationship. Thank you.

[The prepared statement of Mr. Schriver follows:]

The U.S – China Relationship and
the Role of the Strategic and Economic Dialogue

Testimony by Randall G. Schriver
Founding Partner, Armitage International and President of the Project 2049 Institute

Presented to the House Foreign Affairs Committee
10 September 2009

Mr. Chairman, thank you for the invitation to address this committee on the topic of U.S.-China relations and the role of the Strategic and Economic Dialogue (S&ED). I also want to thank you for seating me along side these impressive luminaries. If we're partly judged by the company we keep, I know my reputation is enhanced today by virtue of the company I'm keeping on this panel.

Mr. Chairman, I was asked specifically to offer some thoughts on the degree to which the S&ED is effective in promoting the U.S.-China bilateral agenda, as well promoting U.S. interests on a range of important regional and global issues.

In trying to provide constructive comments on this topic, I think it would be useful to address three separate questions: what are the prospects for U.S.-China cooperation in the near-to-medium term irrespective of the modalities for dialogue, what are the likely benefits and the likely downsides of the S&ED format as currently configured, and what specific policy steps would I recommend to strengthen or alter the current approach of the S&ED.

I think it is important to begin with a general assessment of the prospects for U.S.-China cooperation in the near-to-medium term. To a large degree, the modalities for dialogue and engagement are secondary to the fundamentals of the relationship itself. If our interests are aligned, and the obstacles are limited, the specific modalities chosen will only affect outcomes on the margins. The reverse is also true – if the overall relationship is adversarial and there is little basis for quality cooperation, even the best plan for engagement will produce little.

This is particularly important to assess in the case of U.S.-China relations. While it is undeniable that the United States and China are experiencing converging interests across a broad spectrum of issues, it is also true that our interests diverge in important ways. We cannot expect that there is some optimal formula for a dialogue format that will alter the fundamental fact that United States and China will find cooperation difficult in the near-to-medium term due to the aforementioned divergence in interests. We have profound differences over human rights, Taiwan's security, proliferation, and the future of U.S. military alliances in Asia.

I think it is also important that we give careful consideration to the policy areas where increasingly many analysts are describing common interests. I would submit that many of these issues – such as North Korea, global climate change, and peace and stability in the Taiwan Strait – are in actuality areas where we have common aversions, not common interests. A common aversion can be the foundation for dialogue and limited cooperation. But a common aversion is not enough to generate close cooperation and coordinated joint efforts.

None of this is to say dialogue is not worthwhile. I endorse high-level dialogue between the United States and China. But our expectations should remain modest, and we should be careful about treating this as a truly "strategic" dialogue – the official name of this Forum notwithstanding. In fact, when Strategic Dialogue was first proposed by the Chinese to the United States in 2004, then-Deputy Secretary of State Armitage agreed to regular Senior Dialogue only. He made of point to convey that the United States reserves true Strategic Dialogue for our closest allies who share our interests and our values.

The second question to address relates to the S&ED format itself. I acknowledge there are benefits to holding this particular forum. Specifically, I believe the S&ED strengthens interagency coordination within each respective government. There are so many cross-cutting issues on the agenda, multi-agency participation in the policy prescriptions is essential. The S&ED forces all the key players into a room, and compels all the players to examine common agenda items. Our own system has suffered historically from poor internal coordination. Reportedly the problem is worse in China. The S&ED helps in this regard.

The S&ED can also be a powerful forum to communicate clear messages to one another so as to avoid miscommunication or miscalculation. It would be difficult to question the authority or authenticity of a message delivered in the presence of so many Ministers and Cabinet Secretaries. Clear communication is a helpful outcome even if joint cooperation does not result. Conflict avoidance is an extremely important objective in the United States and China. However, we should add a cautionary note to this point. It is true that messages will be seen as more authoritative in a forum such as the S&ED – but it is also true that omissions can inadvertently convey a lack of interest in a particular issue. I fear the lost opportunity to raise the plight of the Uighers in Xinjiang during July's meeting of the S&ED left the Chinese almost gleeful that the U.S. government was not overly concerned with human rights conditions in Western China.

The S&ED can also be useful as an "action forcing event." Having a major flagship dialogue on the calendar every year can provide the right kind of incentives to the respective bureaucracies to make concrete proposals.

There are potential downsides to sustaining the S&ED format as currently configured – and I'll note five. First, it seems we have inadvertently placed our Chinese counterparts in a place of prominence that they have yet to earn. To put a finer point on this, we have no comparable dialogue with Japan Korea or other Asian partners. This can

engender feelings of insecurity among our closest allies. Japan in particular can still boast the second largest economy of the world – larger than China's – on top of being a close treaty ally, Yet our engagement with Japan lacks the same type of high-level flagship dialogue.

The aforementioned concern segues into the second potential downside I'll mention. China often measures success not by deliverables or concrete actions agreed upon – but on symbolism and status. If China perceives they are being treated as Washington's most important relationship, accompanied by all the symbolic trappings of a strategic partner, this may actually *decrease* their incentive to pursue consequential cooperation. In other words, treating Japan, Korea, Australia and others as valued allies and showing them respect befitting close allies is not only the right thing to do, it is also the smart thing to do in terms of incentivizing China. The key to a successful engagement strategy with respect to China often has little to do with direct interactions with China itself – and much to do with engagement of allies and others in the Asia-Pacific region as a means of impacting China's decision-making. This can be put differently: the way to get China right, is to get the rest of Asia right first. Attention and meaningful engagement of our allies in Asia will best position us for meaningful cooperation with China.

A third concern to note is actually the opposite side of the same coin mentioned above as a potential positive element of the S&ED. While it may be true that an annual S&ED serves as an "action forcing event" for both bureaucracies, it may also be true that little else can be accomplished in the interim. Our Chinese interlocutors often argue privately that movement on major initiatives and/or agreements must be held in abeyance until the next round of major dialogue (only to disappoint when the actual dialogue does roll around). The Administration runs the risk of structurally creating an environment where very little can be done in between meetings of the S&ED. This could also adversely impact "subordinate" Dialogues such as the Joint Commission on Commerce and Trade. Even worse, the Administration may feel constrained from taking punitive actions when needed (e.g. a potential WTO case or human rights resolution) in the lead-up to a Dialogue for fear of souring the atmospherics.

A fourth potential downside to the S&ED format as currently structured is the very unwieldy nature of the agenda, and the lack of focus to the Dialogue. While the Administration noted publicly that certain issues were prioritized within the S&ED, it was quite frankly difficult to discern that watching things unfold. Admittedly, there are parts of the S&ED that are rightly kept private and behind close doors. Even if those private messages were much more pointed – and I might add I suspect the Chinese messages on Tibet and Taiwan were quite sharp in private – the effect can be diluted by a public Dialogue that meanders from the Middle East to health care to regional architecture and so on.

And finally, I will register concern that an S&ED process can breed false confidence on the U.S. side with respect to personal relationships between U.S and Chinese interlocutors. It is a common argument that an S&ED process can help build

mutual trust and can create stronger personal relationships between principle actors that can be leveraged in both good times and bad. However, history belies this theory altogether. In fact, this is a very American trait in diplomacy to want to have personal relationships with interlocutors, to have direct phone lines that can be called in crisis, and to have confidence that decisions made in the private council of the other government will take personal relationships into account. But the Chinese do not share this trait in diplomacy. In past times of crisis, even "old friends of China" could not get their phone calls answered. There is no reason to believe Chinese government officials would behave any differently in the future. Further, a flagship dialogue with such high-level participation on both sides could lead to complacency in thinking that we are linking up with all the important actors under the auspicious of this single forum. Yet we still have precious little interaction with the most important members of the People's Liberation Army (PLA) and virtually no crisis communication modalities in which we can have confidence.

Let me reiterate, I support high level dialogue between the United States and China – but I think the foundation for cooperation overall is relatively weak, and the many downsides embedded in the current S&ED format give me little optimism for robust cooperation emerging. I think there is ample evidence from the first S&ED last July to support this view. The Administration set extremely low expectations for the Dialogue…then met them. But those are hardly the results on climate change, the global economic crisis, and regional security cooperation worthy of the time and energy invested by so many senior people in the U.S. government.

I still believe we can do better. With respect to specific policy steps, I offer the following four specific recommendations

1) The U.S. should enhance our engagement of key allies in Asia in both *form* and *substance*. We should have high level engagement with Japan, Korea and Australia that conveys a place of priority for our allies. The United States should move immediately to conclude KORUS, should enhance TIFA talks with Taiwan, and should commence efforts to achieve a robust security declaration on the upcoming 50th anniversary of the U.S.-Japan alliance. These are the right policy steps for U.S. interests. In addition, these steps with friends and allies will create the right kind of incentives for China to pursue constructive cooperation with the United States.

2) The United States should limit the subject matter covered in the next S&ED to reflect true priorities. Rather than an unwieldy agenda that threatens to dilute our messages of urgency on issues critical to our national interests, we should pursue a much more focused discussion when the S&ED resumes in China next year. We should reduce the number of cabinet secretaries who participate accordingly. At present, the United States should vigorously pursue greater Chinese cooperation on matters related to Pakistan and Afghanistan. Depending on where things stand next summer, the issue could very well be appropriate as a top agenda item for the coming S&ED.

3) The S&ED should not become an excuse for missing other creative approaches to problem-solving in the U.S.-China relationship. The United States should continue to press China for active participation in fora that may prove to be even more consequential than the S&ED. For example, it is conceivable that our greatest bilateral gains could come from active Chinese participation on the part of the PLA in an operator-to-operator dialogue focused on safety on the high seas.

And

4) The United States should re-introduce the important topics of human rights and religious freedom as issues of core concern to our government, our Congress and our people. These issues should be raised by President Obama as well as by participating cabinet secretaries of the S&ED.

Mr. FALEOMAVAEGA. Thank you very much, gentlemen.

The gentleman from California for his questions.

Mr. ROHRABACHER. Thank you very much, Mr. Chairman. Let me note in terms of a little comment on your original comment, which was how China has had such stability, economic stability, when there has been such economic chaos going on in the United States and the western markets.

I think that if you live in a country where they have killed the lawyers and jailed all the union organizers and cut off all free press and political opposition, it would appear to be a stable regime.

Mr. FALEOMAVAEGA. Will the gentleman yield?

Mr. ROHRABACHER. And you could actually make sure the profit is directed toward the right people. Yes, sir.

Mr. FALEOMAVAEGA. I think it was one of the great writers, a fellow by the name of William Shakespeare, who said the first thing we do is kill all the lawyers.

Mr. ROHRABACHER. Well, the Chinese have certainly read that one all right.

So let us note that that is the kind of society. There is a facade of stability and strength, but I think that underneath that is you have millions and millions of Chinese people who long for the same things that we long for, and that is to be able to live in freedom and to have better lives for our children and to express ourselves and to be able to worship God as they see fit.

I think these are not things that only westerners want. I think that the Chinese people, I see them as our greatest ally, and they right now have a boot on their face and it does not do us any good or the world any good to ignore that fact and to just talk about how we can cooperate with the guy who has the boot on his foot and that boot is on the face of their own people.

So with that said, let me ask a question because the first two witnesses seemed very optimistic about cooperation. As a matter of fact, your whole testimony was about how we cooperate with this regime. Pardon me for being cynical here, but do either one of your groups receive contributions or have clients from business that are making profit from the China market?

Mr. PODESTA. I will let Mr. Bergsten answer for his group. We take small corporate contributions at the Center for American

Progress generally in the vicinity of $25,000, but never for any work that we do, and so I think that we have no economic stake in the people that——

Mr. ROHRABACHER. By the way, $25,000 does not sound like a small contribution to me.

Mr. PODESTA. Well, we take contributions from corporations as part——

Mr. ROHRABACHER. But do you make a profit from China-to-China trade? More than $5,000?

Mr. PODESTA. You know, we do no work on their behalf and we take no corporate contributions to do particular studies, Mr. Rohrabacher.

Mr. ROHRABACHER. Okay. I understand. You do take contributions.

Mr. PODESTA. We take union contributions. We take individual contributions, and we take corporate contributions.

Mr. ROHRABACHER. There it is. Okay. I am just asking. People need to know who is talking. We have a group that takes $25,000 contributions from people who are doing business with gangster regimes.

Now, what about your organization?

Mr. BERGSTEN. About a third of our funding comes from philanthropic foundations, about a third from individuals, about a third from companies, some of which certainly have business in China.

Mr. ROHRABACHER. All right.

Mr. BERGSTEN. They of course have businesses in hundreds of countries, and we take——

Mr. ROHRABACHER. Sure.

Mr. BERGSTEN [continuing]. Funding for our China related projects——

Mr. ROHRABACHER. Okay.

Mr. BERGSTEN [continuing]. From companies that are involved in——

Mr. ROHRABACHER. And what size? We heard about $25,000 is the biggest contribution from any business that does business in China from his organization. What about the biggest contribution from a company that does business in China for your organization?

Mr. BERGSTEN. Well, we are much better fundraisers than Podesta so we get more than that from some companies.

We get $10,000 from some, $5,000 from some. But I suspect—I would have to check the record—we get $50,000 or more from a couple of companies——

Mr. ROHRABACHER. All right.

Mr. BERGSTEN [continuing]. That have business in China.

Mr. ROHRABACHER. All right. So we understand, okay? No one is saying that what you are saying is untrue or that you don't believe it, but that is the environment in which you are working.

So with that said, and again you are focused on cooperation. I will have to say I am a little flabbergasted by someone who would suggest that the United States be viewed in the world as a partner with the world's worst human rights abuser and that in some way is going to have a positive impact with the G–2, but let me ask this question of you all.

Mr. BERGSTEN. Could I answer that directly?

Mr. ROHRABACHER. Yes, you may. Go right ahead.

Mr. BERGSTEN. Because you raise a very fundamental question. It comes up all the time in our debates on how to organize the world. There are two conflicting schools of thought.

One would say, and that is what I have said, that when another country is the world's second largest economy, second most important economy, and you can't really make progress on any global economic issues without it. You have to deal with them as effectively as you can.

Your view is that despite all that if their values are not ones we share——

Mr. ROHRABACHER. Yes.

Mr. BERGSTEN [continuing]. That you stay distant.

Mr. ROHRABACHER. Right.

Mr. BERGSTEN. And I think one has to reconcile the two as best one can, but one has to ultimately choose which way you lean.

I think honest people can disagree, but I don't see how we can promote our economic interests unless we deal effectively and extensively with the world's second largest and most important economy.

Mr. ROHRABACHER. Well, as Mr. Schriver pointed out, Japan for a long time was the world's second largest and we never tried to afford them the type of prestige that you are suggesting we move forward with China.

Mr. BERGSTEN. Not actually true, Mr. Rohrabacher.

Mr. ROHRABACHER. Okay. Let me move forward with a couple things here.

Mr. BERGSTEN. We were very close with Japan with many, many——

Mr. ROHRABACHER. Okay. Let me just note this. First of all, I have heard from the business community for year after year after year, for decades now, that if we just deal with these people in a cooperative spirit and really treat them as friends that there will be a liberalization going on.

I have not seen any liberalization going on in the Chinese Government throughout this expansion of economic relationships, and I believe that the hug-a-Nazi-make-a-liberal theory has not worked. We have hugged them, we have kissed them, we have put our investment money in their pockets, we have helped build their economy, and they still have a fascist regime in Beijing.

One last question, and that is right now which do you believe to be the worst threat to the stability and peace of the world, the Somali pirates or China's claim to almost the entire South China Sea?

Which one, the Somali pirates or this major massive power laying claim to all of the trade routes through which Japan has to bring all of its oil into almost all the entire South China Sea? Do you think that claim is a belligerent, arrogant act on the part of the Beijing?

Mr. PODESTA. If you are forgiving the Somalia pirates, I don't know why.

Mr. ROHRABACHER. Okay.

Mr. PODESTA. I mean, it seems to me that we need to deal with both questions or both security issues, but, you know, you see the

world as black and white and I see it I guess in shades of gray, Mr. Rohrabacher.

Mr. ROHRABACHER. Okay.

Mr. BERGSTEN. I would like a few more choices. You just gave two choices and which is the greatest threat.

Mr. ROHRABACHER. Okay. What about for you, Mr. Schriver?

Mr. BERGSTEN. There are a number of countries, incidentally, that claim portions of the South China Sea and the Spratlys and all that——

Mr. ROHRABACHER. Right.

Mr. BERGSTEN [continuing]. So it is not only China. It is literally last count I think eight or 10 countries in Asia that——

Mr. ROHRABACHER. I will have to say, when the Philippines go out there with their little putt-putt patrol boat and say yes, we own this much of the South China Sea it doesn't seem as threatening as when the Chinese claim the whole thing.

What about you, Mr. Schriver?

Mr. SCHRIVER. Well, I wouldn't hesitate to say that China represents the greatest potential threat to the United States.

It doesn't imply necessarily the full policy prescription of what we do about it, nor does it say that there aren't potential opportunities as well, but I think their trajectory, we have to be very sober minded about that.

Mr. ROHRABACHER. Thank you, Mr. Chairman.

Mr. FALEOMAVAEGA. Thank you. We are joined now by our distinguished ranking member, the gentleman from Illinois, my good friend, Mr. Manzullo. If he has an opening statement or a series of questions he would like to——

Mr. MANZULLO. I ask that my opening statement be made part of the record.

Mr. FALEOMAVAEGA. Definitely. Without objection.

[The prepared statement of Mr. Manzullo follows:]

COMMITTEE ON FOREIGN AFFAIRS
SUBCOMMITTEE ON ASIA, THE PACIFIC, AND THE GLOBAL ENVIRONMENT
U.S. HOUSE OF REPRESENTATIVES
WASHINGTON, D.C. 20515

Donald A. Manzullo (IL-16), Ranking Member
Opening Statement

September 10, 2009

Mr. Chairman, thank you for calling this hearing regarding the Strategic and Economic Dialogue (S&ED) between the United States and the People's Republic of China. Given the importance of the overall relationship between our two nations, the existence of a mechanism where senior-level leaders can regularly meet and discuss issues of mutual importance is extremely valuable. The true measure of success for President Obama's S&ED, as with the Bush Administration's Strategic Economic Dialogue, is whether increased contact translates into outcomes of real significance.

I strongly hope that as a result of this new discussion framework, the U.S. and China can build a more positive relationship, particularly on trade and environment. China's recent move to eliminate tariffs on American auto parts exports into their country, prompted by a World Trade Organization ruling, is a positive step in the right direction. However, I hope that our two governments can work closer together so that trade matters can be resolved without the frequent use of the WTO dispute settlement mechanism and other fair trade remedies in U.S. law. For example, last year, the U.S. International Trade Commission ruled in favor of the workers I am proud to represent at Titan Tire in Freeport, Illinois and other off-the-road tire manufacturers to stop illegal dumping and government subsidization of Chinese-made tires. Yesterday, the Commerce Department determined that China steel pipe producers have received illegal government subsidies. If the S&ED can reduce the trade tensions and make China play by the trade rules that they agreed to, then it will be considered a great success.

The S&ED must not become yet another forum for endless conversation and symbolic gestures. The Administration must be willing to push the Chinese side to make real changes now that the dialogue has been elevated to such a high-level event. We must also remember that there are other friends and allies in the Asia-Pacific region that have done a lot to enhance their relationship with the U.S. The U.S. must not forget countries like Japan and Korea in our effort to improve relations with China.

I look forward to your testimonies.

Mr. MANZULLO. You know, we have been working with China ever since I came here in 1993. I served as the first chair of the U.S.-China Interparliamentary Exchange, have been to China several times, helped entertain the Chinese here in the United States, and one of the impressions that I get it is very hard to refer to the "Chinese" as one people just as it is hard to refer to Bergsten and Podesta as people of like mind.

And I say that facetiously because depending upon the area of China with which you are dealing or the individual we have found some extraordinary open people that have really in individual cases gone to bat for United States companies that were getting clobbered by the Chinese themselves in various parts of that country, so I find it——

I know we are still dealing with a country that is closed and I am disappointed it is not more open than we anticipated in light of the different laws that we have passed regarding China's trade obligations, et cetera, but one of the things that I want to explore with you, and this comes as a person who also sits on the Financial Services Committee.

I am really concerned that the Chinese, which owe over $800 billion in U.S. notes, the first part of April at the G–20 had talked about a bag of currencies, cache of currencies, whatever it is, to supplant the U.S. dollar as a currency of reserve for international trade purposes.

On April 2, the G–20 signed an extraordinary agreement that sort of indicated that, and prior to that Secretary of Treasury Geithner had made some remarks that perhaps he hadn't studied talking about this substitute for the U.S. reserve. China now of course wants more of a say so in the G–20 because they are putting more money around the world.

My question to the three of you is what implications would happen if the U.S. dollar no longer is the international currency of reserve? That is an easy question. Who wants to start with that? Fred?

Mr. BERGSTEN. Let me start. Sure. First of all, the Chinese holdings of dollars are probably more like $1.5 trillion now, almost double what you said. We can only record about $800 billion of their direct holding of U.S. Government paper, but the estimated total is close to double that and rising very rapidly, whatever they may say about their unhappiness about dollars.

I made the point before that they have intervened massively in the currency markets to keep their exchange rate undervalued to improve their trading competitiveness. The way they do that is to buy dollars. They buy dollars, sell renbinmi. It holds the price of the renbinmi down against the dollar, gives them more price competitiveness.

The financial consequence is their dollar reserves keep rising so whatever anxieties they may enunciate they keep piling up dollars more and more. So one can understand that they want the best of all worlds. They want to be able to keep their currency down, but also get some kind of takeout for the dollars that they hold. I don't think they are likely to get that.

I am not sure what you referred to in the G–20 in April, but it may have been the decision to create a large amount of special

drawing rights at the IMF to supplement global reserves. In an indirect way you might say or might interpret that as a response to the anxiety of China and some other countries incidentally—Russia and some others—about their large dollar holdings, but I think the G–20 viewed that, and rightly, as part of the response to the global crisis.

The idea of creating special drawing rights through the IMF is to add to the reserves of all member countries around the world. That gives them more wherewithal to buy imports, restore the level of international trade, which has dropped so sharply, and thereby contribute to the global economic recovery. It is legitimate to say a side effect is to slightly decrease the role of the dollar in world finance.

The SDRs up until now have accounted for something like 0.2 percent of all global financial reserves. The decision at London—it has now been implemented, incidentally, August 28 by the IMF—takes the SDR share of total reserves up to 5 percent not by reducing the amount of dollars but simply by increasing an alternative asset.

Now, what would happen if the dollar no longer becomes the key reserve asset? First of all, that could not possibly happen for a very, very long time. The dollar is the currency of international commerce. It is used in variously estimated 70–80 percent of all international transactions, including by countries far away from us geographically, so there is not much risk that its role is going to diminish any time soon. There just wouldn't be any technically feasible way to do that.

I may shock you, however, when I suggest that a gradual and orderly reduction of the dollar's role might not be such a bad thing for the United States. Why do I say that? First of all, the dollar enables us to finance our huge trade deficits much more easily. That is generally viewed as its main benefit. We can live beyond our means. We can buy more from abroad than we sell because the foreigners are willing to pile up dollars, finance our debit card as if nobody was collecting on principal, and so we can live beyond our means. In the short run that is attractive.

But it also means that we often pursue policies that are not greatly in our own interest, and I would submit that the huge foreign financing of our huge trade deficits was an important cause of the current crisis. Why? All those dollars came in from China and elsewhere. They kept our interest rates very low. They kept our monetary conditions very lax. They kept our liquidity extremely high.

The Chinese did not force our banks to make stupid subprime loans, but the conditions, the monetary conditions, that ensued were an open invitation to overleveraging, underpricing of risk, all the things that brought on the crisis. In short, the great financing of our big deficits and all that wonderful foreign capital inflow created conditions that really rose up to bite us.

There is a second reason why it is not such a great thing for the United States to have all this foreign dollar financing, and my China example describes it. The Chinese manipulate their exchange rate because they can buy dollars in the currency market and keep their currency low. That overvalues our currency, makes

us less competitive in world trade, brings on those big trade deficits and to some extent job losses here. We don't control our own exchange rate because of the international role of our currency.

So it is a mixed bag. I don't want to be totally negative. There are advantages and disadvantages. It is a complicated business. I wrote a book on it a long time ago. I have just done a big article for the next Foreign Affairs issue addressing that whole set of topics.

But I for one would believe that over time as we move into a more multipolar world economy where the euro is rising as a national currency, where the IMF can create this alternative asset, it is probably a good thing for the United States to have that greater variety.

The United States in fact was the country that initiated the idea of special drawing rights in the IMF 40 years ago and again strongly supported the G–20 action to create the $250 billion just in the last few weeks, and I think that is a constructive course for U.S. policy.

Mr. PODESTA. Mr. Chairman, could I just add one word to that?

Mr. FALEOMAVAEGA. Please.

Mr. PODESTA. I defer to Fred's expertise on this, but it seems to me that he is laying out a solution that the implication may be that the course should be to weaken the dollar and weaken the reserve position of the U.S. dollar, and it seems to me that the more effective way to approach this problem is actually to get our macroeconomic policy right and fix our own economy and retain the strength of the dollar as a reserve asset by doing things like returning to fiscal discipline and creating a macroeconomic policy that is going to have wage growth happen in the United States so that the pressure to kind of borrow our way into prosperity is reduced as people's incomes rise.

Mr. SCHRIVER. Well, I am not an economist, but as a China watcher I would say that I think much of their actions and statements are actually driven by insecurity. They never invested in U.S. dollars and held U.S. dollars out of affinity for us or love of us or because they wanted to be nice to the United States. It is the best place for them to keep wealth and hold wealth.

And they are nervous. They are nervous by our profligate spending. They are nervous by the trajectory of things right now, and I would completely agree that the best thing we can do is return to fiscal discipline as soon as possible. Otherwise this dynamic will surely continue.

Mr. BERGSTEN. Just to be clear, that is exactly the same policy conclusion I come to and stress in the upcoming article, but I do have a somewhat different view on whether the international role of the dollar is a great thing for the United States.

Mr. MANZULLO. I appreciate your answers on all of those, and as somebody who spends probably 60 percent of his time in Congress working on manufacturing issues—I think I am the only member who has gone to warehousing school—I am concerned over the drift actually started with Chairman Greenspan, who never thought the loss of manufacturing jobs was significant. Fortunately, Chairman Bernanke takes the opposite view and is concerned about every sin-

gle job that we lose to a foreign competitor and very sincere and very earnest in that.

I think it is a matter of how you look at this thing. Mr. Podesta, I don't know how the United States can get its macroeconomic house in order. I don't think we could sit down and all agree to wear the same color tie on alternative Wednesdays. Excuse me, Mr. Chairman. Or bolo ties or whatever we are going to wear.

You know, you could take piecemeal what we see going on in manufacturing in this country, and I see often times a company will say either—a large company will tell a supplier either you are going to knock out so much per dollar or we are going to take it to China, and often times there is no supplier from China. It is used as a paper dragon, if I could use that term. Many of the suppliers say all right, if you want to buy that thing from China, and then there is a pause and a hesitancy.

What I see going on is a lot of these jobs are going to China. A lot of the price to the suppliers is being forced down by the manufacturer who threatens that. I don't think you can develop a macroeconomic policy when China is used both as a source of manufacturing and as a threat of source of manufacturing. I just don't see how we can overcome that except to make U.S. manufacturing more competitive.

There are any number of ways that could be done through the work we are doing on export controls and things of that nature, but I had just asked for a comment. I didn't really ask for a solution because I know none is here. I appreciate the comments of each of the three of you.

Mr. BERGSTEN. Just to say very briefly, I very much agree. The reason I have railed rather adamantly against China's exchange rate policy is because it contributes very importantly to the erosion of United States manufacturing and job base that you indicated.

Certainly we have to do everything we can domestically in terms of fiscal policy, as John said, and in terms of tax policy to maintain a competitive base here for the manufacturing sector and job creation.

Mr. MANZULLO. If I could quote, when Madame Wu Yi was here this was April 22, 2004, the U.S.-China Business Council—I think, Fred, you were at that meeting—she made the most extraordinary statement, so extraordinary I had to record it forever in my Blackberry.

She said China has a "market based managed unitary floating exchange rate." I thought I had heard that wrong, and then she had actually put out an English translation. Actually she spoke in English. I said how could you have a market based managed unitary floating exchange rate, but that is their definition of their fair currency.

I thought you would enjoy that, Chairman. Do you like that? Thank you.

Mr. BERGSTEN. It is a double oxymoron.

Mr. MANZULLO. Well, whatever it is.

Mr. FALEOMAVAEGA. Unfortunately my good friend from California has had to leave, but I wanted to just share with him a little sense of my perspective about our relationship with China.

China is not a perfect country, but neither is the United States or any other country in the world for that matter. And I say with a sense of a historical perspective, that at the height of the Cold War we had a major adversary almost to the brink of using nuclear annihilation if you will.

But something happened in 1972—to President Nixon's and Mr. Kissinger's credit—to have a dialogue with the most powerful Communist country, I guess the most populous at that time. Mao Zedong and Zhou Enlai, literally changed not only the balance of power in the world, but probably in my humble opinion made a better world. The fact is that this historical event in my humble opinion was due to China's willingness to deal with us, a matter of power politics, if you will, but they did.

They were willing to dialogue to the point where we eventually established a formal diplomatic relationship. So I wanted to share that with my friend from California, but maybe next time.

Gentlemen, I know it has been a long afternoon and certainly want to commend all three of you for your most eloquent statements and opinions in terms of this very important issue.

I just wanted to ask Dr. Bergsten. I think it was at one time China wanted to propose an idea of an international currency rather than using the dollar as the basis of all other currencies. What do you think of that idea?

Their concern comes about because of what we have done in terms of our own economic recession, which has literally affected the entire world economy, including their own, I suppose, as being worried about almost a $1 trillion investment in the United States. Japan almost a $900 billion investment.

What do you think of the idea? Why don't we have an international currency rather than just relying on the dollar or other forms of currency?

Mr. BERGSTEN. The IMF currency that I mentioned before, the special drawing rights are actually an international currency, and, as I said, with the creation of a large new amount in the last few weeks it has now become at least a modestly significant component of monetary reserves held by national governments.

However, there are no private markets in that currency. When it was first created in the early 1970s there were in fact some nascent efforts to create a private market, and it was used to denominate some contracts and some bonds and things like that, but it never caught on.

It could. It could become used in the private sector if individual financial institutions and companies decided they wanted to do so, and that would move us toward a more internationalized monetary and economic system. As I said before, I do not think that is likely.

The dollar has huge advantages of convenience. The United States is by far, for all its recent problems, the deepest and broadest financial market in the world, so right through the crisis, countries and private actors around the world have continued to build their dollar balances.

In fact, one of the most interesting and some would say ironic elements of the crisis, which was of course initially caused in the United States, was that the exchange rate of the dollar strengthened very sharply throughout the crisis. Why was that? In the

depths of the problems and fears about economic security and financial stability there was a flight to quality and the safe haven of U.S. Treasury securities and the dollar.

Therefore, our interest rates went to virtually zero. Our exchange rate strengthened. All that was a result of world demand for dollars in the teeth of a crisis largely caused by the United States.

Now, that does indicate that the dollar is not about to go away any time soon as a global currency, but if one wanted to move incrementally toward a bigger role for an international asset, that move has already begun and could be elaborated.

Mr. FALEOMAVAEGA. Mr. Schriver, you indicated earlier that you don't think China has earned her stripes of being in standing with the United States not necessarily as a co-equal economically, but substantively in any other way that it seems to be.

Can you elaborate a little further by saying what does she have to do to earn being a co-equal partner with the United States that you seemed to have reservations about?

Mr. SCHRIVER. Well, my own opinion is that it goes beyond the size of the economy and the size of the population in terms of how you interact with another country.

Undeniably, I wouldn't question anything that was said earlier about the importance of working with China to deal with the whole swath of global and regional issues. It is far easier to get things done if China is on board and I daresay almost impossible in some cases, depending on the issue, to get things done if they are an adversary to you on those issues. But I do think symbolism matters in international relations and I do think tactics in terms of how you approach another country can be consequential.

As I said in my testimony, I think elevating China to this position before they have earned it, and I will add a thought or two on that, actually can create the wrong kinds of incentives or disincentives for them to cooperate constructively because they do value that symbolism and that status much more than other countries.

So I have always not pulling back on how we engage China, but to ensure that our allies are properly positioned, we are doing all the things like to create a United States free trade agreement, TIFA talks with Taiwan, a robust security declaration with Japan and so forth so that China understands we still have close allies and valued allies and we are doing things with them, in addition to what we are doing with China.

I would suggest actually, and maybe this is out of line with other panelists and the administration, but I think the cupboard is actually very bare on United States-China cooperation if you want to really talk about meaningful consequential outcomes.

And I know there is a range of issues people point to. North Korea, for example. I think the cupboard is very bare there. Proliferation, global climate change. I think we have really yet to see truly constructive behavior from China and constructive cooperation. On top of that, I think you have some pretty irresponsible behavior in the international community, and much of that was mentioned earlier, so what I am really talking about is tactics and how to get the right kinds of outcomes.

I am not suggesting we shouldn't be engaging in China at a high level, nor am I suggesting it is unimportant to do so. It is just, how do you get the outcomes you want?

Mr. FALEOMAVAEGA. Mr. Podesta?

Mr. PODESTA. Well, I would probably come down someplace in between Mr. Bergsten and Mr. Schriver. I think the G–2 is a bad construction. I don't think the Chinese want that. I don't think the United States wants it. Maybe it is a kind of glib construction. I don't know, Fred.

But it seems to me that the relationship—we should not be sending the signal to the rest of our partners that somehow China and the United States are going to kind of control or dominate the international architecture on either the economy, security or the environment as we have talked about, but we need China in all those relationships, in all those arenas, and I think that the Strategic and Economic Dialogue opens the door to strengthen that relationship, strengthen the partnership.

I think that a number of the potential outcomes have already been mentioned. We have spent a lot of time thinking through again the energy and climate aspect. If you take the two countries together, there is more than 40 percent CO2 emissions globally from the United States and China.

If we both don't move forward, both independently but also together, then I think the world faces tremendous challenges again across all those dimensions: On the environment with respect, but there is also an extreme security dimension to the impacts, potential impacts of climate change, and obviously there is tremendous economic impacts as well from severe storms from the other consequences that have been well noted.

I think we need particularly in that arena, if you will, we need cooperation for sure on the research and development side, on the technology deployment side, but we also need diplomatic cooperation to ensure that the world moves forward. I think the same is true with respect to the security arrangements.

I actually think that particularly this year the Chinese have actually been, and I say this from the perspective of not just listening to what I have heard in the United States and in Beijing, but actually what I heard in the DPRK. I think that the Chinese have surprised to some extent the North Koreans in the vigor with which they reacted to the missile launch and to the nuclear test.

So I think they are an important player globally and we need to strengthen our relationship, and clearly from the economic perspective we could find ourselves in a very unfortunate rapid delinkage I suppose in the near term, but what we need to do I think is find a way forward that is going to work for the United States fundamentally, and that is going to require the Dialogue that I think you heard from the first panel.

Mr. FALEOMAVAEGA. In fairness to the administration, the first meeting was held in July, and I think in fairness to what they are trying to do they are trying to sieve through what exactly the issues that are relevant and important. And I suppose the more we get the results of that dialogue that we can probably make a better judgment of how this concept is being taken by both countries.

But I do, as I am sure my colleagues will take a tremendous interest in where the S&ED is taking us for the future. And I kind of like to follow Dr. Bergsten's idea of being positive and constructive, and I think this is what I believe honestly in my dialogues with the leaders of China is their desire as well.

I suppose it all comes down to one word, gentleman, and that word is trust. Ideologically different, but I don't think you will find the Chinese any different in terms of their desire to have the same things that we want in life here in our society.

You gentlemen have been so patient and so kind to give us your precious time. I sincerely hope that this hearing has been good for the public and especially for my colleagues. All your statements have been made part of the record. Without objection, if you wish to submit any additional materials to be made part of the record, I would welcome it.

Gentlemen, I am sorry I don't have any Kalua pig to give you for this afternoon, but maybe on another occasion. Thank you so much for coming.

The hearing is adjourned.

[Whereupon, at 3:16 p.m., the subcommittee was adjourned.]

APPENDIX

Material Submitted for the Hearing Record

SUBCOMMITTEE HEARING NOTICE
COMMITTEE ON FOREIGN AFFAIRS
U.S. HOUSE OF REPRESENTATIVES
WASHINGTON, D.C. 20515

SUBCOMMITTEE ON ASIA, THE PACIFIC AND THE GLOBAL ENVIRONMENT
Eni F. H. Faleomavaega (D-AS), Chairman

September 3, 2009

TO: MEMBERS OF THE COMMITTEE ON FOREIGN AFFAIRS

You are respectfully requested to attend an OPEN hearing of the Subcommittee on Asia, the Pacific and the Global Environment to be held in Room 2172 of the Rayburn House Office Building:

DATE: Thursday, September 10, 2009

TIME: 1:00 p.m.

SUBJECT: U.S.-China Relations: Maximizing the Effectiveness of the Strategic and Economic Dialogue

WITNESSES:

Panel I
Mr. David Shear
Deputy Assistant Secretary
Bureau of East Asian and Pacific Affairs
U.S. Department of State

Mr. David Loevinger
Executive Secretary and Senior Coordinator for China Affairs and the Strategic and Economic Dialogue
U.S. Department of Treasury

Panel II
Mr. John Podesta
President and Chief Executive Officer
Center for American Progress

Mr. Fred Bergsten
Director
Peterson Institute for International Economics

Mr. Randall G. Schriver
Partner
Armitage International, L.C.
(*Former Deputy Assistant Secretary for East Asian and Pacific Affairs, U.S. Department of State*)

By Direction of the Chairman

The Committee on Foreign Affairs seeks to make its facilities accessible to persons with disabilities. If you are in need of special accommodations, please call 202/225-5021 at least four business days in advance of the event, whenever practicable. Questions with regard to special accommodations in general (including availability of Committee materials in alternative formats and assistive listening devices) may be directed to the Committee as noted above.

COMMITTEE ON FOREIGN AFFAIRS

MINUTES OF SUBCOMMITTEE ON ASIA, THE PACIFIC AND THE GLOBAL ENVIRONMENT

Day: Thursday

Date: September 10, 2009

Room: 2172 Rayburn House Office Bldg.

Start Time: 1:07 p.m.

End Time: 3:14 p.m.

Recesses:

Presiding Member(s): Chairman Eni F.H. Faleomavaega

CHECK ALL OF THE FOLLOWING THAT APPLY:

Open Session	X
Executive (closed) Session	
Televised	X
Electronically Recorded (taped)	X
Stenographic Record	X

TITLE OF HEARING: "U.S.-China Relations: Maximizing the Effectiveness of the Strategic and Economic Dialogue"

COMMITTEE MEMBERS PRESENT: Rep. Manzullo, Rep. Inglis, Rep. Rohrabacher, Rep. Royce

NONCOMMITTEE MEMBERS PRESENT:

WITNESSES: Same as meeting notice attached? Yes X No ____ *(If "no", please list below and include title, agency, department, or organization.*

ACCOMPANYING WITNESSES: *(Include title, agency, department, or organization, and which witness the person accompanied.)* Jeff Miotke, Deputy Assistant Secretary, State Department, accompanying Mr. Shear (witness).

STATEMENTS FOR THE RECORD: *(List any statements submitted for the record)*
Chairman Faleomavaega, Ranking Member Manzullo, Rep. Watson, Mr. Shear (witness), Mr. Loevinger (witness), Mr. Podesta (witness), Mr. Bergsten (witness), Mr. Shriver (witness)

TIME SCHEDULED RECONVENED _____ **or TIME ADJOURNED** _____

Lisa Williams
Staff Director

Statement
Congresswoman Diane E. Watson
Subcommittee on Asia, the Pacific, and Global Environment
Committee on Foreign Affairs
Thursday September 10, 2009
2172 Rayburn House Office Building
1:00 p.m.

"The U.S. - China Relationship and the Role of the Strategic and Economic Dialogue"

Good Afternoon, Mr. Chairman. Thank you for holding this timely hearing on US-China Relations, specifically the new Strategic and Economic Dialogue. This Dialogue uniquely offers the U.S. State and Treasury Departments joint interaction with their Chinese counterparts.

However, this emerging Strategic and Economic Dialogue with China presents a bit of a dilemma. On the one hand, it encourages high level interaction with a nation that has traditionally kept its doors closed. On the other hand, the schedule and the large portfolio of

issues under discussion make the forum a cursory interaction. Meetings have been held only twice a year, with seemingly little interaction throughout the remainder of the year. It is important to gauge the Chinese reaction to a broad range of issues, but the strategic aspect of this forum leads me to believe that it should focus its discussion on a few issues and pursue them diligently.

Though I believe that this forum affords the U.S. rare insight into Chinese policy, we must evaluate if the structure of the forum is the most beneficial approach. I hope our panelists can also enlighten us on how this forum fits into overall US-China diplomacy. Thank you, Mr. Chairman, and I yield back the remainder of my time.

ADDITIONAL MATERIAL SUBMITTED BY THE HONORABLE ENI F.H. FALEOMAVAEGA, A REPRESENTATIVE IN CONGRESS FROM AMERICAN SAMOA, AND CHAIRMAN, SUBCOMMITTEE ON ASIA, THE PACIFIC AND THE GLOBAL ENVIRONMENT

Statement of Jon M. Huntsman, Jr.
Ambassador-Designate to the People's Republic of China
Submitted to the Senate Foreign Relations Committee
July 23, 2009

Mr. Chairman and Members of the Committee,

I am deeply honored to appear before you today as President Obama's nominee to be the next United States Ambassador to the People's Republic of China. I am extremely humbled by and grateful to the President and Secretary Clinton for the trust and confidence they have shown in me. I would like to take this opportunity to thank and introduce members of my family who are here with me today: my wife, Mary Kaye, my children Mary Anne, Abby, Liddy, Jon, Will, Gracie and Asha.

My family has long been supportive of my interest in Asia during the past three decades. Of course, for part of our family, this is an opportunity to return home. My son, Will, was born in Singapore when I served as ambassador there, and our two adopted daughters, Gracie Mei and Asha Bharati, were born in China and India, respectively – happily, no border disputes yet surrounding their bedrooms!

It was a difficult decision for our family to make, to leave a state and a job that we love for this new challenge that takes us half the world away. I want to thank the citizens of Utah for their support and understanding as my family and I embark on this important mission for our country. With the support of the Senate, we are committed to this new responsibility.

If confirmed, I look forward to working with and learning from the outstanding team of Foreign Service Officers, Locally Engaged Staff, and representatives of the many U.S. agencies and offices that collectively make up U.S. Mission China, as well as their family members, who are vital and contributing members of the American community. We have an excellent team of first-class career professionals assembled at our Embassy in Beijing and our Consulates General in Chengdu, Guangzhou, Shenyang, Shanghai, and Wuhan, and, if confirmed, it will be my honor to serve as both their leader and cheerleader in pursuing and promoting American interests and objectives in China.

If confirmed, I will be in the enviable position of representing the United States during an exceptionally exciting time in our thirty year bilateral relationship with China, a period during which it is my fervent hope that our cooperation will deepen and broaden. The simple fact of the matter is that China is critically important and represents one of our most consequential bilateral relationships.

President Obama and Secretary Clinton have made clear their commitment to working with China to build a positive, cooperative and comprehensive relationship for the 21st century. This coming Monday, July 27, right here in Washington, D.C., the United States and China will launch the inaugural meeting of the Strategic and Economic Dialogue, the most ambitious dialogue in the history of our bilateral relations. Through this Dialogue, the United States and China aim to address together the challenges and opportunities we both face on a wide range of bilateral, regional, and global issues, including the global financial crisis, regional security concerns, global sustainable development, and climate change.

We have reached a point in history where a positive contribution from China can substantially improve our chances of addressing the most pressing problems. This Administration is committed to encouraging major and emerging global powers – including China – to join with our traditional friends and allies as partners in tackling the global agenda. If I am confirmed, one of my key missions will be to expand and reinforce China's support of our efforts to achieve solutions to the vexing problems that we all face, including proliferation of advanced weapons, terrorism, economic instability, and climate change.

One of our highest priorities is repairing the global economy. The United States and China have both enacted bold fiscal stimulus plans. In April, President Obama and Chinese President Hu Jintao agreed on the need to reform and strengthen the global financial system and resist protectionism. It is critical that our two countries maintain robust and close economic and financial coordination at this critical time for the health of the world economy.

A positive and cooperative U.S.-China relationship speaks to the need for a stronger global community committed to security, peace and prosperity. China's regional influence – politically, economically and diplomatically – continues to grow, and one of the key objectives of our engagement with China is to maintain peace and stability in Northeast Asia. In recent years, senior Chinese officials have demonstrated an unprecedented and – frankly – unexpected, degree of constructive leadership in regional affairs by chairing the Six-Party Talks and working closely with the United States in the United Nations Security Council to respond to North

Korea's provocations. As we all know, achieving a denuclearized Korean Peninsula is going to require some complicated and delicate bilateral and multilateral diplomacy. We need to continue working closely with China to convince North Korea to abandon its nuclear weapons program, which remains the most acute challenge to peace and stability in Northeast Asia, including through cooperating on the full implementation of United Nations Security Council Resolutions 1718 and 1874.

Likewise, we encourage China to develop constructive relations with its regional neighbors, including our allies Japan, South Korea and Australia, as well as our partners in ASEAN. We believe such relations can be a positive force in promoting and maintaining regional stability and prosperity, and should not be seen as a threat to U.S. interests or relationships in the region.

We hope to work increasingly in tandem with China on other issues in which we share a common interest. Some examples would include advancing global counterterrorism efforts, pursuing arms control, stemming the spread of weapons of mass destruction and their delivery systems, and combating extremism and promoting stability in Afghanistan and Pakistan. Iran's pursuit of a nuclear weapons capability continues to be a matter of international concern, and China's assistance will be important to achieving our objective of a stable and secure Middle East.

As its global economic and political influence grows, China can and should play an increasingly constructive international role. We would like to see China work with us to address governance and development concerns in places like Sudan, Burma, and Zimbabwe. If confirmed, I will use every opportunity to encourage China to become a constructive actor by fostering positive change among unaccountable and repressive regimes.

On the margins of the April 2009 G-20 Summit, President Obama and President Hu affirmed their commitment to work for the continued improvement and development of U.S.-China military-to-military relations, which have lagged behind other dimensions of our relationship. In military affairs we have and will continue to develop areas of common interests, although undoubtedly there will also remain areas where our interests diverge. The challenge before us is to maximize the space for cooperation in pursuit of common interests, while working to narrow our differences and prevent misunderstandings or accidents that could lead to confrontation. As China continues to modernize its military, there are numerous opportunities for China to demonstrate its role as a constructive actor in

upholding international stability. For example, adopting an open and transparent approach to its activities will help ease concerns that others may harbor about China's strategic intent, and will assist in developing the trust and understanding that can lead to greater levels of cooperation. If confirmed, I will work closely with the Defense Department and the representatives of our military services to improve the military-to-military relationship and build a framework for increased strategic trust between our two militaries.

We have entered an era in which all nations are called upon to work together to address the urgent problem of global climate change. The United States and China should be part of the solution, and collaboration on clean energy and greater energy efficiency offer a real opportunity to deepen the overall U.S.-China relationship. U.S. agencies have been encouraging their counterparts in China to expand cooperation on clean energy and other emission-reducing activities and to advance the international climate change negotiations. As Utah's Governor, I have been deeply involved in exploring clean energy options for the Western States. During my chairmanship of the Western Governors Association, we focused specifically on the global nature of climate change, working directly with China and other major carbon emitters on this critical issue. If confirmed, I will continue my personal interest in working with China to identify and take action in areas that are mutually beneficial and which promote low-carbon economic growth in ways that are consistent with our trade and investment policies.

I have highlighted some of the areas where the United States and China cooperate and agree. Of course, there are areas where we have differences, including Taiwan, human rights, Tibet, and other areas. Secretary Clinton has emphasized that the promotion of human rights is an essential element of American global foreign policy, and if confirmed, I look forward to robust engagement with China on human rights. In addition to expressing candidly our concerns regarding individual cases, it will be my objective to find new and constructive ways to support the efforts of Chinese citizens to strengthen civil society and rule of law in their own country. I believe that much can be achieved through dynamic public diplomacy, people-to-people exchanges, and other programs designed to assist China to implement the rule of law, support the development of civil society, promote religious freedom, and improve policies to protect the unique languages, cultures and religions of China's ethnic minorities. Thank you to those on the Committee who have championed these causes. If confirmed, I look forward to working with you on these shared goals in the coming months and years.

Memorandum of Understanding
to Enhance Cooperation on Climate Change, Energy and the Environment

between
the Government of the United States of America
and
the Government of the People's Republic of China

July 28, 2009

The Government of the United States of America and the Government of the People's Republic of China (hereinafter referred to as "the Participants"), recognize the following:

Climate change, clean and efficient energy and environmental protection are among the greatest challenges facing the United States and China.

Cooperation between the United States and China is critical to enhancing energy security, combating climate change, and protecting the environment and natural resources through pollution control and other measures.

Cooperation on climate change, clean and efficient energy and environmental protection can serve as a pillar of the bilateral relationship, build mutual trust and respect, and lay the foundation for constructive engagement between the United States and China for years to come, while also contributing to multilateral cooperation.

The Participants have therefore reached the following understandings:

I. Purpose

The purpose of this Memorandum of Understanding (MOU) is to strengthen and coordinate our respective efforts to combat global climate change, promote clean and efficient energy, protect the environment and natural resources, and support environmentally sustainable and low-carbon economic growth.

Both countries commit to respond vigorously to the challenges of energy security, climate change and environmental protection through ambitious domestic action and international cooperation.

Toward this end, both countries intend to transition to a low-carbon economy, carry out policy dialogue and cooperate on capacity building and research, development and deployment of climate-friendly technology.

Both countries resolve to pursue areas of cooperation where joint expertise, resources, research capacity and combined market size can accelerate progress towards mutual goals. These include, but are not limited to:

1) Energy conservation and energy efficiency
2) Renewable energy
3) Cleaner uses of coal, and carbon capture and storage
4) Sustainable transportation, including electric vehicles
5) Modernization of the electrical grid
6) Joint research and development of clean energy technologies
7) Clean air
8) Clean water
9) Natural resource conservation, e.g. protection of wetlands and nature reserves
10) Combating climate change and promoting low-carbon economic growth

Wherever possible, cooperation should seek to include expertise from all sectors of society and provide incentives for engagement at the sub-national level as well as by the business and academic sectors and non-governmental organizations.

II. Implementation

This MOU is to be co-chaired by the Department of State and Department of Energy on the U.S. side and the National Development and Reform Commission on the Chinese side. The Participants intend to hold regular ministerial consultations to deepen mutual understanding and promote and guide bilateral cooperation on climate change, clean and efficient energy and environmental protection through a range of mechanisms, including:

A. Ten Year Cooperation Framework on Energy and Environment
The Participants recognize the ongoing importance of the Framework

for Ten Year Cooperation on Energy and Environment ("TYF") dated June 18, 2008 in facilitating practical cooperation between the two countries in the areas of energy and environment. Both sides are committed to implementing all five existing action plans and to expanding the work of the TYF through new action plans.
The Participants also recognize the importance of and are committed to strengthening the EcoPartnerships initiative under the TYF in promoting sub-national cooperation and public-private partnerships to meet climate change, clean and efficient energy, and environmental goals.

Both sides also recognize the fruitful work of the TYF Joint Working Group in meeting the goals of this MOU and are committed to maintaining this effective working mechanism. As is defined by the TYF, the Joint Working Group is composed of officials at the Assistant Secretary-level for the United States and at the Director General-level for China. The Joint Working Group is co-chaired by the Department of State and Department of Energy on the U.S. side and by the National Development and Reform Commission on the Chinese side.

B. Climate Change Policy Dialogue and Cooperation
The Participants have decided to establish Climate Change Policy Dialogue and Cooperation as a platform for the United States and China to address global climate change and to identify and resolve areas of concern.

Consistent with equity and their common but differentiated responsibilities, and respective capabilities, the United States and China recognize they have a very important role in combating climate change. The United States and China will work together to further promote the full, effective and sustained implementation of the *United Nations Framework Convention on Climate Change*.

The Participants concur that their Climate Change Policy Dialogue and Cooperation should promote (i) discussion and exchange of views on domestic strategies and policies for addressing climate change; (ii) practical solutions for promoting the transition to low-carbon economies; (iii) successful international negotiations on climate change; (iv) joint research, development, deployment, and transfer, as mutually agreed, of climate-friendly technologies; (v) cooperation on specific projects; (vi) adaptation to climate change; (vii) capacity building and the raising of public awareness; and (viii) pragmatic cooperation on climate change between cities, universities, provinces and states of the two countries.

The Participants intend to hold consultations between representatives of the two countries' leaders on a regular basis. The Participants may establish working groups or task forces involving relevant ministries as necessary to support the objectives of the Climate Change Policy Dialogue and Cooperation.

C. Other Mechanisms for Cooperation
New initiatives, frameworks or other mechanisms for cooperation intended to achieve the goals of this MOU may be established with the mutual consent of both countries. Existing bilateral efforts may also be included as part of the cooperation described in this MOU, with such mutual consent.

Cooperation under this MOU may commence upon the date of signature and is not intended to give rise to rights or obligations under international law.

THE WHITE HOUSE

Office of the Press Secretary

For Immediate Release July 27, 2009

REMARKS BY THE PRESIDENT AT THE U.S./CHINA STRATEGIC AND ECONOMIC DIALOGUE

Ronald Reagan Building and International Trade Center
Washington, D.C.

9:35 A.M. EDT

THE PRESIDENT: Thank you. Good morning. It is a great honor to welcome you to the first meeting of the Strategic Economic Dialogue between the United States and China. This is an essential step in advancing a positive, constructive, and comprehensive relationship between our countries. I'm pleased that President Hu shares my commitment to a sustained dialogue to enhance our shared interests.

President Hu and I both felt that it was important to get our relationship off to a good start. Of course, as a new President and also as a basketball fan, I have learned from the words of Yao Ming, who said, "No matter whether you are new or an old team member, you need time to adjust to one another." Well, through the constructive meetings that we've already had, and through this dialogue, I'm confident that we will meet Yao's standard.

I want to acknowledge the remarkable American and Chinese leaders who will co-chair this effort. Hillary Clinton and Tim Geithner are two of my closest advisors, and they have both obtained extraordinary experience working with China. And I know that they will have extremely capable and committed Chinese counterparts in State Councilor Dai and Vice Premier Wang. Thank you very much for being here.

I'm also looking forward to the confirmation of an outstanding U.S. Ambassador to China, Governor Jon Huntsman, who is here today. (Applause.) Jon has deep experience living and working in Asia, and -- unlike me -- he speaks fluent Mandarin Chinese. He also happens to be a Republican who co-chaired Senator McCain's campaign. And I think that demonstrates Jon's commitment to serving his country, and the broad,

bipartisan support for positive and productive relations between the United States and China. So thank you, Jon, for your willingness to serve.

Today, we meet in a building that speaks to the history of the last century. It houses a national memorial to President Woodrow Wilson, a man who held office when the 20th century was still young, and America's leadership in the world was emerging. It is named for Ronald Reagan, a man who came of age during two World Wars, and whose presidency helped usher in a new era of history. And it holds a piece of the Berlin Wall, a decades-long symbol of division that was finally torn down, unleashing a rising tide of globalization that continues to shape our world.

One hundred years ago -- in the early days of the 20th century -- it was clear that there were momentous choices to be made -- choices about the borders of nations and the rights of human beings. But in Woodrow Wilson's day, no one could have foreseen the arc of history that led to a wall coming down in Berlin, nor could they have imagined the conflict and upheaval that characterized the years in between. For people everywhere -- from Boston to Beijing -- the 20th century was a time of great progress, but that progress also came with a great price.

Today, we look out on the horizon of a new century. And as we launch this dialogue, it's important for us to reflect upon the questions that will shape the 21st century. Will growth be stalled by events like our current financial crisis, or will we cooperate to create balanced and sustainable growth, lifting more people out of poverty and creating a broader prosperity around the world? Will the need for energy breed competition and climate change, or will we build partnerships to produce clean power and to protect our planet? Will nuclear weapons spread unchecked, or will we forge a new consensus to use this power for only peaceful purposes? Will extremists be able to stir conflict and division, or will we unite on behalf of our shared security? Will nations and peoples define themselves solely by their differences, or can we find common ground necessary to meet our common challenges, and to respect the dignity of every human being?

We can't predict with certainty what the future will bring, but we can be certain about the issues that will define our times. And we also know this: The relationship between the United States and China will shape the 21st century, which makes it as important as any bilateral relationship in the world. That really must underpin our partnership. That is the responsibility that together we bear.

As we look to the future, we can learn from our past -- for history shows us that both our nations benefit from engagement that is grounded in mutual interest and mutual respect. During my time in office, we will mark the 40th anniversary of President Nixon's trip to China. At that time, the world was much different than it is today. America had fought three wars in East Asia in just 30 years, and the Cold War was in a stalemate. China's economy was cut off from the world, and a huge percentage of the Chinese people lived in extreme poverty.

Back then, our dialogue was guided by a narrow focus on our shared rivalry with the Soviet Union. Today, we have a comprehensive relationship that reflects the deepening ties among our people. Our countries have now shared relations for longer than we were estranged. Our people interact in so many ways. And I believe that we are poised to make steady progress on some of the most important issues of our times.

My confidence is rooted in the fact that the United States and China share mutual interests. If we advance those interests through cooperation, our people will benefit and the world will be better off -- because our ability to partner with each other is a prerequisite for progress on many of the most pressing global challenges.

Let me name some of those challenges. First, we can cooperate to advance our mutual interests in a lasting economic recovery. The current crisis has made it clear that the choices made within our borders reverberate across the global economy -- and this is true not just in New York and Seattle, but in Shanghai and Shenzhen, as well. That is why we must remain committed to strong bilateral and multilateral coordination. And that is the example we have set by acting aggressively to restore growth, to prevent a deeper recession and to save jobs for our people.

Going forward, we can deepen this cooperation. We can promote financial stability through greater transparency and regulatory reform. We can pursue trade that is free and fair, and seek to conclude an ambitious and balanced Doha Round agreement. We can update international institutions so that growing economies like China play a greater role that matches their greater responsibility. And as Americans save more and Chinese are able to spend more, we can put growth on a more sustainable foundation -- because just as China has benefited from substantial investment and profitable exports, China can also be an enormous market for American goods.

Second, we can cooperate to advance our mutual interest in a clean, secure, and prosperous energy future. The United States and China are the two largest consumers of energy in the world. We are also the two largest emitters of greenhouse gases in the world. Let's be frank: Neither of us profits from a growing dependence on foreign oil, nor can we spare our people from the ravages of climate change unless we cooperate. Common sense calls upon us to act in concert.

Both of our countries are taking steps to transform our energy economies. Together we can chart a low carbon recovery; we can expand joint efforts at research and development to promote the clean and efficient use of energy; and we can work together to forge a global response at the Climate Change Conference in Copenhagen and beyond. And the best way to foster the innovation that can increase our security and prosperity is to keep our markets open to new ideas, new exchanges, and new sources of energy.

Third, we can cooperate to advance our mutual interests in stopping the spread of nuclear weapons. Make no mistake: The more nations acquire these weapons, the more likely it is that they will be used. Neither America nor China has an interest in a terrorist acquiring a bomb, or a nuclear arms race breaking out in East Asia. That is why we must continue our collaboration to achieve the denuclearization of the Korean Peninsula, and make it clear to North Korea that the path to security and respect can be traveled if they meet their obligations. And that is why we must also be united in preventing Iran from acquiring a nuclear weapon, and urging the Islamic Republic to live up to its international obligations.

This is not about singling out any one nation -- it is about the responsibility of all nations. Together, we must cooperate to secure all vulnerable nuclear materials around the world, which will be a focus of our Global Nuclear Summit next year. And together, we must strengthen the Nuclear Non-Proliferation Treaty by renewing its basic bargain: countries with nuclear weapons will move towards disarmament; countries without nuclear weapons will not acquire them; and all countries can access peaceful nuclear energy. A balance of terror cannot hold. In the 21st century, a strong and global regime is the only basis for security from the world's deadliest weapons.

And fourth, we can cooperate to advance our mutual interests in confronting transnational threats. The most pressing dangers we face no longer come from competition among great powers -- they come from extremists who

would murder innocents; from traffickers and pirates who pursue their own profits at the expense of others; from diseases that know no borders; and from suffering and civil wars that breed instability and terror. These are the threats of the 21st century. And that is why the pursuit of power among nations must no longer be seen as a zero-sum game. Progress -- including security -- must be shared.

Through increased ties between our militaries, we can diminish causes for dispute while providing a framework for cooperation. Through continued intelligence-sharing, we can disrupt terrorist plots and dismantle terrorist networks. Through early warning and coordination, we can check the spread of disease. And through determined diplomacy, we must meet our responsibility to seek the peaceful resolution of conflict -- and that can begin with a renewed push to end the suffering in Darfur, and to promote a comprehensive peace in Sudan.

All of these issues are rooted in the fact that no one nation can meet the challenges of the 21st century on its own, nor effectively advance its interests in isolation. It is this fundamental truth that compels us to cooperate. I have no illusion that the United States and China will agree on every issue, nor choose to see the world in the same way. This was already noted by our previous speaker. But that only makes dialogue more important -- so that we can know each other better, and communicate our concerns with candor.

For instance, the United States respects the progress that China has made by lifting hundreds of millions of people out of poverty. Just as we respect China's ancient and remarkable culture, its remarkable achievements, we also strongly believe that the religion and culture of all peoples must be respected and protected, and that all people should be free to speak their minds. And that includes ethnic and religious minorities in China, as surely as it includes minorities within the United States.

Support for human rights and human dignity is ingrained in America. Our nation is made up of immigrants from every part of the world. We have protected our unity and struggled to perfect our union by extending basic rights to all our people. And those rights include the freedom to speak your mind, to worship your God, and to choose your leaders. These are not things that we seek to impose -- this is who we are. It guides our openness to one another and to the world.

China has its own distinct story that shapes its own worldview. And Americans know the richness of China's history because it helped to shape the world and it helped to shape America. We know the talent of the Chinese people because they have helped to create this great country. My own Cabinet contains two Chinese Americans. And we know that despite our differences, America is enriched through deeper ties with a country of 1.3 billion people that is at once ancient and dynamic -- ties that can be forged through increased exchanges among our people, and constructive bilateral relations between our governments. That is how we will narrow our divisions.

Let us be honest: We know that some are wary of the future. Some in China think that America will try to contain China's ambitions; some in America think that there is something to fear in a rising China. I take a different view. And I believe President Hu takes a different view, as well. I believe in a future where China is a strong, prosperous and successful member of the community of nations; a future when our nations are partners out of necessity, but also out of opportunity. This future is not fixed, but it is a destination that can be reached if we pursue a sustained dialogue like the one that you will commence today, and act on what we hear and what we learn.

Thousands of years ago, the great philosopher Mencius said: "A trail through the mountains, if used, becomes a path in a short time, but, if unused, becomes blocked by grass in an equally short time." Our task is to forge a path to the future that we seek for our children -- to prevent mistrust or the inevitable differences of the moment from allowing that trail to be blocked by grass; to always be mindful of the journey that we are undertaking together.

This dialogue will help determine the ultimate destination of that journey. It represents a commitment to shape our young century through sustained cooperation, and not confrontation. I look forward to carrying this effort forward through my first visit to China, where I hope to come to know better your leaders, your people, and your majestic country. Together, I'm confident that we can move steadily in the direction of progress, and meet our responsibility to our people and to the future that we will all share.

Thank you very much. (Applause.)

END 9:50 A.M. EDT

THE WHITE HOUSE

Office of the Press Secretary

FOR IMMEDIATE RELEASE April 1, 2009

STATEMENT ON BILATERAL MEETING WITH PRESIDENT HU OF CHINA

On 1 April 2009, President Barack Obama of the United States and President Hu Jintao of China met on the sidelines of the G20 Financial Summit in London, the United Kingdom. The two heads of state had an extensive exchange of views on U.S.-China relations and global issues of common interest, and reached the following points of agreement:

I. Toward Enhanced U.S.-China Relations

The two sides agreed to work together to build a positive, cooperative, and comprehensive U.S.-China relationship for the 21st century and to maintain and strengthen exchanges at all levels. President Hu Jintao invited President Obama to visit China in the second half of this year, and President Obama accepted the invitation with pleasure.

The two sides decided to establish the "U.S.-China Strategic and Economic Dialogue." U.S. Secretary of State Hillary Clinton and Chinese State Councilor Dai Bingguo will chair the "Strategic Track" and U.S. Secretary of the Treasury Timothy Geithner and Chinese Vice Premier Wang Qishan will chair the "Economic Track" of the Dialogue, each as special representatives of their respective presidents. The two sides will hold the first round of the dialogue in Washington DC this summer. The two sides stated that they will continue to advance mutually beneficial cooperation in economics and trade through the mechanism of the high-level Joint Commission on Commerce and Trade.

The two sides agreed to further deepen mutually beneficial cooperation in a wide range of areas, including economy and trade, counterterrorism, law enforcement, science and technology, education, culture and health. They also agreed to resume and expand consultations on non-proliferation and other international security topics. They welcomed further exchanges between the national legislatures, local authorities, academics, young people and other sectors. The two sides agreed to resume the human rights dialogue as soon as possible.

Both sides share a commitment to military-to-military relations and will work for their continued improvement and development. The two sides agreed that Admiral Gary Roughead, U.S Chief of Naval Operations, will visit China upon invitation in April to attend events marking the 60th anniversary of the founding of the Navy of the Chinese People's Liberation Army. The U.S. looks forward to visits by senior Chinese military leaders this year.

The two sides agreed to maintain close communication and coordination and to work together for the settlement of conflicts and reduction of tensions that contribute to global and regional instability, including the denuclearization of the Korean Peninsula, the Iranian nuclear issue, Sudan humanitarian issues, and the situation in South Asia.

The two sides agreed to intensify policy dialogue and practical cooperation in energy, the environment and climate change building on the China-US Ten Year Energy and Environment Cooperation Framework, carry out active cooperation in energy efficiency, renewable energy, and clean energy technologies and work with other parties concerned for positive results at the Copenhagen conference.

II. Strengthening Economic and Financial Cooperation

The two presidents discussed challenges facing the global economy and financial system. They pledged that, as two major economies, the U.S. and China will work together, as well as with other countries, to help the world economy return to strong growth and to strengthen the

international financial system so a crisis of this magnitude never happens again.

The two presidents welcomed the fiscal stimulus measures taken by the other, and agreed that these measures were already playing a stabilizing role for the global economy. They also agreed that strong financial systems were essential for restoring growth, and they welcomed the commitment of both countries to address issues in this area. President Obama underlined the commitment of the United States to implement the American Recovery and Reinvestment Act and the Financial Stability Plan. He underscored that once recovery is firmly established, the United States will act to cut the U.S. fiscal deficit in half and bring the deficit down to a level that is sustainable. President Hu emphasized China's commitment to strengthen and improve macroeconomic control and expand domestic demand, particularly consumer demand, to ensure sustainable growth, and ensure steady and relatively fast economic development.

The two presidents agreed the international financial institutions should have more resources to help emerging market and developing nations withstand the shortfall in capital, and the two countries will take actions toward this goal. China and the United States agreed to work together to resolutely support global trade and investment flows that benefit all. To that end, they are committed to resist protectionism and ensure sound and stable U.S.-China trade relations.

President Hu and President Obama discussed regulatory and supervisory changes needed to reform and strengthen the global financial system, including regulatory standards. President Hu welcomed the recent U.S. announcement of a comprehensive financial regulatory reform agenda. President Obama welcomed the commitment of China to continue the development and reform of its financial system.

The Presidents agreed on the need for sweeping changes in the governance structure of international financial institutions. President Obama underscored that such changes were needed so that these

organizations better reflect the growing weight of dynamic emerging market economies in the global system

President Hu and President Obama concluded that continued close cooperation between the United States and China was critical at this time to maintain the health of the world economy and would remain so in the future. They both recognized that as major economies, the United States and China have a need to work together, as well as with other countries, to promote the smooth functioning of the international financial system and the steady growth of the world economy. To this end, the two sides will exchange views and intensify coordination and cooperation on global economic and financial issues, climate change and energy, and other important issues through the Strategic and Economic Dialogue that the two countries have decided to establish.

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ADDITIONAL MATERIAL SUBMITTED BY MR. FRED BERGSTEN, DIRECTOR, PETERSON INSTITUTE FOR INTERNATIONAL ECONOMICS

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Two's Company

C. Fred Bergsten

To the Editor:

Like most critics of the idea of a G-2 made up of the United States and China, an idea that I initiated in my book *The United States and the World Economy*, published in 2005, and was publicized most widely in these pages ("A Partnership of Equals," July/August 2008), Elizabeth Economy and Adam Segal ("The G-2 Mirage," May/June 2009) misunderstand the basic concept.

The proposed G-2 was never intended to supplant any of the existing international economic steering committees, of which the G-20 has now attained preeminence, let alone the long-standing multilateral organizations, such as the International Monetary Fund and the World Trade Organization. To the contrary, its chief purpose is to supplement the existing institutions and make them work better by promoting prior agreement between the two countries whose cooperation has become a sine qua non for making progress on virtually any international economic issue. It would simply be a caucus of the two rather than any attempt to create a new governing entity, let alone a "dominant condominium," as mischaracterized by some.

The United States and China are the world's two most important economies. The United States leads the high-income economies, and China leads the emerging-market economies. Each of these groups now accounts for half of global output. The United States and China are the two largest trading countries and the two largest polluters.

There will be no sustained recovery from the current global economic crisis unless the United States and China lead it. There will be no renewed momentum toward progress on global trade, through the Doha Round or otherwise, unless they endorse it. There will be no international compact on global warming unless they embrace it. The United States is the world's largest largest deficit/debtor country, and China is the world's largest surplus/creditor country -- and there will be no resolution of the global imbalances that helped bring on the current crisis, nor lasting reform of the international financial architecture, without their concurrence.

Hence, an effective G-2 is imperative if the world economy is to move forward both cyclically and structurally. Of course, it must be kept informal and indeed unremarked on by the two countries themselves. Of course, the European countries, Japan, and some other countries must participate in the multilateral agreements that are required on virtually all issues. Of course, the linkages between the G-2 and other institutions must be handled with diplomatic skill. But the substance of the issues that these institutions address will not be advanced unless the United States and China work it out together.

Chinese Premier Wen Jiabao, in fact, recently assured the Europeans that the United States and China had no intention of trying to manage the world on their own and that instead the development of close U.S.-Chinese relations would benefit other countries.

Economy and Segal would move in precisely the opposite direction by suggesting that the United States "sit down with Japan, the EU, and other key allies to begin coordinating their policies toward China." This would be viewed by the Chinese as an effort to surround and even isolate them. It would be hugely counterproductive and would surely fail, not least because none of those U.S. allies would be willing to play (and correctly so).

I am delighted that such foreign policy and security experts as Zbigniew Brzezinski and Niall Ferguson have recently advocated that the G-2 concept be expanded well beyond the economic domain for which I originally proposed it. The Hu Jintao and Obama governments also seem to be moving in this direction, building on former Deputy Secretary of State Robert Zoellick's Senior Dialogue and former Secretary of the Treasury Henry Paulson's Strategic Economic Dialogue. Economy and Segal in fact conclude by proposing "one overarching negotiation that sits above or outside the purview of the U.S. government's traditional cabinet-level agencies" and by arguing that "the National Security Council and the vice president's office would ideally play a central role in this effort," which is pretty close to the annual summits that I have recommended to both establish the G-2 and make sure that it works effectively.

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A Partnership of Equals

How Washington Should Respond to China's Economic Challenge

C. Fred Bergsten

To BE an economic superpower, a country must be sufficiently large, dynamic, and globally integrated to have a major impact on the world economy. Three political entities currently qualify: the United States, the European Union, and China. Inducing China to become a responsible pillar of the global economic system (as the other two are) will be one of the great challenges of coming decades—particularly since at the moment China seems uninterested in playing such a role.

The United States remains the world's largest national economy, the issuer of its key currency, and in most years the leading source and recipient of foreign investment. The EU now has an even larger economy and even greater trade flows with the outside world, and the euro increasingly competes with the dollar as a global currency. China, the newest member of the club, is smaller than the other two but is growing more quickly and is more deeply integrated into the global economy. Its dramatic expansion is therefore having a powerful effect on the rest of the world. (China is often paired with India in such discussions, but India's GDP is less than half of China's. The value of the annual growth of China's trade exceeds the total annual value of India's trade. China will dominate its Asian neighbor for the foreseeable future.)

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China poses a unique challenge because it is still poor, significantly nonmarketized, and authoritarian. All three characteristics reduce the likelihood that it will easily accept the systemic responsibilities that should ideally accompany superpower status. The integration of China into the existing global economic order will thus be more difficult than was, say, the integration of Japan a generation ago. The United States and the EU would like to co-opt China by integrating it into the regime that they have built and defended over the last several decades. There are increasing signs, however, that China has a different objective. In numerous areas, it is pursuing strategies that conflict with existing norms, rules, and institutional arrangements.

Some take this lightly, viewing it as simply the usual free-riding and skirting of responsibility by a powerful newcomer cleverly exploiting the loopholes and weak enforcement of existing international rules to pursue its perceived national interests. After all, they say, even the United States and the EU do the same on occasion, as do other major emerging-market economies. And to be sure, there is no evidence that China's challenges to the current economic order derive from any cohesive or comprehensive strategy concocted by the country's political or intellectual leadership. Despite calls in Beijing for "a new international economic order" and talk of how a "Beijing consensus" might supplant the so-called Washington consensus, to date China's proposed alternative approaches do not add up to a revisionist challenge to the status quo.

Nevertheless, the situation is worrisome. Given its status as a powerful newcomer benefiting from an efficient economic order, China actually has a profound interest in seeing that the international rules and institutions function effectively. It should be trying to strengthen the system, whether the present version or an alternative version more to its liking.

Moreover, Chinese recalcitrance seems to be increasing rather than decreasing over time. At the outset of its economic reform process, in the late 1970s, China was eager to join (and to replace Taiwan in) the International Monetary Fund (IMF) and the World Bank. These institutional ties subsequently played important, and apparently welcome, roles in China's early development success. Later, Beijing not only endured lengthy negotiations and an ever-expanding set of

requirements in order to join the World Trade Organization (WTO) but also used the pro-market rules of that institution to overcome resistance to reform among die-hards inside China itself.

But a country's attitudes can change dramatically along with its circumstances. Russia, for example, was a supplicant for international capital and support after its bankruptcy in 1998 and with world oil prices near $20 a barrel, but it is aggressively pursuing a resumption of great-power status now that it has recovered and with oil over $100 a barrel. China appears to be undergoing a similar evolution, albeit with a more cautious leadership and an incremental style. It is also experiencing the same internal backlash against globalization as have the United States and many other countries. This attitudinal shift simply has to be reversed, even if doing so requires a fundamental adjustment of the international economic architecture.

TOWARD AN ASIAN BLOC?

ON TRADE, China has been playing at best a passive and at worst a disruptive role. It makes no effort to hide its current preference for low-quality, politically motivated bilateral and regional trade arrangements rather than economically meaningful (and demanding) multilateral trade liberalization through the WTO. Since China is the world's largest surplus country and second-largest exporter, this poses two important challenges to the existing global regime.

First, China's refusal to contribute positively to the Doha Round of international trade negotiations has all but ensured the talks' failure. Beijing has declared that it should have no liberalization obligations whatsoever and has invented a new category of WTO membership ("recently acceded members") to justify its recalcitrance. Such a stance by a major trading power is akin to abstention and has practically guaranteed that the Doha negotiations will go nowhere. And since the global trading system does not stay in place, but is always moving either forward or backward, a collapse of the Doha Round would be quite serious: it would represent the first failure of a major multilateral trade negotiation in the postwar period and place the entire WTO system in jeopardy. China is not the only culprit in the Doha drama, of course. The United States and the EU have been unwilling to abandon their

agricultural protectionism, other important emerging economies have been unwilling to meaningfully open their markets, and several poor countries have resisted contributing to a global package of reforms. But China, with its major stake in open trade, exhibits the sharpest contrast of all the major players between its objective interests and its revealed policy.

Second, China's pursuit of bilateral and regional trade agreements with neighboring countries is more about politics than economics. Its "free-trade agreement" with the Association of Southeast Asian Nations (ASEAN), for example, covers only a small share of its commerce with the countries in question; it is simply an effort to calm their fears of being swamped by their huge neighbor. Again, it is true that the United States and other major trading powers also factor foreign policy considerations into their selections of partners for regional and bilateral trade agreements. But they also insist on economic standards that largely conform to the WTO's rules. China is able to escape legal application of those rules by continuing to declare itself a "developing country" and by taking advantage of "special and differential treatment." But for a major global trading power to hide behind such loopholes provokes substantial international strains.

China has a profound interest in seeing that the international rules and institutions function effectively.

China is also hurting the global trading system by supporting the creation of a loose but potent Asian trading bloc. The network of regional agreements that started with one between China and ASEAN has steadily expanded to include virtually all other possible Asian permutations: parallel Japanese-ASEAN and South Korean–ASEAN deals; various bilateral partnerships, including perhaps a Chinese-Indian one; a "10 + 3" arrangement that brings together the ten ASEAN countries and all three Northeast Asian countries, and possibly even a "10 + 6" agreement that would broaden the group to include Australia, India, and New Zealand. All this activity is likely to produce, within the next decade, an East Asian free-trade area led by China.

Such a regional grouping would almost certainly trigger a sharp backlash from the United States and the EU, as well as from numerous developing countries, because of its new discrimination against them.

Even more important, it would create a tripolar global economic regime—a configuration that could threaten existing global arrangements and multilateral cooperation.

China's challenges to the global trading system are most visible in its opposition to the U.S. proposal, launched at the Asia-Pacific Economic Cooperation forum in 2006, for a free-trade area of the Asia-Pacific. The APEC initiative, immediately endorsed by a number of those smaller member economies that fervently want to prevent trade conflict between the group's two superpowers, seeks to head off the looming confrontation between an Asia-only trading bloc and the United States, which could draw a line down the middle of the Pacific. The initiative would eventually consolidate the many preferential pacts in the Asia-Pacific region and offer an economically meaningful Plan B for widespread trade liberalization if the Doha Round definitively fails. China has led the opposition to the idea, demonstrating its preference for bilateral deals with minimal economic content and its lack of interest in trying to defend the broader trading order.

TRASHING THE IMF?

CHINA'S CHALLENGE to the international monetary order, meanwhile, is at least as serious. Alone among the world's major economies, China has rejected the adoption of a flexible exchange-rate policy, which would promote adjustment of its balance-of-payments position and avoid a buildup of large imbalances. Under IMF rules, China has the right to peg its currency—but it does not have the right to intervene massively in the foreign exchange market, as it has for the past five years, to maintain a hugely undervalued yuan and thereby boost its international competitive position. This violates the most basic norms of the IMF's Articles of Agreement, which require members to "avoid manipulating exchange rates . . . in order to prevent effective balance of payments adjustment or to gain unfair competitive advantage." It is also a violation of the IMF's implementing guidelines, which explicitly proscribe the use of "prolonged, large-scale one-way" interventions to maintain competitive undervaluation.

The results are unprecedented for a major trading country. China's current account surplus has reached 11–12 percent of its GDP. By next year,

its annual global surplus could approach $500 billion, approximating the value of the U.S. current account deficit. Its hoard of foreign currency exceeds $1.6 trillion and is by far the world's largest. These imbalances and the unprecedented flow of international funds that they require could trigger a crash of the dollar and a "hard landing" for the global economy, severely compounding the current global financial crisis.

Previous surplus countries, notably Germany in the 1960s and 1970s and Japan in the 1970s and 1980s, have also resisted making necessary and inevitable adjustments to their currency pegs. But no earlier imbalances have ever approached the current Chinese one in terms of its share of the country's GDP. Moreover, all of these countries eventually agreed to conform to the international rules.

To date, however, China has resisted all entreaties to alter its behavior. Its announced move to "a managed floating exchange rate based on market supply and demand" in July 2005 has still not produced any significant rise in the trade-weighted value of its currency, despite the recent acceleration of the yuan's appreciation against the dollar, nor has it prevented continued huge surpluses in China's external accounts. The number of interventions in the currency markets that China has undertaken to block faster appreciation of the yuan has at least doubled since that time.

China has actually questioned the basic concept of international cooperation in dealing with these problems, claiming that a country's exchange rate is "an issue of national sovereignty" (rather than a quintessentially international concern in which foreign parties have an equal interest). It has objected even to the IMF's consideration of the issue. Its actions have raised an implicit threat that it might promote the creation of an Asian Monetary Fund, further eroding the global role of the IMF, and may seek a regional or even global role for its national currency over the long term. These monetary steps intensify the challenge to the global trading system because large exchange-rate misalignments are a potent stimulus for protectionism in deficit countries, as indicated at present by the numerous bills in Congress to address the China currency issue with trade sanctions.

On energy (China will shortly become the world's largest consumer of energy), the challenge China poses is less frontal, but only because there exists no body of agreed global doctrine, rules, and institutions.

There are at least two conflicting energy regimes, the (periodically effective) producer cartel embodied in the Organization of the Petroleum Exporting Countries and the (very loose and incomplete) consumer anticartel embodied in the International Energy Agency. China is creating problems for both with its drive to line up "secure sources of supply" through long-term contracts with selected producing countries. It is unwilling to rely solely, or even primarily, on market mechanisms, attempting to insure itself against both output interruptions by the producers and the market power of other large consumers.

Here, as elsewhere, China is hardly alone in its behavior. But as the driving force behind the single most important commodity market in the world, the country has a particular interest in (and responsibility for) forging systemic responses rather than trying to carve out exceptions and special privileges for itself. China appears to be either unaware of the abject failure of such strategies in the past or confident that its contemporary clout will suffice to sustain its contractual arrangements even in difficult periods, and it is pursuing such strategies with respect to other raw materials as well as oil and gas.

On foreign aid, China may have already become the largest national donor (depending on how "aid" is defined), and it is posing a direct challenge to prevailing norms by ignoring the types of conditionality that have evolved throughout the donor community over the past quarter century. Beijing rejects not only the social standards (on human rights, labor conditions, and the environment) that have become prevalent but also the basic economic standards (such as poverty alleviation and good governance) that virtually all bilateral and multilateral aid agencies now require as a matter of course. As with its trade and commodity pacts, China's "conditionality" on aid is almost wholly political: insistence that the recipient countries support China's positions on global issues, in the United Nations and elsewhere, and funnel their primary products to China as reliable suppliers.

NEW RULES OF THE GAME

WHAT THESE policies demonstrate is that China's international mindset has not kept pace with its breathtaking economic ascent. China continues to act like a small country with little impact on the global

system at large and therefore little responsibility for it. Such a lag in perceptions is not difficult to understand, particularly as it regards a conservative leadership still following Deng Xiaoping's directive to maintain a low international profile. The central thrust of contemporary Chinese foreign policy is not to assume a large role in the world but to avoid international entanglements that could disrupt the country's ability to focus on its huge domestic challenges. Moreover, the speed at which China has risen is difficult for even the most experienced observers to comprehend. (The pattern is similar to the one that accompanied Japan's growth from the early 1970s into the 1980s, when its meteoric rise also triggered sharp global reactions, while Tokyo maintained a passive and reactive stance on almost all international issues.)

Even the strongest defenders of the current world trading system would concede that at least some of China's criticisms are valid. At best, the Doha Round will achieve only marginal liberalization of world trade after almost a decade of effort. The IMF has failed to enforce its own rules and is being forced to downsize. The World Bank has lost any clear direction. The G-7 (the group of highly industrialized states) has adopted a mutual nonaggression pact among its members, making its criticisms of outsiders such as China seem hypocritical. And by failing to adapt their governance structures to the dramatic changes in the relative economic power among nations, the international economic institutions have lost much of their legitimacy. The fact that some Chinese attitudes are understandable and some Chinese concerns legitimate does not lessen the significance of the challenge but rather suggests some of the logical components of an intelligent response.

China is uncomfortable with the very notion of simply integrating into a system it had no role in developing.

To deal with the situation, Washington should make a subtle but basic change to its economic policy strategy toward Beijing. Instead of focusing on narrow bilateral problems, it should seek to develop a true partnership with Beijing so as to provide joint leadership of the global economic system. Only such a "G-2" approach will do justice, and be seen to do justice, to China's new role as a global economic superpower and hence as a legitimate architect and steward of the international economic order.

A Partnership of Equals

The present U.S. approach seeks to entice China to join the existing global economic order. Washington's fondness for the status quo is understandable given its basic success and the prominent role it accords Washington. But China is uncomfortable with the very notion of simply integrating into a system it had no role in developing. Both Chinese officials and Chinese scholars are actively discussing alternative structures for which China can be present at the creation. At one particularly contentious point in its negotiations to enter the WTO, the Chinese ambassador reportedly thundered, "We know we have to play the game your way now, but in ten years we will set the rules!" The existing system, moreover, has become increasingly sclerotic, and it might well be that the only way to overcome the enormous resistance to change (manifested in positions such as Europe's refusal to wind down its excessive quotas and give up some of its IMF executive-board seats) is to undertake a fundamental overhaul.

Current U.S. policy also purports to include tough enforcement measures to punish noncooperation: Washington has taken Beijing to the WTO for dispute settlement on a number of occasions and has tried to mobilize the IMF and the G-7 to penalize China for its undervalued currency. But Washington's criticism of Beijing has not been translated into any serious retaliatory pressure because too many Americans receive too many benefits from their actual or potential dealings with China for policymakers to jeopardize the relationship and because other key countries are also unwilling to confront China. Abandoning the present position and adopting a less confrontational approach might be the only way to persuade China to start cooperating.

THE BIG TWO

IN PART, the strategy proposed here would treat old issues in new ways, recasting conflicts as opportunities for progress. The United States and China could agree to construct their regional trade agreements in ways that support, rather than impede, subsequent multilateral liberalization—and even permit eventual linkage between the regional bodies. Failures to offer significant new market-opening opportunities in the Doha Round would be addressed not as legitimate mercantilist behavior but as threats to the WTO that would jeopardize both countries'

stake in an open world economy. Competitive currency misalignments would be treated as deviations from IMF norms that hurt all trading partners, especially poor countries. Washington would concede that its errant fiscal policy has contributed to the overvaluation of the dollar, just as Beijing would concede that undervaluation of the yuan has reflected inadequate Chinese internal demand and excessive government intervention. The United States could escort China into the International Energy Agency to help organize the response of consuming countries to high oil prices.

More far-reaching steps might involve the creation of new international norms and institutional arrangements to govern issue areas that are important but currently unregulated, such as global warming and sovereign wealth funds (SWFs). To date, China has steadfastly refused to even contemplate binding constraints on its greenhouse gas emissions. So has the United States, but that stance seems likely to change dramatically after the presidential election in November, no matter who wins. An emissions regime, however, may well lead to the installation of trade barriers in participating countries against carbon-intensive products from nonparticipating countries. Moreover, global warming cannot be seriously addressed without China, which has become the world's largest polluter. Unless Washington and Beijing find ways to cooperate in attacking the problem together, the result could be a trade war between them and little or no action on the environment.

China has already indicated some skepticism about the adoption of new international guidelines, even if voluntary and nonbinding, regarding the structure and investment activities of SWFs. But the United States is championing such codes in order to permit continued foreign investment and head off the risk of protectionist domestic reactions. Since the U.S. economy is especially dependent on Chinese capital, without some new agreement a frontal clash could develop over this issue, triggered either by China's rejection of proposed new guidelines or by the United States' rejection of Chinese investments in particularly sensitive areas.

Whether in dealing with old or new issues, the basic idea would be to develop a G-2 between the United States and China to steer the global governance process. Other major powers, such as the EU and,

on some issues, Japan, would of course need to be deeply involved as well. The new rules, codes, or norms could frequently be implemented through existing multilateral institutions, such as the IMF and the WTO. Some of them might work better through new worldwide organizations created to deal with truly new issues, such as a global environmental organization to manage climate-change policy. But effective systemic defenses against international economic challenges in today's world must start with active cooperation between its two dominant economies, the United States and China.

Given other powers' sensitivities, of course, it would be impolitic for Washington and Beijing to use the term "G-2" publicly. But for the strategy to work, the United States would have to give true priority to China as its main partner in managing the world economy, to some extent displacing Europe. Nothing less is likely to attract China or engage the United States sufficiently to create the effective leadership that the world so desperately needs.

> It is not enough for China to be seen as a "responsible stakeholder." It must also be accorded full rights as a true leadership partner.

Some initial steps have already been taken in this direction. After I floated the idea of a G-2 in late 2004, Robert Zoellick, in his new capacity as deputy secretary of state, which he undertook in February 2005, launched initial discussions with Chinese counterparts. In 2007, Treasury Secretary Henry Paulson escalated the engagement to what is now known as the U.S.-China Strategic Economic Dialogue, which involves the leaders of ten or so cabinet agencies in each country. The beginnings of an institutional framework for a working G-2 have thus already been put in place, and patterns of cooperation are already developing on topics such as the environment and international finance. But it is not nearly enough for China to be seen as a "responsible stakeholder." It must be seen, and accorded full rights, as a true leadership partner.

Such a relationship between a rich developed country and a poor developing one would be unprecedented in human history—as is there being a poor economic superpower, which is what China is. There are enough examples of similar cooperation on specific issues, however,

to suggest that converting U.S.-Chinese disputes into systemic management issues can be extremely effective. In the late 1970s, for example, the United States was applying countervailing duties to scores of Brazilian products because Brazil's export subsidies accounted for almost half the value of all of its foreign sales. A frontal assault on the subsidies was politically unacceptable in Brazil, but the two countries agreed to cooperate closely in negotiating a new subsidy code for the General Agreement on Tariffs and Trade (the precursor to the WTO): this agreement turned out to be simultaneously the linchpin of a successful Tokyo Round of trade talks, a basis for adding an injury clause to the U.S. countervailing-duty law, and a foundation for phasing out the Brazilian subsidy policy.

Are the United States and China ready for such a substantial reorientation? Washington would need to accept China as a true partner in managing global economic affairs, the development of an intimate working relationship with an Asian country rather than its traditional European allies, and constructive collaboration with an authoritarian political regime rather than a democracy. All these changes would pose substantial challenges for U.S. policymakers and would likely encounter domestic political resistance.

China is rapidly approaching a moment when its chosen strategy of integration into the world economy will force it to assume increased responsibility for the successful functioning of that economy. China's own interests, in other words, should lead it to accept an invitation from the United States to help steer the system in a mutually acceptable direction. The Chinese today are hotly debating whether their country should proceed unilaterally or work within the international system, and an offer of true partnership could tilt the outcome of that debate decisively and constructively, raising the possibility that China could continue its upward trajectory without provoking the clashes that previous rising powers have.

If China is reluctant to get too close to the United States—say, because of continuing controversies over security issues—alternative institutional arrangements are of course available. The EU could be a member from the outset of a G-3, a group of the current global economic superpowers. The new G-5, recently created by the IMF to conduct its intensified multilateral consultative process, which adds Japan and

Saudi Arabia (to represent the oil producers) into the mix, is another possibility. The central need is to embrace China in the context of a new and effective leadership grouping in light of its critical role in the world economy and its legitimate desire to be engaged in systemic management at all relevant stages of the process.

Under seven successive presidents, the United States has chosen to engage, rather than confront, China, taking the eminently sensible view that provoking an unnecessary confrontation would be profoundly contrary to U.S. interests. Given the signs that China's economic advance will continue, the same logic suggests that Washington should make every effort to engage Beijing as a true partner in steering global economic affairs. At a minimum, creating a G-2 would limit the risk of bilateral disputes escalating and disrupting the U.S.-Chinese relationship and the broader global economy. At a maximum, it could start a process that might, over time, generate sufficient trust and mutual understanding to produce active cooperation on crucial issues.

Right now, the prospects of such active cooperation are uncertain. But in addition to their differences, the two countries share many common interests, and their global economic positions are converging rather than diverging. Developing a partnership of the sort outlined here will not be easy and will take much time and effort. But the issues at stake are so important that even partial success would be worthwhile, and the only way to gauge the idea's feasibility is to try it. The upcoming negotiations to create a global strategy to counter global warming offer a compelling opportunity for just such an experiment.