In the last three days, the United States government has added new pressures to the Chinese government: The US Department of Treasury demanded a revaluation of the renminbi, and the Commerce Department moved to restrain textile imports from China. One of the defining features of globalization today is the complex way in which countries are economically intertwined, as well as the political implications of this interdependence. China's rise as an economic giant in recent years is a boon for US, Japanese, and European companies doing business in China, but for this very reason they must tread cautiously in political dealings. Jeffrey E. Garten, Dean of the Yale School of Management, suggests that applying punitive pressures to China will only intensify tensions. In fact, because of the complex economic relationships, these actions would likely backfire – harming more than helping the other powers. What the US, Japan, the EU, and China must do now is to engage in an over-arching dialogue about the issues troubling them. "Unless a new order is negotiated," Garten warns, "the world will risk entering a frightful period where damaging political and economic turmoil is no longer a far-fetched prospect." – YaleGlobal

Can China Be Contained?

In a close-knit world, pressuring Beijing could have unintended consequences

Jeffrey E. Garten
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NEW HAVEN: For over a decade now pundits have speculated as to how the rise of China as a major power would affect the world. That future is now, and the Western powers are flailing about, wondering how to respond. Pressure is building on China on many fronts to modify its behavior without clear thought as to how all these pressures will end up affecting everyone caught in the web of globalization.

Empire of toys: Growing Chinese trade surplus will bring protectionist pressure but consumers won't be happy

It is tempting to look to history to see how – short of war – entrenched powers opposed the rise of newcomers or adversaries. But such analogies as 19th century balance of power politics or NATO's containment of the former Soviet Union don't work. Reason: Never before has the rise of a nation occurred while it was so intertwined economically with those countries that might wish to slow it down. And since China seems set on expanding its global role – economically, politically, and militarily – the rising nation's antagonists would be best served by working together. They must determine an approach that is less knee-jerk in its punitive nature and more open to working more closely with China on difficult issues.

It is rather remarkable that the international environment has been so benign for China these past fifteen years.

It is no small matter when an emerging superpower faces simultaneous challenges in its relationships with the US, the EU, and Japan. These trends are not just temporary or normal adjustments to China's positioning in a new international order; they are deeper, more prolonged, and potentially more destabilizing.

China's rise to great power status may be inevitable, but no one should have ever thought that it could occur smoothly – not with the force, scale, and compressed timeframe that characterizes the Middle Kingdom's bursting onto the world scene. In fact, it is rather remarkable that the international environment has been so benign for China these past fifteen years.

But that is sure to change. The US has reimposed textile quotas on China, and Europe is likely to follow suit. Washington, EU finance ministers, the G-7, the IMF, and the World Bank have all been pushing Beijing to revalue the renminbi. Concern has been rising in the US, Japan, and within the International Energy Agency that China's voracious appetite for oil will drive up global prices. Tokyo has deplored Chinese demonstrations against Japan. The EU is having second thoughts about loosening its embargo on weapons sales to China. Even excluding the explosive issues of Taiwan and North Korea, a number of big problems are sure to grow.

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Escalating trade tensions are in store as China's global trade surplus grows – as China accounts for more of the US trade deficit, begins to flood the world with politically sensitive products like autos, and shifts toward more high technology exports (aided in large part by US firms). Europe's arthritic economies are likely to be particularly hard hit, setting back the EU's present support for open trade.

In finance, even if China implements a modest currency revaluation in the near future, it is sure to come under relentless pressure to keep pushing up the value of the renimbi and to further open its shaky banking system to foreign investment.

Washington will look increasingly askance at China's current strategy of cozying up to energy suppliers on the US list of rogue states, such as Iran, Sudan, and Venezuela. Nor will the US take kindly to China's bid to replace it as the major power in Asia. Diplomatic sparks will also fly as the Bush administration's crusade for democracy inevitably begins to focus on the Middle Kingdom.

The Chinese anti-Japan protests are not just about the past, but the opening shot in what promises to be a fierce competition for future dominance in Asia. This rivalry could see rising nationalism from both countries, as well as expansion of military capabilities. China's stated intention to veto Japan's drive to win a seat on the UN Security Council will be particularly inflammatory.

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Beijing could be forgiven if it thinks that the major industrial powers are trying to constrain its rise directly and through multilateral institutions. But even if that were the intention of Washington, Brussels, and Tokyo, such policies cannot succeed. Their economies are too intricately intertwined; essentially, what goes around comes around in some fashion.

The US might be frustrated with China's trade prowess, but the nature of complex global supply arrangements means that imports of product components from China – many of which come from US firms that are operating there – are critical to the viability of key US industries such as telecom and computers. Those same imports are helping to keep US inflation down – which means lower interest rates on mortgages, car loans, and other big ticket items, and a more buoyant stock market.

The United States might want to hammer China on its currency, but it can't forget that China is its second largest creditor and holds over US$600 billion in foreign reserves. Were China to sell the American IOUs it holds, the dollar would crash, interest rates would shoot up, and the US would likely experience a recession or worse.

Japan is in a bind, too, since it now depends on China's market for much of its export growth. Without the China market, Japan would have no hope of sustaining a recovery after years of stagnation. And were the EU to turn to trade protection, it would lose any chance of keeping its competitive edge; its industries would suffer, its economies would sag, and its unemployment would become even worse.

> **Admittedly, there is little precedent for governments' following enlightened policies, for that takes far-reaching compromise.**

The problems of making room for China should not be underestimated. But the US, EU, Japan, and China have only one good choice: to begin intense consultations among themselves, well beyond what now takes place. They must hammer out more understandings about how to accommodate China in the world economy, albeit in some measured way. They must face frankly the challenge of keeping under control what will be decades of political tensions.

There will be a need for new trade and financial arrangements that balance everyone's interests. New understandings about the rules for energy competition will also be required. The US will have to understand that it can no longer monopolize power in Asia in the way it has these past 50 years – not just because of Chinese and Japanese ambitions, but also because of its overstretched resources – and find a way to cede some of it without giving up a leadership role. China will have to recognize that Japan can be – and wants to be – a highly constructive and stabilizing force in the world.

This much is certain: Allowing things to proceed along the current course is more likely to be a recipe for intense political and economic conflict than for a continuation of the relative harmony that has existed these past two decades. So something has to give. Something has to change. Admittedly, there is little precedent for governments' following such enlightened policies, for that takes far-reaching compromise. But the world has become much smaller, the web of communications and relationships much tighter, the importance of enlarging the pie rather than just carving it up much clearer than ever before. Unless a new order is negotiated, the world will risk entering a frightful period where damaging political and economic turmoil is no longer a far-fetched prospect.

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