

# **U.S.-China Relations – A Look Back and Ahead**

**Keynote remarks by**

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*[Note: These are notes from which remarks were drawn.]*

## **SUMMARY**

Contrary to popular wisdom, the US-China relationship has, all things considered, been managed very well. There have been ups and downs, for sure, but the benefits of cooperation and the boundaries of tolerable conflict have been recognized by the leadership of both countries in a rather remarkable way. After all, these are two nations with different histories, cultures, institutions, political and economic systems, and even fundamental priorities. And while one of them more or less rules the roost, the other promises to challenge that position. This said, the road ahead will be more difficult. China's internal challenges, its impact on the global economy, its national security imperatives, and America's own lack of proper domestic policies that are weakening its global economic clout – all against the backdrop of a rapidly changing global system – will present horrendous challenges for both Washington and Beijing. Truth is, maintaining the boundaries within which peaceful and constructive relations will hopefully remain will be an enormous task.

## **INTRODUCTION**

The topic also couldn't be more appropriate for today, with visit of Chinese president Hu Jintao to the US and to Yale.

China is also a great topic for the Yale School of Management since the future of that country will have critical impact on global economy – perhaps more so than any other country in this century.

It is a good topic, too, for a school and a university that is devoted to preparing leaders who have a grasp of the interaction of business and society. For even as China changes the global market, it will also reshape everything from global politics to the environment, and these combined changes will touch every country, every community, and virtually all of our lives.

I'm going to strike a few introductory themes and to open the floor for some questions and comments.

I've been asked to talk about the history of US-China relations since China reopened to the world in 1972, and then about some imperatives for US-China relations for the future. This will be a very quick *tour d'horizon* just to provide some context for this conference today and tomorrow.

Let me admit at the outset that I am not a scholar of China in the way so many of the Yale faculty and others whom you will meet these next two days are. But I have had the experience of serving in the Nixon, Ford, Carter and Clinton administrations in the global economic and foreign policy arenas, and I have often had a front row seat as US-China relations unfolded this past quarter century. This was particularly true in the mid-1990s, when I was undersecretary of commerce for international trade in the first Clinton administration and involved in several path-breaking trade missions to China. I also worked with Chinese officials to facilitate American investment there, and helped to lay groundwork of China's entrance into the WTO. I have lived and worked extensively all over Asia during much of this time, including having had deep involvement in Hong Kong. And I have written a lot about China in my Business Week and Newsweek columns and in the Harvard Business Review.

## **HISTORICAL OUTLINE**

We can divide the recent history of US-China relations into five parts:

### **PHASE I**

1972 – President Nixon went to China, met with Chairman Mao, and discussed the possibility of reestablishing relations at some indefinite time in the future. This was of course the watershed event, because for the previous quarter century China and the US were cardinal enemies with no formal relations at all. Nixon’s goal was to acquire China’s cooperation in winding down the war in Vietnam, and getting China on the US side against former Soviet Union. BIG ISSUE: TAIWAN. How could the US not abandon its long standing support for Taiwan – support that constituted one of the bedrock principles of U.S. foreign policy – and at the same time recognize Chinese sovereignty over it?

## PHASE II

1978 – President Carter established formal relations. It took these six intervening years to accomplish this. SAME BIG ISSUES. China card vs. Soviet Union. It was a tortuous process of fuzzing the Taiwan issue so that the overall relationship wasn’t ruptured. There were almost no economic ties at this point.

## PHASE III

1978-1989 – Relations started to normalize. They were not warm but also not cold. China was entering the international fold. But then came Tiananmen and while relations weren’t severed, they almost were and they at least went back to square one. The event had the effect of bringing all anti-China political views in the US together, both from the right and the left. Everyone from pro-Taiwan to human rights advocates came together. The US imposed economic sanctions. Relations were *de facto* frozen. Further progress dead in the water.

## PHASE IV

1993-2000: Clinton years. There was a move from the dead-in-the-water Tiananmen environment to normal economic relations. That was a huge distance to travel. Clinton campaigned against the “butchers of Beijing.” Two years later he became one of China’s greatest advocates in the US. This was the first time US had the perception that trade from China could be significant, although no one envisioned what would eventually happen. Clinton’s efforts

culminated in China's entrance into WTO – a transforming event for China and world.

## PHASE V

Current administration. Started off rocky, too. “Strategic competitors,” was the term of art. But by now China's economic significance was apparent to all.

Here is a startling statistic. At the end of the Clinton administration, two-way US-China trade stood at about \$75 billion. Even before the Bush administration is over, it now stands at \$285 billion – four times as much.

But there was much more, too. Key events were 9/11 and North Korea/Iran, cooperation on terrorism and non-proliferation, the latter creating some tension because of the differing positions.

Today, there is no major international issue – political, security or economic – in which US-China relationship is not relevant.

## **SUMMARY OF 46 YEARS**

1. Huge Progress, obvious point: US-China relationship has come a long way.
2. Issues have come full circle – The issues started out as political and strategic. In the 1990s the economic issues came to the fore as China emerged as so important in the global economy. But eventually the security questions reemerged such that the US and China have overlapping interests and tensions across the board – political, military, economic, environmental.
3. Substantial global integration – Let's not forget that in the early days of US-China engagement, if you were to ask top Washington officials what their hopes were, they would have said they involved China's full integration into the international system – the UN, the trade and financial systems. Well, that has been achieved in spades. They would have wanted China to be on the same side as the US on the most contentious political problems of the day. That, too, is pretty much the case.

**IN FACT, MY READING OF THIS RELATIONSHIP IS THAT IT IS VERY STRONG, REMARKABLY STABLE ACTUALLY, EVEN REMARKABLY SUCCESSFUL. NOT NECESSARILY ALWAYS FRIENDLY ACROSS THE BOARD, NOT NECESSARILY WITHOUT SET BACKS ON A PARTICULAR ISSUE, BUT THE TWO LEADERSHIP GROUPS HAVE RECOGNIZED THAT THE ALTERNATIVE TO THE US AND CHINA WORKING TOGETHER IS ALWAYS WORSE FOR BOTH COUNTRIES, AND MOREOVER THAT THE STAKES IN WORKING TOGETHER, RATHER THAN AT ODDS WITH ONE ANOTHER, ARE VERY HIGH. TODAY THIS RELATIONSHIP IS KEY TO GLOBAL PEACE AND TO A PROSPEROUS WORLD ECONOMY.**

**THIS MAY SOUND LIKE A MUNDANE OBSERVATION, BUT IN FACT THERE ARE CREDIBLE PEOPLE WHO THINK MUCH DIFFERENTLY. PROBABLY MOST OF THE US CONGRESS WOULD DISAGREE WITH ME, FOR EXAMPLE. THERE ARE THOSE WHO BELIEVE THAT OVER TIME CHINA'S AND AMERICA'S INTERESTS ARE ON A COLLISION COURSE, AND THOSE WHO BELIEVE THAT WE SHOULD BE MUCH MORE AGGRESSIVE IN OPPOSING CERTAIN CHINESE POLICIES NOW. THERE IS YET ANOTHER GROUP THAT BELIEVES THAT THE RELATIONSHIP IS VERY FRAGILE, AND THAT ISSUES LIKE NORTH KOREA OR TRADE COULD EASILY DERAIL IT. I THINK ALL THESE PERSPECTIVES ARE WRONG.**

**IT IS, IN FACT, RATHER REMARKABLE HOW TWO COUNTRIES, WITH SUCH DIFFERENT HISTORIES, CULTURES, POLITICAL SYSTEMS AND PRIORITIES HAVE MANAGED TO KEEP THINGS FROM GETTING OUT OF HAND. I SUSPECT FEW HISTORIANS WOULD HAVE PREDICTED THIS STEADINESS AND THIS LEVEL OF PRAGMATIC REALISM 36 YEARS AGO WHEN THE RELATIONSHIP BETWEEN WASHINGTON AND BEIJING BEGAN TO BE FORMED.**

- 4. THAT SAID, THERE IS ONE EXPLOSIVE WILD CARD: TAIWAN. IF THINGS GO WRONG BETWEEN CHINA AND TAIWAN, THAT COULD CHANGE EVERYTHING. THIS**

## **WOULD HAPPEN, OF COURSE, IF TAIWAN WERE TO DECLARE INDEPENDENCE AND CHINA TOOK MILITARY ACTION, SETTING OFF US INTERVENTION.**

### **LOOKING AHEAD**

In many ways, the future could be more complicated than the past. Reason: For the last quarter century the global setting has been quite benign. An old order – the Cold War – was unwinding, and the US became the lone superpower. Meanwhile, China could focus on its internal development without great international distractions. And coming from such a low base, China could export to the world without causing the kind of dislocations that could result in a protectionist backlash.

**These times are coming to an end.** China has now emerged as a power player in Asia and the world economy.

Its domestic challenges are greater than ever, for its rapid growth has resulted in a variety of problems such as widening income disparities and environmental degradation that will require difficult policy changes and acrimonious internal political debate for many years to come.

Its impact on the global economy has resulted in trade pressures from the US and EU, as well as pressures from abroad to revalue its currency.

Its foreign policy – such as its soft approach to North Korea and Iran, its willingness to do business with rouge states, its fractious relations with Japan – will be increasingly troublesome for the U.S.

Its need for energy and other resources will create competition between it and the US and generate enormous anxieties in the world.

China's environment issues have spilled over to become global concerns, as well.

China's companies will soon become world class multinationals challenging US and other companies.

Every one of these issues has the capacity to become high-profile crises of one sort or another in the US-China relationship, because they are complex issues to handle in any case, but also because in many areas China will be – or appear to be – challenging the pre-eminent position the US has enjoyed for so long.

At the same time there is growing concern in the West about what China will become, both as a political and economic actor. No matter how much it would like the opposite, China is too big and powerful now to have the luxury of focusing inward or focusing just on itself. It will be constantly pressured to assume many new responsibilities to contribute to political and economic stability – from helping to contain North Korea and Iran to helping to strengthen global economic institutions. This will be no small challenge because in many ways the rate at which China is gaining global influence is greater than its feeling of having responsibilities to the global system.

There is another issue, too. As I said, it is remarkable how China has integrated itself into the global system so quickly and deeply. But now that it is inside the tent, and now that it has substantial clout, it is likely to want to influence the shape of the system itself. Given that for the most part, this is a system built and led by the US, there is no guarantee that China and the US won't clash over some fundamental issues and directions.

All this will be occurring in a world that itself is changing very fast.

The structure of global trade is being revolutionized under the influence of complex supply chains, the growth of offshoring, and shifting centers of industrial production, R&D, etc., not to mention billions of new workers who have entered the mainstream of the global economy.

The international financial system has become exceedingly complex under the weight of new financial instruments raising all sorts of questions about what constitutes prudent regulation and how well equipped the world is for crisis management.

The global energy system is under great strain as demand exceeds reasonably priced supplies, and as resource nationalization heightens geopolitical tensions.

The nuclear club seems to be falling apart and proliferation could become the order of the day.

Many emerging markets besides China are coming on to the world stage, such as India and Brazil.

Its old news that the Cold War system is long gone, but its still not clear what is replacing it.

The US-China relationship is central to the resolution of every one of these issues, even as it complicates them.

### **What the U.S. Should Do**

There are many ways that I could describe the challenges ahead, but for the sake of manageability let me look at them through the eyes of US policy. I'd like to suggest that America need to do FIVE big things.

#### **Size up the problem correctly.**

- The number 1 priority is to establish the right framework for thinking about China. In particular, that framework has to be big enough. China will not be just an ordinary big country. It's the most important relationship the US will have. The two are the two most important countries in the 21<sup>st</sup> Century. Key to solving all international problems. Cannot get mired in ME and terrorism and distracted from the bigger issues.
- But sizing the problem correctly means not just not understanding the challenge from China but not overestimating it either.
- China will soon have the largest reserves in the world, for example, reaching \$1 trillion this year. But its GDP is less than 20% of America's; its per capita income is just 1/25<sup>th</sup> that of the US; it spends less than 10% of what the US does on R&D.
- China's military budget has been growing, to be sure, but its still 10% of what the Pentagon spends.

- These are just a few examples but we have to come to grips with the factual realities.

Remember that foreign policy begins at home, and that it cannot make up for domestic deficiencies for very long. And in the case of the US, we are handicapping ourselves very seriously.

- The biggest constraints on US behavior are becoming domestic. We have huge budget deficits and an anxious population worried about social safety net. Reversing this is key to American confidence. For trade deficits and currency, we have to do something about our savings rate, in order to reduce reliance on foreign capital. For the energy question we need to reduce dependence on imported oil. This requires everything from a tax on gasoline, to mandatory mileage standards, to incentives to develop alternative fuels. There is a need for big changes in education and workforce training to enhance US competitiveness. These are just some examples.
- China, too, will have to overcome its serious domestic challenges to have the resources and the energy to play the role it wishes on the global stage. To take one big example, it needs to institute policies that make its growth more dependent on domestic demand than on exports. This in turn means, among other things, creating enough of a social safety net so that people won't feel they have to save 40% of their income just to protect themselves for the future.

Deepen and broaden bilateral engagement with China.

- Huge agenda for bilateral cooperation in trade, finance, technology, energy, environment, education. My impression is that these efforts are being made, but they could be expanded into education at all levels, parliamentary visits, more cultural exchanges.
- China is playing this game very well. It has been sending emissaries to meet with many US groups besides the usual Washington suspects. These include mayors, business

leaders, labor leaders, academic leaders. I hope that our diplomatic corps is as savvy.

Build a 21<sup>st</sup> century global economic system that recognizes China's role and takes account of its ideas.

- Strengthening G-8, IMF, WTO, International Energy Agency, need for new organization for international investment. Major point: Multilateralism is essential if every issue isn't to be seen as a win-lose proposition for either the US or China. But China needs seat at table with voting rights appropriate to its influence. It needs to feel that these international efforts have legitimacy, and they won't if China doesn't have a major part in running them.
4. Redouble efforts to cooperate on terrorism, non-proliferation, military matters in Asia. Also effort to work with China to reduce support for rogue states such as Burma or Sudan.

## **CONCLUSION**

As Peter Mendelson, chief trade negotiator of the EU said recently, we are at the beginning of the China story, not the end.

Policies will be unfolding amidst great uncertainties as to how China will evolve.

Think of the questions to which no one can know the answer:

- Will China become an economic superpower that helps build a global framework in which everyone can prosper, or will it attempt to reorganize the rules in such a way that it takes but doesn't give.
- Will it be able to evolve a political system that can deal with its growing domestic discontent, or will it be subject to deep seated internal unrest.
- Will it make a positive contribution to global peace and security, or will it act selfishly enough to undermine those goals?

Between 1972 and today, the US and China did a good job in managing a different relationship. Let's hope they can continue the record even as the environment becomes more complex. But no one should doubt that the road ahead will be much more challenging than the last 36 years have been.

Thanks very much.