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ECONOMIC VIEWPOINT
By Jeffrey E. Garten

It's Time To Let China Into The Clubhouse

Beijing deserves a bigger say in setting global trade policy

Few would deny that China is becoming a powerful force in international trade and finance. But the implications for how the global economy should be managed have received almost no attention. The conventional wisdom of the 1980s and early '90s that the U.S., Germany, and Japan would share world economic leadership was wrong given the consistently disappointing performances of Berlin and Tokyo. The current system in which the U.S. is the only global growth engine is straining under American deficits and an increasingly weak dollar. It is time for a new way to organize global economic affairs, one that more centrally involves the Middle Kingdom.

Alongside the U.S., China is becoming the most important global economic power. Although Beijing's gross domestic product falls somewhere between that of Italy and France today, it tripled in size during the 1990s. According to Fred Hu, a Hong Kong economist and managing director at Goldman Sachs (GS) Asia, within five years its economy could be larger than that of every nation but the U.S. and Japan. China is now the world's fourth-largest exporter and third-largest importer. It has attracted more direct foreign investment than any country except the U.S. Its currency has an impact on global financial stability. Soaring industrialization and higher living standards have boosted global prices for everything from beef to shipping rates. After the U.S., China is the second-largest consumer of imported petroleum. In 2003, its production of crude steel was 20 times that of the European Union.

Asia has embraced a Chinese-centric development model, observes Stephen Roach, Morgan Stanley's (MWD) chief economist. The Middle Kingdom has become the hub of the region's low-cost production. It is now an indispensable source of export growth for countries from Japan to Indonesia and promises to be an even more important commercial partner as Asia embarks on a series of free-trade agreements. Countries in the Far East hold about two-thirds of all official foreign-exchange reserves, and China holds more of them than any country except Japan.

The logic of a much larger role for China in the world economy -- not just as a passive participant but as a leader in managing it -- is compelling. It is premature to talk about a U.S.-China partnership -- a "Group of Two" -- as the spine of a new governing arrangement, but it's not ridiculous to think something like that may eventually be

necessary. Goldman's Hu calculates that the U.S. and China have contributed nearly two-thirds of world economic growth over the past four years. The U.S. is the world's largest consumer society, and over the next decade China is destined to become the largest producer of goods. The U.S. has an insatiable appetite for foreign capital, and China is building enormous foreign-exchange reserves that can help finance America's needs. Currency stability, an open trading system, reasonable oil prices, and management of the massive surplus of Asian labor are possible only if Washington and Beijing cooperate.

It is time to change the arrangements in which Canada and Italy are in the Group of Seven and Russia belongs to the Group of Eight -- while China is in neither. The four economic powers -- the U.S., the EU, Japan, and Canada -- that have appointed themselves the guardians of global trade policy also ought to invite Beijing to join them. It's not right that China's voting power in the International Monetary Fund is far less than that of France or Italy, nor that South Korea and Mexico are in the Organization for Economic Cooperation & Development and China is not.

I doubt that the Bush Administration, which is now preoccupied with getting reelected, spends much time contemplating these issues; indeed, when it comes to China, Washington is more focused on trade protectionism. Moreover, Beijing's elite still think of their country as poor and underdeveloped and are unlikely to welcome more responsibility for global economic management. But unless China's economic ascendance is handled with more political forethought, Beijing's bursting onto the world stage could raise some of the problems associated with the disastrous experiences of Germany and Japan when they challenged the status quo in the first half of the last century. Back then, the economic expansion of those countries created enormous resentment around the world, leading to protectionist policies everywhere -- and ultimately to military conflict. Must history repeat itself?

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