

Press Room

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**Remarks by Special Envoy for China and the Strategic Economic
Dialogue
Alan Holmer
on the U.S.-China Strategic Economic Dialogue:
Sustaining Economic Growth
at Wuhan University**

Wuhan, China - Thank you President Liu and Vice President Zhou for your invitation and for your hospitality. It is a privilege and honor to be with you today at Wuhan University.

Before I begin, I want to extend my condolences to those injured and to the families of the victims of the earthquake in Sichuan Province. I am particularly saddened by the number of students and children affected by this tragedy. The thoughts and prayers of the American people are with the Chinese people at this time, especially those directly affected. Both the American people and the United States government have provided assistance and remain ready to help in any way possible.

I would also like to recognize Wendy Lyle, United States Consul General for the newly established U.S. Consulate General here in Wuhan. We are proud to have this official presence in Wuhan and believe it will strengthen the U.S.-China relationship in the years and decades to come.

When I became Special Envoy for China and the Strategic Economic Dialogue in February of 2007, Vice Premier Wu Yi, a native of your great city, encouraged me to visit the parts of China beyond Beijing and Shanghai. I have happily followed her advice. In the past 15 months, I have been privileged to visit Shenyang, Qinghai, Xi'an, Chengdu, Guangzhou, Shenzhen, Hong Kong, and Ningbo (just yesterday). My trips have included visits to rural villages to see both the opportunities and the challenges you face in promoting balanced, harmonious growth.

I've learned that China is a country of contrasts as it develops rapidly: contrasts between eastern, central and western regions; urban and rural areas; contrasts between one province and another. There are also large contrasts within provinces, and your province Hubei is no exception.

Hubei Province and Wuhan

I have been impressed by Wuhan's strategic geographic location in China and your strong traditions of trade and intellectual advancement that date back to the Han Dynasty. I learned that nearly 2,000 years ago one of the critical battles of the Romance of the Three Kingdoms occurred right here in this area. You are both an ancient and a modern city, a city rooted in tradition but at the heart of an economically rising central China.

An increasing amount of China's – and the world's – economy passes through Wuhan. Your city is a transport nexus for central China, located where the mighty Han and Yangtze Rivers meet, and is critically important for shipping, rail, and highways – as Wuhan sits at the crossroads of one of China's main North-to-South and East-to-West national highways.

I applaud your country's and your province's initiative to promote the rise of Central China. Vice Premier Wang Qishan's speech here in Wuhan less than one month ago was impressive, as he encouraged your region to speed reform and opening. Your efforts to promote the development of Central China through increased trade and investment are significant and worthwhile.

I am here today, in part, to tell you that my colleagues and I in the United States government believe that closer U.S.-China economic cooperation benefits the development of all regions of China and the United States, not just our political and economic centers. Broad-based, high-quality economic growth that benefits the people of our countries is of utmost importance to all of us.

U.S.-China Economic Relations: A Paradox of Optimism and Apprehension

As part of my responsibilities, I also travel widely throughout the United States and meet with business, economic, and academic groups, along with government leaders at all levels. I explain the consequential nature and positive impact of our economic relationship, and the importance of the U.S.-China Strategic Economic Dialogue.

We have a deep reservoir of good will between the people of our two countries. And yet while our growing economic interdependence was once a source of stability in our bilateral relations, it is now increasingly also a source of tension, in both of our countries.

A 2008 survey that simultaneously conducted public polling both here in China and in the United States characterized these mutual perceptions between our countries' two peoples as a "paradox of hope and fear." This survey, published by an influential group of Chinese Americans called the Committee of 100, shows that, on the one hand, a majority of citizens in the United States and China generally hold positive views of each other and broadly recognize the importance of U.S.-China relations and our increasing economic interdependence. On the other hand, a strong majority of Americans view China's growing economic and military power as a serious or potential threat, and nearly half of the Chinese feel that the United States is trying to prevent their country from becoming a great world power.

Both sides recognize that our most common interests lie in trade. Among Americans, trade is regarded as the most likely area of shared interests, yet it also ranks as the most likely source of conflict. There it is again, a mix of hope and fear. These concerns are straining the domestic consensus in both the United States and China on the benefits of economic engagement, leading to the rise of economic nationalism and isolationism among some sectors in both our nations. These sentiments may constrain leaders from adopting policies that are in the long-term interests of the citizens and economies of your country and mine.

Recognizing that this paradox of optimism and apprehension is real, I have come to Wuhan to speak with you about a reality that is central to the well-being of the people of our two great nations: that is, free trade and investment between our two countries are in our fundamental mutual interests. One only needs to consider how far our relationship has developed since we normalized relations nearly thirty years ago to appreciate the rapid growth of our mutual benefit.

I will also describe three essential steps we must take together as we look to the future that will sustain and enhance our mutual, growing economic prosperity.

China and the United States: Beneficiaries of Free Trade, Open Markets, and Foreign Direct Investment

I have been deeply involved with international economic issues for over 25 years. One of the clearest lessons I have learned is that those countries that open themselves to competition, reform their economies, and welcome foreign investment benefit their citizens greatly. Direct investment in another country, such as manufacturing plants or service companies, is the ultimate vote of confidence in that country's economy.

Such openness is the most reliable path to economic growth and reduction of poverty: it provides better jobs and opportunities, improved living standards, greater consumer choice and lower prices and inflation. Openness is not a zero-sum game; it enhances efficiency, productivity, and competitiveness.

Benefits for China

China's reform and opening over the past three decades have arguably produced the most dramatic economic transformation in world history. China has transformed itself from a poor, mostly agrarian, and almost completely closed economy, into an integral driver of the global economy. In the process, China has achieved economic growth of nearly 10 percent per year that has lifted hundreds of millions of Chinese citizens out of poverty. In 2007, China became the world's second-largest exporter, and its trade volume for the first time exceeded the combined trade of Japan and South Korea. Free trade and foreign direct investment have been central to China's extraordinary economic achievements.

While China has benefited greatly from inward investment over the past three decades, it is now becoming a large supplier of capital to other nations as well. According to China's Ministry of Commerce, China's total overseas investment in 2007 was over \$18 billion. Chinese investors visit the United States with increasing regularity to consider foreign investments; we welcome their investments and their confidence in the American economy.

Benefits for the United States

U.S. exports to the world now account for 12 percent of our GDP, the highest level in our history. Exports supplied more than 40 percent of U.S. economic growth in 2007. In the United States, the Peterson Institute for International Economics estimates that the integration of the global economy generates an economic gain of \$1 trillion to the U.S. economy every year.

With respect to China specifically, China is now the United States' third largest export market, with our exports including goods ranging from aircraft,

to soybeans to electrical machinery. In the past decade, our exports to China have increased six times faster than our exports to the rest of the world. A recent study by the U.S.-China Business Council found that over 90 percent of U.S. congressional districts had triple-digit export growth to China in the past 8 years.

In a speech in Shanghai two weeks ago, my colleague David McCormick, Treasury Undersecretary for International Affairs, noted that foreign direct investment flows into the United States were \$204 billion in 2007, nearly double the level of a decade earlier. Foreign-owned firms in the United States directly employ over 5 million Americans – 4.5 percent of all private sector employment. These are good jobs with good wages, paying more than 25 percent higher compensation on average than other private sector jobs. Foreign-owned firms contribute almost six percent of U.S. output, 14 percent of U.S. R&D spending, and 19 percent of U.S. exports.

Yet the Consensus for Open Economies is Eroding

Despite these compelling facts, the longstanding consensus in support of open economies shows signs of eroding, in both our countries.

Any dynamic economy that is constantly creating new, higher-value jobs inevitably faces factory closings and job losses that are real and painful. The benefits of free trade are often spread across an entire country, while the lost jobs are more focused and immediately visible. But succumbing to the temptation to make trade and foreign investment a scapegoat only breeds support for isolationist policies that will make us worse off, reducing the losses of the present by sacrificing the job opportunities and higher standards of living of the future.

Some Specific Concerns

With respect to investment, we often hear concerns from China about the U.S. investment review process and whether the United States truly welcomes Chinese investment. U.S. legal authority in this area is narrowly targeted to address acquisitions that raise genuine national security concerns, not broader economic interests or industrial policy factors. Last year, for instance, less than 10 percent of all foreign direct investments were reviewed by the Committee on Foreign Investment in the United States (CFIUS), and the vast majority of those were resolved without controversy, including those by state-owned enterprises.

Last month, the Treasury Department issued proposed regulations on investment to clarify and improve our existing review process, reinforce strong open investment principles and procedural protections for foreign investors, and ensure a more timely and efficient review process. We welcome your comment on these proposed regulations.

The United States is strongly committed to maintaining an open investment climate, including for investments from China.

In addition, Chinese officials have expressed frustration that the United States has filed cases in the World Trade Organization (WTO) against Chinese practices. But we should not regard such actions as a failure of our bilateral economic relationship. Rather, the WTO provides neutral, legal mechanisms to address issues that cannot be resolved through negotiation. As U.S. Trade Representative Susan Schwab has said, "WTO dispute settlement is designed to prevent trade wars rather than fuel them."

From American companies investing in China, we often hear concerns that China's interest in foreign investment is no longer as robust as before, that foreign investment regulations are opaque and seem to be designed to favor Chinese "national champions." These concerns include implementation of the new Anti-Monopoly Law; protection of specific Chinese competitors rather than competition in general; technical standards that appear to be discriminatory; treatment of foreign firms more harshly than Chinese firms; and other steps inconsistent with China's impressive move toward market-based economic principles.

The Role of the SED

Fortunately, the Strategic Economic Dialogue provides a forum and a mechanism to address these and other issues. At our most recent Cabinet-level meeting in December 2007, the United States and China agreed to create a high-level exchange on investment and to intensify ongoing discussions about a Bilateral Investment Treaty to provide meaningful investor protections.

Each twice-yearly, Cabinet-level SED meeting presents multiple opportunities to share perspectives and clarify misunderstandings. We can never do too much communicating.

The "Three Essentials": Keys to the Future of U.S.-China Economic Cooperation

I have been privileged to support and participate in our semi-annual discussions between the economic leaders of our two countries, led on the U. S. side by Secretary of the Treasury Henry Paulson and on the Chinese side by Vice Premier Wang Qishan (formerly by Vice Premier Wu Yi). Through the SED, we are strengthening the foundations of the U.S.-China economic relationship, and we are pursuing solutions to the big, strategic economic issues that face our two countries.

As we do so, there are essential behaviors we must strengthen if we are to continue to enhance our economic strength and mutual interests. I will name three.

Essential Number One: Keep Relationship on an Even Keel

When President Bush and President Hu Jintao established the SED in 2006, they envisioned a forum and a mechanism to allow both governments to communicate at the highest levels and with one voice on issues of critical, long-term importance to ensure bilateral economic stability and prosperity. And that's what direct engagement does: it keeps the relationship on an even keel by lessening miscommunication and dispelling misperceptions so common in the history of the U.S.-China relationship.

This kind of enhanced dialogue and engagement means we must confront problems frankly and honestly – and often rapidly. One example is product safety.

In the spring of 2007, many Americans were alarmed about a wave of reports of unsafe food and product imports from China. The credibility of the "China brand" in the United States was at risk. Fortunately, at the Cabinet-level SED meetings in May, 2007, our governments were able to begin intensive work together to address this problem. And at the SED meetings in December 2007, we achieved two landmark agreements on food, feed, drugs, and medical devices.

While there have been bumps along the way, those agreements and related interactions have fostered a culture of collaboration. But this is just the beginning. These issues are deep-seated, complicated, and will not be resolved immediately; this is why we need to continue to work together to build science-based quality into each stage of the manufacturing process. Our efforts will be further enhanced by progress on other related and fundamental issues, such as rule of law, transparency, and intellectual property protection.

In fact, the effectiveness with which the Chinese government continues to manage these safety issues will have long-term implications for U.S.-China trade relations, the integration of China into the global trading system, and the sustainability of China's economic growth trajectory.

(2) Essential Number Two: Address Forward-Looking, Strategic Areas of Critical Mutual Interest

Looking to the future of our relationship, we cannot afford to succumb to the problem of "short-termism" where we primarily consider the issues just in front of our eyes. We also need visionary leaders, supported by understanding citizens, who look out at the horizon, identify the transformational issues of our times, and address them now with policies and actions that will help us realize a sustainable and even more prosperous future in the next generation and beyond. Through the SED mechanism, the leaders of our two countries work diligently to identify and address those critical issues – including the need to address our respective macroeconomic imbalances, financial sector liberalization and currency reform, innovation and intellectual property rights, investment, transportation, rule of law, and transparency, among other issues.

One example I would like to elaborate upon is our joint work on energy security and environmental cooperation. The United States and China are shaping, and being shaped by, global energy and environmental trends that have strong economic consequences. Our countries are the world's largest energy consumers and the largest emitters of greenhouse gases.

We share the challenge of achieving balanced economic growth along with energy security and environmental sustainability. It will take resourcefulness, creativity, determination and a long-term commitment to achieve the results we seek.

At last December's SED meeting, the United States and China announced a ten-year cooperative effort on energy and environmental issues. Our ten-year energy and environment cooperative framework is part of that commitment. We will focus on shared objectives, including energy security, lower greenhouse gas emissions, clean water, clean air, clean and efficient transportation, and the preservation of wild and beautiful places.

This effort will challenge our governments, industries, universities, research institutions, thought leaders, and non-governmental organizations to find answers to these and many other questions: How do we reduce dependency on oil and increase energy security? How do we better preserve the natural

environment and prevent greenhouse gas release due to deforestation? How do we meet our energy goals? How do we ensure that our water is clean and safe?

These questions may be answered differently in the United States than in China. Yet our approaches to finding answers may be similar – to implement proven, effective policies, to educate individuals to make environmentally sound decisions, to ensure that companies follow regulations designed to protect human health. Other solutions will require technological breakthroughs and making existing or new technology affordable by reducing market access barriers.

Since December, we have been hard at work developing action plans for joint projects that will build upon and accelerate existing efforts. We are placing a priority on shared goals, such as reducing dependency on oil. We are defining specific energy targets, such as increasing vehicle fleet fuel efficiency and creating incentives for the development and use of alternative fuels. We want to build clean and efficient transportation systems and protect the wetlands and forests of our two countries. These action plans will help each country identify policy solutions to improve implementation of existing regulations and incentives, and challenge us to develop even more innovative approaches and answers.

(3) Essential Number Three: Develop a Culture of Collaboration and Trust

The U.S.-China economic relationship is complex and managing complexity is daunting. It begins with speaking to the right people, at the right time, on the right issues, and in the right way. The Strategic Economic Dialogue – as a new and leading institution in U.S.-China relations – has created these useful channels among policymakers in Washington and Beijing. Our approach engages multiple and diverse government officials in both countries to facilitate more inclusive interactions. It breaks down classic bureaucratic stove-pipes that hinder effective communication and impede results.

And, as important as any contribution, it helps develop and expand trust between leaders. Trust among leaders is a strategic asset in any economic relationship. Views are respected, ideas are shared candidly, and mutual interests are pursued.

Just as there have been challenges along the way since normalization of U.S.-China relations in 1979, there will undoubtedly be challenges in the decades to come. Eliminating challenge is not the primary goal – that would be

impossible – rather, the goal is to create deeper foundations of trust and communication to better manage those challenges.

The deepening of trust and communication is not solely the role of government leaders. It is also the responsibility of businesspersons, workers, farmers, professors, students, and others. And in August, thousands of athletes from over 100 countries, including athletes from the United States and China, will have the opportunity to deepen communication and trust when they participate in the 2008 Beijing Olympics.

Information about each other, accessible through the internet, is exploding. But there is an understanding deficit. We do not know each other as well as we should. The best way to close this understanding gap is through strengthening the exchange of people and our interaction. That's another major benefit of a U.S. Consulate General now here in Wuhan.

We will also advance our understanding and communication because of the new U.S.-China Tourism Agreement and Civil Aviation Agreement, signed at the SED meetings in May and December, 2007. New nonstop flights between Atlanta and Shanghai, San Francisco and Guangzhou, Philadelphia and Beijing, and the other flights that follow, will strengthen the bonds between us.

These interactions provide the opportunity for Americans to underscore that we welcome the rise of a confident, peaceful and prosperous China. A weak and insecure China is not in America's economic or security interests.

Conclusion

One of the most important economic questions of this century is whether we get the economic relationship between our two countries "right." That means stable, growing, mutually beneficial, and supportive bilateral relations. If you question that statement, consider two different visions of the future of the U.S.-China relationship.

The first is a vision that is dark and problematic. It's a future of a superpower and a rising power on a collision course, increasingly suspicious of the other's intentions, scrambling in a zero-sum competition for resources and influence -- oblivious to the possibilities for cooperation that serve our mutual interest. It's a future in which we see each other through caricatures. This future portends a fragile relationship, which is cracked easily by unavoidable misunderstanding and accident.

The second vision is one in which our ability to work together matches the degree to which our economies are already so deeply integrated. In this future, I see the leaders in each nation communicating well, growing in their trust for one another, working through misunderstandings and crises, and expanding -- where possible -- common interests, while recognizing distinct national goals. In this vision, I also see people in each nation that recognize our commonalities -- that we mutually benefit from trade, investment, and all forms of communication and exchange.

It's this second vision that we are promoting through the Strategic Economic Dialogue. It's a vision that I hope you share, of a strong and lasting relationship we will continue to develop, expand, and help flourish.

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