



# Washington REPORT

News and analysis from Washington, D.C. about key issues in U.S.-Asia Pacific Relations

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## Global Issues Take Center Stage In U.S.-China Relations

Dr. Kenneth Lieberthal

*President Obama's highly anticipated visit to China November 15–18, 2009 did not produce headline-grabbing commitments by Beijing to reform its currency policy or increase U.S. imports, among other issues that have fueled the concerns of many Americans about the implications of China's rise. But the visit was not the disappointment that quite a few U.S. media outlets portrayed, argues Dr. Kenneth Lieberthal of the Brookings Institution. It produced agreements aimed at building the fundamentals for effective cooperation on climate change over the longer term, he points out. Most important, Lieberthal says, the Obama-Hu conversations moved global economic, environment, and security-related issues to the center of the U.S.-China relationship.*

**USAPC:** You have described China as “a group of relatively developed islands with a cumulative population of over 400 million people that are scattered around in a sea of over 800 million people who live very much in developing country conditions.”

Please elaborate on how this affects China's perception of its economic status, particularly with respect to the climate change debate.

**Lieberthal:** Until a couple of decades ago China, by anyone's definition, was clearly a developing country and a fairly poor one at that. Since then, it has achieved

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## USTR Kirk, House Lawmakers Agree On Need To Expand U.S.-Asia Pacific Trade Ties

The Obama Administration and key House lawmakers active on trade policy agree on the importance of expanding trade with the nations of the Asia Pacific and view the Trans-Pacific Partnership Agreement (TPP) as a vital means toward this goal.

U.S. participation in the TPP negotiations—which will include Australia, Brunei, Chile, New Zealand, Peru, Singapore, and Vietnam—will provide an important opportunity “to update and upgrade existing Free Trade Agreements (FTA) to high standards that include

environmental protections and workers' rights,” House Trade Subcommittee Chairman Sander Levin (D., Michigan) told a Washington, D.C. program on December 15.

Rep. Kevin Brady (R., Texas), ranking member of the House Trade Subcommittee, concurred that U.S. involvement in the TPP process will enable Washington to shape a higher quality trade agreement. Just as important, according to Brady, the TPP will help the United States become deeply engaged economically

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## Official Washington

In each issue, *Washington Report* will provide the names and contact information for selected executive branch officials with jurisdiction over economic, political, and security issues important to U.S.-Asia Pacific relations. This issue focuses on pertinent personnel from the *Department of State*.

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## Lieberthal Interview

remarkable economic growth, but this growth has been very uneven geographically.

When foreigners come to China they tend overwhelmingly to congregate on the east coast in major metropolises as well as at a couple of major tourist destinations inland. Those are the areas that have benefited most dramatically from this economic growth. They create an image of a China that not only is 21st century, but also in some respects ahead of industrialized countries.

But if anyone travels in China's interior or lives in parts of these cities that are not the glitzy places where foreigners tend to congregate, one would see that the country's modernization in fact is extremely uneven. There are a lot of gaps.

Chinese who come to the United States often say, "Well, on the one hand you don't have the dramatic view of all these phenomenal new structures in Shanghai, but on the other hand, everything works!" Everywhere you go in the United States—from small towns in the Midwest to large cities—is well put together. That simply is not the case in China. There still is an enormous amount that has yet to be brought up to speed.

So when Chinese leaders look at their country, they see the problems of a developing country even as they also see the problems of a modern country—because they

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*Attending to all of China's needs requires a level, speed, and type of economic growth that the West doesn't fully understand*

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govern both. The two sides of that equation interact intensively across the board.

For example, those big modern cities are magnets for rural migrants who come, not in the tens, hundreds, or even thousands, but in the millions. The government has to build structures to house them, provide basic services, and manage their social and economic integration into the urban areas without fundamental disruption.

Attending to all of those needs requires a level, speed, and type of economic growth that the West doesn't fully understand. But we need to understand this because it ultimately affects China's willingness to impose absolute limits on greenhouse gas emissions.

Chinese leaders say their country needs too much steel, cement, aluminum, and new electric power to be able to conveniently take on those limitations. The best they can do, they say, is to be less egregious in their emission of greenhouse gases per unit of output than they've

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## Congressional Watch

**China's Currency Valuation and IP Theft**—Senate Majority Leader Harry Reid (D., Nevada) provided a preview on December 9, 2009 of the more aggressive approach Members of Congress likely will pursue in 2010 toward rectifying the imbalance in U.S.-China economic relations. Although preoccupied with the health care debate, the Senate Majority Leader nevertheless took the initiative to send a letter to Chinese President Hu Jintao. Reid urged the Chinese leader to give his “personal attention” to (1) significant revaluation of the RMB to “bring [it] in line with economic fundamentals,” and (2) ending “rampant” intellectual property (IP) theft and policies aimed at “undermining American competitiveness in sectors where we are strong.”

Insiders suggest that Reid's letter is indicative of growing concern in Congress about the broader impact of China's industrial policies. They say the second session of the 111th Congress likely will see a resurgence of support for legislation aimed at forcing China to revalue its currency as well as bills to strengthen U.S. trade enforcement capabilities.

**GSP Extension**—On December 14, 2009 the House of Representatives passed legislation that would extend until December 31, 2010 the General System of Preferences (GSP) program; the Senate followed suit on December 23. The GSP program was set to expire on December 31, 2009.

Under this program, 132 beneficiary developing countries are eligible to export approximately 3,400 types of products duty-free to the United States. To qualify for GSP benefits, participants must meet certain eligibility criteria, such as whether the country has taken or is taking steps to afford internationally recognized worker rights, and whether the country provides certain protections to U.S. investors. Several Asia Pacific nations are GSP beneficiaries.

House Trade Subcommittee Chairman Sander Levin (D., Michigan) and Senate Finance Committee Chairman Max Baucus (D., Montana) said their respective panels will conduct a comprehensive review of GSP and other preference programs in 2010 to examine their effectiveness in promoting development.

**“Buy American” Provision**—On December 16, the House of Representatives passed the “Jobs for Main Street Act of 2010.” It includes health-related, infrastructure, energy, housing, and educational components aimed at counteracting unemployment and state revenue losses. It also retains the “Buy American” provision that was included in the \$790 billion stimulus bill enacted early in 2009. This provision—aimed primarily at China—requires all iron, steel, and manufactured goods used in public works projects funded by the bill to be produced in the United States. The Senate is expected to consider a “jobs package” early in 2010.

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## U.S.-Asia Pacific Trade

in the Asia Pacific and catch up with China and Japan, which have been actively pursuing their own trade agreements with regional partners. “The United States now only has two FTAs with Asian nations in the works . . . We have been looking back at NAFTA while the Asia Pacific nations are looking toward the future,” he said.

U.S. Trade Representative Ron Kirk, who also spoke at the meeting, shared Brady's concern about the proliferation of Asia-Pacific trade agreements that exclude the United States. However, he was optimistic that U.S. engagement with its TPP partners would evolve into “the largest, most dynamic trade collaboration of our time,” which over time will involve even more Asia-Pacific economies.

**New Model**—The administration is in sync with the House trade leaders about using the TPP process to elevate the standards of trade agreements and, in so doing, create “a model for the future of American trade . . . [that is] in keeping with a changing world.” Amb. Kirk was

asked whether the TPP negotiations would produce a completely new agreement that would override existing FTAs with Australia, Chile, Peru, and Singapore or simply cobble together and consolidate these existing accords.

The U.S. Trade Representative did not answer this directly, instead responding that the administration wants to be as “aspirational” in these negotiations in as many areas as possible and is committed to realizing the highest quality FTA.

**Vietnam**—Reps. Levin and Brady served notice that U.S. lawmakers will be watching closely to make sure that Vietnam is held to the same high standards with respect to worker rights, intellectual property protections, and market reforms as other TPP participants. This will be challenging, both acknowledged, and exemplifies how complicated these negotiations likely will become. Nevertheless, the lawmakers suggested that Congress likely would not approve a TPP accord that did not require major changes from Vietnam, particularly with respect to worker rights.

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## Lieberthal Interview

been before. “But given where our output must go, you can’t reasonably expect us to match your record in putting a cap on and then applying reductions to overall emissions—because frankly, we couldn’t do it even if it were our top priority.”

**USAPC:** As we saw during the Copenhagen climate talks,<sup>1</sup> the Chinese also have problems with some of the proposals aimed at ensuring verifiability of greenhouse gas reductions.

**Lieberthal:** Yes, the Chinese have been very tough on that issue for a mix of reasons. First, there is the matter of sovereignty, and the Chinese are very sensitive about sovereignty. The United States also is very sensitive about sovereignty so we should be able to understand their views and they should be able to understand ours.

Neither of us likes others poking their noses in and telling us what is actually going on in our countries and what we should do about it. This doesn’t sit well in either society—admittedly for different reasons—but nevertheless it doesn’t sit well.

Beyond that, I would suspect China continues to be nervous because at a national level it has adopted a number of very forward-leaning policies on greenhouse gas

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emissions and energy efficiency. Beijing put money behind those policies and has approved projects and passed regulations to give them real teeth.

But the Chinese government is a multi-layered, bureaucratic leviathan. What starts off at the top tends to get adjusted as it goes down through the system. The capacity of central government officials to know accurately what is happening on the ground is more limited than most Americans understand.

For example, when the Chinese build a new power plant, they equip it with world-class technology for efficient burning of coal. For the most part, China builds coal-fired plants. I imagine they estimate emissions from new plants based on the assumption that the plants are operating according to specifications.

However, U.S. investigators, mostly from academia,

who last year visited power plants around South China discovered something interesting. Most of the coal used in these power plants is supposed to come from a huge basin in northern China. This basin produces higher quality coal, which also is more expensive.

But investigators found in talking to local plant managers that when economic times get tough and their profits begin to drop, they discontinue buying the coal from the northern basin and instead use local coal, which is of much lesser quality.

Unfortunately, burning the lower-quality coal permanently interferes with the operation of some of the more sensitive sensors and other high-efficiency equipment, which causes the equipment to perform below specified standards. When the plant resumes using the high-quality coal later on, it continues to perform below standard.

I think Chinese officials probably are worried about what international inspectors might uncover on the ground that they themselves in good faith don’t know about. They are trying to count their emissions accurately, but they are doing this within the constraints of their own capabilities. In addition, they may be worried about losing face against a backdrop of increasing pressure to improve their game.

So for a variety of reasons, the Chinese have been very recalcitrant on transparency, beyond telling you what they are doing and what they are accomplishing. I think it’s going to be hard to get them to change.

Nevertheless, quite a few Members of the U.S. Congress remain very concerned about verification of Chinese commitments. Their view—which I think is wrong—is that the Chinese say they are reducing their emissions, but in fact they are lying. By contrast, when we in the United States say something, we actually do it.

The reality is that at the national level, what the Chinese say they mean, and they put resources behind it. But this is a country that still has a great deal of developing country capabilities, so they cannot accomplish it all.

The intentions of the Chinese are better than many Members of Congress apparently believe. And their performance also is better than many U.S. lawmakers think—but their performance probably isn’t as good as they say it is or that they believe it is. And so you can see the politically difficult choices this creates.

**USAPC:** One of the high points of the Obama-Hu summit in November 2009 was the leaders’ agreement on a package of seven initiatives aimed at strengthening bilateral cooperation on clean energy.

You have spoken about how both countries bring complementary capabilities to this initiative. How do you think elements of the clean energy package will bear fruit in the coming months and years?

<sup>1</sup>The 15th United Nations Climate Change Conference (COP15) was held in Copenhagen, Denmark, December 7–18, 2009.



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**Lieberthal:** These agreements were very well structured. Substantively, they address clean energy from a wide variety of angles, from electrical vehicles, to clean coal (especially carbon capture sequestration), to joint research labs doing some fairly fundamental science on clean energy. In addition, each initiative is quite sensitive to what each side can contribute and how the end product would be in the interests of both sides.

This is not a set of agreements in which the United States gives aid to China and then lets China go off and do its own thing. It is not a set of agreements that calls for a straight technology transfer from the United States to China. The agreements recognize that there are many areas where, if the two countries combine our knowledge and capabilities, they may be able to develop something that is world-class which we both will own and can apply in our own markets as well as in world markets.

The development of electrical vehicles is a good example. China has some good battery technology and strong manufacturing capabilities, while the United States brings to the table vast experience in vehicle design, sales, service, and finance. The same complementarity exists with respect to carbon capture sequestration.

Moreover, these initiatives aren't huge "make or break" projects. They are modest in scale at the beginning, but are structured so they naturally can expand and become more important over time. Through such joint efforts we can build trust and expand our ability to work together.

**USAPC:** So you think that success on clean energy cooperation can spill over into other aspects of U.S.-China relations?

**Lieberthal:** It certainly has the up-side potential to do that because clean energy is one of those areas in which we have major shared interests. Of course, there is a competitive dimension too, but there are major shared interests. The importance of the issue, moreover, will inevitably grow over time as the effects of climate change become more dramatic.

Perhaps most important, the clean energy projects enable the kind of joint cooperation that goes far beyond the normal sphere of diplomats, national security experts, and economic and trade specialists. This initiative will bring together whole communities from major universities, the corporate sector, and the scientific community that normally don't deal with each other on a large scale.

We have the potential over time to create a much larger and more diverse community of people in both the United States and China who are seriously engaged with their counterparts in a multi-decade effort that can benefit

both sides enormously as well as benefit the world—particularly since our two countries emit over 40 percent of global greenhouse gases.

So we're getting off to a good start, and that is why I appreciate the nature of the clean energy agreements. A "good start" here is not something that is big, brash, or showy. It entails building the fundamentals necessary to realize effective cooperation that can be expanded over time.

In a political sense, I think these agreements actually hurt President Obama because the China summit didn't produce a big, dramatic breakthrough that reporters who really don't know much about the issues can write about. Although the White House issued fact sheets and provided media briefings about the President's China visit, I didn't find one single American news outlet that even listed the seven clean energy agreements, much less explained what they will entail.

I believe the President did the right thing in terms of real effectiveness but these agreements are not the kind of achievements that generate breathless press coverage.

**USAPC:** In general, the American media did not portray the China leg of President Obama's Asian tour in a very positive light.

**Lieberthal:** Yes, I agree. I suspect that was because the White House press corps who travel with the President are by their very nature experts on the presidency and not on issues in Asia or technical matters. So regrettably, what they tend to write about is what they know, which tends not to be what's most substantively important in these visits.

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I was in Beijing during the visit and involved in some ancillary activities, although I was not part of the official party. At the time, I thought the visit went very well. On balance, this visit did what it was intended to do. It reframed the relationship.

In particular, it introduced in a very prominent and very visible fashion that, for the first time, global issues have moved to the center of the U.S.-China relationship. These are the global economic/financial architecture, clean energy/climate change, and nuclear nonproliferation—not just North Korea, but Iran and other places too.

The Obama-Hu summit was built around these three global issues and their Joint Statement reflected this, although the press managed to miss all of this. The journalists traveling with the President tended to focus on the

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fact that the students who participated in the “town hall” meeting with President Obama were specially chosen. But it is inconceivable that they wouldn’t have been specially selected.

Moreover, does that mean that the President can’t say what he wants to say? Any good speaker—and President Obama is a very good speaker—can take almost any question and find a way to segue into what he wants to say. And in fact, a large part of that town hall meeting was available for Chinese viewing on a widespread basis.

So I thought the U.S. press did not convey the real value of what occurred in China. The summit didn’t resolve all the issues in bilateral relations by any means, but more informed coverage of the summit would have conveyed a different impression.

**USAPC: There is a view in some American quarters and among some Asians that the United States has become China’s supplicant, of sorts, owing to the enormous U.S. debt held by Beijing.**

**Does China enjoy a greater degree of leverage in its relations with the United States because of the economic imbalance?**

**Lieberthal:** I recently had occasion to dig up the particulars about China’s debt holdings of U.S. sovereign and agency debt. By this I mean the Treasury bills they purchased as well as debt from Fannie Mae and Freddie Mac.<sup>2</sup>

The numbers are really quite startling. China holds less than 7 percent of outstanding Treasury bills and less than 7 percent of Fannie and Freddie debt. China’s foreign direct investment in the United States is 0.1 percent of total foreign direct investment. Chinese entities’ U.S. stock market holdings are a comparably small figure.

So the reality is that China has invested a very significant portion of its foreign exchange holdings in U.S. debt instruments. It is the largest single holder of those debt instruments. But the holdings of those debt instruments are so widely distributed that China’s holdings give it virtually no leverage.

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<sup>2</sup>The Federal National Mortgage Association, also known as Fannie Mae, was chartered by Congress in 1968 as a government-sponsored enterprise. Its mission is to provide “liquidity, stability and affordability to the U.S. housing and mortgage markets.” Fannie Mae operates in the U.S. secondary mortgage market. Rather than making home loans directly to consumers, it works with mortgage bankers, brokers, and other primary mortgage market partners to help ensure they have funds to lend to home buyers at affordable rates. Fannie Mae funds its mortgage investments primarily by issuing debt securities in the domestic and international capital markets. In 1970, the U.S. government created the Federal Home Loan Mortgage Corporation, also known as Freddie Mac, to compete with Fannie Mae and ostensibly create a more robust and efficient secondary mortgage market.

## U.S.-China Economic and Security Review Commission Presents Annual Report To Congress

The U.S.-China Economic and Security Review Commission’s (USCC) cautioned U.S. lawmakers in its 2009 Annual Report to Congress, issued on November 19, 2009, to remain mindful of the impact on U.S. companies and the American economy of China’s industrial policies aimed at supporting export- and investment-led growth. These policies contributed to the imbalances that led to the global financial crisis—and China shows no signs of abandoning them, the report stated.

The bipartisan USCC was established by Congress in 2000 to analyze the economic and national security relationship of the two nations. Its 2009 report made 42 recommendations to Congress for further action. They are based on eight hearings, trips to China, a field hearing in Rochester, New York, staff research, and consultation with the U.S. intelligence community.

The USCC recommended that Congress urge the administration to pursue the following actions to address economic issues:

- Employ World Trade Organization (WTO) trade remedies more aggressively to counteract Beijing’s industrial policies;
- Respond effectively to China’s currency manipulation, including enactment of legislation that has the effect of offsetting the impact on the U.S. economy of China’s currency manipulation;
- Evaluate the trade-distorting impact of China’s use of selective value-added tax rebates and determine what steps should be taken to redress this issue;
- Report on the implications of Beijing’s subsidies on U.S.-based companies that manufacture clean energy products; and
- Examine and assess the adequacy of U.S. export control policy for dual-use technology and consider ways to collaborate more closely with authorities in Hong Kong to prevent the transshipment of controlled technologies from Hong Kong to China.

The USCC also recommended U.S. government action aimed at meeting the rising challenge of Chinese espionage—particularly cyber-attacks—as well as China’s efforts at naval modernization and anti-ship ballistic missile development.

See <http://www.uscc.gov> for the complete report.

### **Pacific Economic Cooperation Council (PECC):**

PECC Co-Chairs, Dr. Charles E. Morrison and Mr. Jusuf Wanandi, on November 11, 2009 presented several reports to ministers of the 21 member economies of the Asia Pacific Economic Cooperation (APEC) forum at their meeting in Singapore. The reports included findings and analysis that supported PECC's call to the APEC economies to pursue "an agenda for inclusive, balanced, and sustained growth." PECC is the only organization to enjoy observer status at APEC.

- **PECC Survey Urges APEC Leaders To Stay Focused On The Economic Crisis**—Dr. Morrison and Mr. Wanandi presented the findings of PECC's signature annual survey of nearly 400 opinion-leaders from business, government, think tanks, and civil society. The survey, which was conducted in October 2009, revealed growing optimism about the economic outlook. However, opinion-leaders indicated it was too soon exit the fiscal stimulus measures that were put in place in 2009 in response to the global economic crisis.

Opinion-leaders also underscored the importance of pursuing certain policies aimed at sustaining growth in the Asia Pacific region once the worst of the crisis has passed. These include: (1) strengthening financial regulations; (2) rebalancing the U.S. and Chinese economies; and (3) increasing final goods trade among Asian economies.

In addition, respondents voiced their support for change in global and regional institutions. More than 80 percent agreed with the view that the International Monetary Fund and World Bank should be overhauled to increase the role of Asian economies in the governance of these institutions. The entire survey (incorporated as the final section of the *2009 State of the Region Report*) may be accessed at —<http://www.pecc.org>

- **New PECC Index Show More Economic Integration**—PECC recognized that economic integration issues likely will receive special attention in 2010. This will be the year that APEC reaches the first of the so-called Bogor targets for free and open trade in developed member economies. To help fuel these discussions, PECC therefore created a new measure of economic integration across 17 APEC economies.

The index is based on a combination of measures that considers the extent to which the reference economies are becoming more alike in their economic characteristics as well as the relative importance of regional trade, investment, and human flows compared to economic relations with the rest of the world. "While there has been a definite trend towards regional integration based on trade, investment, and people flows, since 1998 there has been divergence in terms of devel-

opment indicators, such as GDP per capita, life expectancy, level of urbanization, and educational investments," according Mr. Yuen Pau Woo, President of the Asia Pacific Foundation of Canada, who coordinated development of the index. For further information about the index, see <http://www.pecc.org>

- **PECC Task Force Underscores Importance of Post-Crisis Structural Reforms**—Inclusive, balanced, and sustained economic growth will require structural reforms that change economic relationships within economies and among them, according to the report of a special task force of prominent Asia Pacific economists. PECC established the task force in March 2009 to address the global economic crisis.

The task force noted that APEC has an important role to play in efforts to help each of its economies implement structural reforms. APEC's post-crisis work might include initiatives that boost engines of growth based on common social priorities, such as programs in health care, education, and social safety nets, and common environmental goals. The latter might include investments in energy conservation, clean energy research and development, and energy efficient vehicles and transport systems. See <http://www.pecc.org>

- **PECC Pacific Food System Outlook 2009-2010 Explores Impact Of Food Price Volatility**—Public policies and programs are needed to reduce the impact of high food prices on the world's poor, *PECC's Food System Outlook 2009-2010* stated. PECC's agricultural experts urged regional community leaders to "promote the advantages of an open food system and be vocal about the consequences of interventionist policies." The *Food System Outlook* also found that declining profitability has slowed biofuels growth. This means the new demand for agricultural commodities still is much less than for feed or for direct food use. This report may be accessed at <http://www.pecc.org>

### **Key Official Meetings: January–February 2010:**

- **LDP Policy Research Council Chairman Shigeru Ishiba met Assistant Secretary of State Kurt Campbell and Assistant Secretary of Defense Wallace "Chip" Gregson** to discuss the Futenma airfield relocation issue, January 5–8, Washington, D.C.

- The U.S. House of Representatives begins the work of the second session of the 111th Congress on January 12; the U.S. Senate follows suit on January 19.

- **U.S. APEC Senior Official Kurt Tong and Assistant U.S. Trade Representative Wendy Cutler** will attend the first APEC Senior Officials Meeting (SOM1), February 22–March 7, Hiroshima, Japan.



## Regulatory Update

**TPP Notification**—On November 14, 2009, President Obama announced Washington’s intention to engage with Trans-Pacific Partnership (TPP) countries to shape a regional trade agreement. The TPP countries include Australia, Brunei, Chile, New Zealand, Peru, Singapore, and Vietnam. Shortly thereafter—and pursuant to trade law provisions requiring advance notification and consultation with Congress regarding the negotiation of trade agreements—U.S. Trade Representative Ron Kirk briefed the chairs and ranking members of the House Ways and Means Committee and Senate Finance Committee about the pending TPP talks.

On December 14, Amb. Kirk followed this up with a formal written notice to House Speaker Nancy Pelosi (D., California) and Senate President Pro Tempore Robert C. Byrd (D., West Virginia). He highlighted the potential economic benefits of the TPP, saying the accord would “help to expand American exports, saving and creating good jobs here at home.” Two days later, USTR published a notice in the *Federal Register* requesting public input on the direction, focus, and content of TPP negotiations.

Both of these actions officially begin a 90-day period during which USTR is obliged to consider the views of Members of Congress, business, labor, and any other interested parties about priorities and possible concerns to be addressed in the TPP talks. This input, in turn, is meant to inform U.S. trade negotiators when they sit down with their TPP counterparts for the first round of negotiations hosted by Australia probably in mid-March 2010.

**China’s ‘Famous Brand’ Subsidies**—Amb. Kirk announced December 18, 2009 that China had agreed to end “many dozens” of subsidies that had been supporting the export of “famous brands” of Chinese merchandise and other Chinese products. These subsidies were the subject of a World Trade Organization (WTO) dispute initiated by the United States in December 2008. Specifically, Washington challenged a Chinese industrial policy aimed at promoting worldwide recognition and sales of certain brands of Chinese merchandise through “a vast number” of central, provincial, and local government subsidies. The U.S. complaint charged that these subsidies violated WTO rules. As allowed by the WTO dispute settlement process, the United States (joined by Mexico) initially requested consultations with China. The WTO-sponsored talks are aimed at reaching a mutually acceptable agreement and avoiding a potentially punitive outcome.

**WTO Appellate Body Confirms Ruling Against China on Barriers to the Importation and Distribution of U.S. Copyrighted Materials**—On December 21, 2009, the WTO Appellate Body confirmed the finding of a WTO dispute settlement panel on August 12, 2009 that China unfairly restricts the importation and distribution of U.S. copyrighted materials, such as theatrical films, DVDs, music, books, and journals. The Appellate Body echoed the panel’s call on China (1) to allow U.S. companies to import the aforementioned copyrighted materials and (2) to eliminate discriminatory requirements faced by U.S. distributors in China. Amb. Kirk said this ruling helps to ensure protection abroad for U.S. creative ingenuity.

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## U.S.-Asia Pacific Trade

**Fast-Track Authority**—Levin and Brady were asked whether the absence of fast-track negotiating authority not only weakens the U.S. negotiating position in the TPP talks but also potentially jeopardizes congressional approval of the accord.

Under fast-track authority, which expired in 2007, Congress must approve trade agreements in a timely fashion by an up-or-down vote and cannot amend them. There is a view that fast-track authority strengthens Washington’s negotiating hand since it assures foreign governments that while Congress can reject trade deals it cannot unravel them with amendments.

Levin and Brady agreed that any attempt at this time to renew fast-track likely would fail given questions in

both parties about the impact of a free-trade agenda on American workers. But they disagreed about whether the president ultimately will need this authority to pursue an active trade agenda. Brady argued that as the United States participates in increasingly complex trade negotiations—like the TPP—the president will need fast-track authority to secure their approval.

Levin maintained that the key to securing approval of TPP and any other trade agreements is active consultation between the administration and Congress at every important step. He lambasted the Bush administration for engaging in “pro forma” talks with trade lawmakers rather than participatory discussions. “They ignored our warnings about non-tariff barriers [not properly addressed] in the U.S.-Korea Free Trade Agreement, so now there is a dead-lock,” Levin said.

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## U.S.-Asia Pacific Trade

The House Trade Subcommittee Chairman was pleased, however, with the consultative process initiated by the Obama administration on the TPP. On December 14, 2009, Amb. Kirk formally notified congressional leaders that the administration intends to proceed with TPP negotiations (see Regulatory Update on page 8). He preceded this notice by consulting informally with Levin and Brady and their Senate counterparts, Finance Committee Chairman Max Baucus (D., Montana) and Ranking Member Charles Grassley (R., Iowa). “The importance of meaningful back and forth between USTR and others in the administration and the Congress should not be overstated,” Levin said. ♦

## Export Promotion Gets Fresh Focus In Congress

Senator Ron Wyden (D., Oregon), chairman of the Senate Finance Subcommittee on International Trade, Customs, and Global Competitiveness, provided a preview on December 9, 2009 of what likely will be the next turn in the debate on Capitol Hill about how to foster U.S. economic recovery—export promotion. As 2009 drew to a close, statements by lawmakers active on trade policy invariably emphasized the importance of developing a coherent and aggressive export strategy to help rebalance the global economy as well as create U.S. jobs.

“It is time to roll up our sleeves and create an Export Expansion Strategy,” Wyden said. The strategy not only should help U.S. firms identify and exploit sales opportunities overseas but also eliminate trade barriers and unfair trade practices, the subcommittee chairman said.

Echoing the theme of many recent international conferences on the global economic crisis, Wyden said the key to re-igniting the American economy is through increased consumption of U.S. goods. And “we can find much of this consumption beyond our borders,” he said.

Howard Rosen of the Peterson Institute for International Economics agreed that that increasing exports is important to U.S. economic recovery, but he presented a more comprehensive prescription. “We must implement policies that result in production growing faster than consumption . . . [in addition to] encouraging exports to grow faster than imports.” But achieving those two goals will require “considerable increases in private investment in plant, equipment, and technology,” Rosen said.

Rosen elaborated further on this point in a colloquy with Wyden. “The problem we’re having creating jobs is not entirely because of import penetration,” he said.

“Technology changes and shifts in consumer taste also affect jobs.” But the root of the jobs creation problem remains insufficient investment, Rosen emphasized. He urged subcommittee members to look closely at the new jobs bill that the Senate likely will consider in early 2010 and examine how the provisions might (or might not) sufficiently promote new capital investment.

Subcommittee members also expressed concern that many small and medium U.S. enterprises (SME), which are important sources of innovation and new jobs, are not sufficiently aware of federal export promotion programs. “U.S. companies are losing out to **countries**, not individual [foreign] companies,” Subcommittee Member Debbie Stabenow (D., Michigan) charged. Stabenow has been an staunch critic of China’s trading practices and is the chief sponsor of a bill that would make currency misalignment actionable under U.S. trade remedy laws.

Loren Yager of the General Accountability Office (GAO) said that a recent GAO analysis of U.S. and foreign country export promotion activities indeed confirmed a weakness in SME-targeted services. Moreover, there is a lack of continuity in export promotion strategies making it difficult to determine federal government priorities. Congress should provide a new mandate on export promotion priorities, Yager proposed. ♦

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Not only that but, ironically, U.S. debt paper has never been easier to sell than during the global economic crisis this past year. We’re offering almost no interest rate and still are having no trouble moving our debt because of the flight to safety.

To personalize this, our current situation reminds me of a hypothetical case where most of my disposal income is tied up in investments in one company. I would care enormously how that company performed. But from the company’s perspective, if I only held 6 percent of that company’s outstanding stock, I wouldn’t be able to significantly affect that company’s decisions.

Analogies are not perfect, but that one helps to explain the current relationship between China and the United States. The imagery has become distorted from reality. It would be helpful to everyone if the real numbers were made more visible and explained more fully.

Chinese purchases of U.S. debt at this point are important but not critical to the sale of the U.S. debt. But how the U.S. handles the dollar is critical to China. That should not produce a situation where the U.S. feels it must do whatever China says so you don’t upset your banker. The dependence runs significantly in the other direction.

To my mind, the reality is that the debt connection of

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## Lieberthal Interview

our relationship exists, is important, but is one of a number of important dimensions of our relationship. Overall, we're important enough to each other that we need to deal with each other with respect and as adults. The notion that either of us can simply jerk the other around is wildly unrealistic. At the highest levels of the U.S. and Chinese governments, this reality is understood. But the average person in both countries not does understand this well.

**USAPC: As you mentioned, nonproliferation also was an important agenda item during President Obama's visit to China.**

**You have said that the road to securing China's support for United Nations sanctions aimed at punishing Iran for its nuclear program "goes through Moscow." Would you please elaborate on this.**

**Lieberthal:** We have made very clear to the Chinese how important the Iran nuclear issue is. If Iran should acquire a credible nuclear weapons capability, it would have enormous repercussions in that part of the world—which has enough trouble already.

The Chinese have said they are very concerned about the Iran nuclear issue, but officials have argued that sanctions do not work and often are counter-productive. They simply disagree with us as a matter of efficacy as to how much can be done through the use of sanctions.

Having said that, though, China joined the United States in supporting a resolution that found Iran to be in violation of its obligations as a member of the IAEA [International Atomic Energy Agency]. The vote occurred on November 27, 2009 at an IAEA meeting.

The really important vote probably will occur in January 2010 in the U.N. Security Council. I think there will be a finding by then that Iran is not being responsive to the P5-plus-one process.<sup>3</sup> The Security Council then likely will vote to punish Iran with very tough sanctions.

That is the context within which I said the road to securing Beijing's support goes through Moscow. I think the Chinese really don't want the Security Council resolution to be adopted. But the Chinese really, really do not like to be the only ones on the outside when all the major powers are considering a major, sensitive issue.

Chinese officials apparently hope that the Russians won't support it and they can then hide behind the Russians. But if the Russians do support the Security Council sanctions, China will find itself all alone. And

<sup>3</sup>The P5-plus-one group includes China, Britain, France, Germany, Russia, and the United States. This group was formed to negotiate with Iran about ending its nuclear program.

faced with that prospect, they likely will negotiate hard to take some of the edge off the resolution, and then join the rest of the members of the Security Council in supporting it.

**USAPC: China also has been reluctant to aggressively enforce sanctions against the other threat to proliferation, North Korea.**

**What would it take for China to recognize that Pyongyang's nuclear ambitions ultimately could affect its stability?**

**Lieberthal:** Frankly, I don't think a nuclear North Korea threatens China's stability. Nevertheless, they strongly oppose a nuclear North Korea. And they oppose it primarily because they are concerned that a nuclear North Korea will lead to a nuclear Japan and conceivably a nuclear South Korea. In addition, they don't like that a nuclear North Korea invariably will be at loggerheads with its neighbors and with the United States, which creates the potential for instability in the region.

China's concerns about the domestic impact of Pyongyang's nuclear ambitions grow out of an unstable North Korea—more so than a nuclear North Korea. If a succession crisis creates instability in North Korea, China would be quite worried about refugee flows, loose nukes and who would be controlling them, South Korean and U.S. forces being drawn into peacekeeping and stabilization effort,s and the PLA [China's People's Liberation Army] possibly being drawn in on the other side, among other issues. There would be all these military forces operating in a highly unstable environment potentially without the benefit of effective communications among them.

I think those are the reasons why China is serious about trying to secure the denuclearization of North Korea. Where the United States and China disagree is that China is more reticent than us to take tough measures to pressure North Korea precisely because they fear the destabilization of its neighbor.

The United States is concerned, but China is **very** concerned because it shares a border with the North. If it comes down to where that distinction becomes critical to policy, then I think we may see us in substantial disagreement on that. ♦

*Dr. Kenneth Lieberthal is director of the John L. Thornton China Center and senior fellow in Foreign Policy and Global Economy and Development at Brookings. Dr. Lieberthal was a professor at the University of Michigan for 1983-2009. He has authored 15 books and monographs and over seventy articles, mostly dealing with China. He also served as special assistant to the President for national security affairs and senior director for Asia on the National Security Council from August 1998 to October 2000.*



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The United States Asia Pacific Council (USAPC) was founded in April 2003 by the East-West Center (EWC). It is a non-partisan organization composed of prominent American experts and opinion leaders, whose aim is to promote and facilitate greater U.S. engagement with the Asia Pacific region through human networks and institutional partnerships.