



## **Emergence of China in the Asia-Pacific: Economic and Security Consequences for the U.S.**

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Madame Chairman, members of the Subcommittee on East Asian and Pacific Affairs, I am pleased to appear before you this afternoon to discuss a topic that has engaged policymakers, legislators, academics and citizens alike for the past quarter of a century – China's growing influence in Asia. Dealing with China's emergence – its economic and political development, its engagement in a rules-based international world, its evolution as a major military presence in the region – will be a key challenge and an important opportunity for the United States and its allies and friends and over the next quarter of a century and beyond.

### **Getting Our Relationship with China "Right"**

For three decades, seven Administrations have sought to integrate China and its people into the international system. We have succeeded in developing a bipartisan policy that has met with considerable success since 1972. Today's challenge is different from 30 years ago: the key question is how a more integrated and powerful China uses its growing influence and whether it will do so in concert with the United States and its allies. Will it accept the challenge of the international community to help enhance the peace, prosperity, and stability of the region and in doing so, positively change the international system as we know it today? As Secretary of State Rice said in a March 19 speech in Tokyo, the U.S. "welcomes the rise of a confident, peaceful, and prosperous China...[and wants] China as a global partner," but one that is "able and willing to match its growing capabilities to its international responsibilities."

We also seek a China that is moving toward greater openness and rule of law at home, though it clearly has a long way to go. How China changes depends mostly on the people of China, but how others and we interact with it will have an impact on the environment in which China makes its choices.

To further integrate China into regional and global security, economic, and political arrangements will require us to maintain active U.S. engagement in the Asia-Pacific region and around the world. Remaining a steadfast partner to our allies and friends in the region is a fundamental tenet of American foreign policy.

Getting our relationship with China "right" is vitally important. A decade ago, we all wanted China to be more actively involved in regional and global affairs. We wanted China to engage with Taiwan in a dialogue that would lead to the peaceful resolution of outstanding differences acceptable to the people on both sides of the Strait. And we wanted it to open its market of 1.3 billion people to U.S. goods and services.

We have achieved much of what we asked for on the latter: China is a member of the World Trade Organization, it is the world's third-largest trader after the U.S. and Germany, and it is investing around the globe in Asia, Africa, and the Western Hemisphere. Among our tasks now – and one we share with our allies and friends – is to ensure that in its search for resources and commodities to gird its economic machinery, China does not underwrite the continuation of regimes that pursue policies seeking to undermine rather than sustain the security and stability of the international community. We also want to ensure that China joins our efforts in the WTO to lower barriers to world trade; in short, that it cooperates across-the-board with the United States in ways appropriate to the first new great power of the 21<sup>st</sup> century.

### **U.S.-China Ties Not a Zero-Sum Game**

China's success in extending its political influence in the Asia-Pacific region and throughout the developing world is, in my view, a logical evolution, closely tied to its emerging economic clout, and certainly is not a zero-sum game for the United States. Nor should China see our continuing pursuit of U.S. national and security interests in the region as a threat or a loss to them. I believe that China well understands that we are an Asia-Pacific power and that other members of the Asia-Pacific community – and here I would say China included – look to the U.S. market, U.S. investment, U.S. technical expertise, and to our open and vibrant society. And for the 60 years since the end of World War II, the Asia-Pacific community has looked to U.S. military forces in the region as a guarantor of peace and stability.

There is much that is complementary with China in our approach to the region and much on which we look forward to cooperating with them. As the President said on May 31, our relationship with China is complex, but at least in recent years we have been able to communicate often — in remarkably candid and direct fashion, when necessary — and to address common challenges — regional and global, economic and political. Of course, we do have differences with China on a variety of important issues, including human rights, non-proliferation, Taiwan, and some aspects of trade and finance, among others. We seek to ensure that our differences do not preclude cooperation in areas where we agree. All of these issues must be handled sensitively, but in ways that advance our values and national interests. Let me say again that we intend for our relationship with China to be based on a realistic appraisal of our common interests and the exploration of differences through dialogue.

### **The Economic Dimension of U.S.-China Relations**

Let me turn to the economic side of China's emergence and especially how that affects the United States. China's WTO accession in 2001 was a remarkable event. Its implementation of its commitments has created many opportunities for U.S. firms and exporters. U.S. exports to China have grown by 80% since accession, while total global U.S. exports grew just 11% during that same time. Nonetheless, serious problems abound in a variety of areas, from ineffective enforcement of intellectual property rights and barriers to distribution of products, to non-tariff barriers in agriculture (including a ban on U.S. beef) and a dramatic surge in textiles with the termination of the quantitative restrictions allowed by the WTO Agreement on Textiles and Clothing.

We expect China to fully and effectively implement all of its WTO commitments and to take action on key trade and economic concerns to further open its market and eliminate distortions. We are determined to see change and have made that clear to the highest levels of the Chinese Government. A number of these issues will be discussed at the Joint Commission on Commerce and Trade this summer. At the same time, extreme protectionism is not the answer. We need to find solutions that do not derail our broad, long-term commitment to free and fair trade. I believe the countries of the Asia-Pacific

region share many of these same concerns about maintaining open markets and insisting on fair, rules-based trade.

Protection and enforcement of intellectual property rights (IPR) in particular remains a vexing problem and a top priority in our trade relationship with China. If China does not provide effective enforcement of IPR, it will undermine the development of knowledge industries and innovation around the world. Piracy and counterfeiting in China are rampant. If we can make it, they can fake it. The items being pirated and counterfeited range far beyond DVDs and other creative media. They include automobile brakes, even entire passenger cars, electrical switches, medicines, marine pumps, processed foods, and other items that create health and safety risks in China and abroad because of poor product quality regulation. The scope and magnitude of the problem is huge and increasing – some American firms experience wholesale theft of product lines. Premier Wen Jiabao, Vice Premier Wu Yi, and others have spoken of the importance of IPR to an advancing economy and of the need to enforce IPR more actively. Yet, piracy and counterfeiting rates are as high as ever. We need to see a substantial reduction in IPR infringement in China; that is the real measure.

As a result of USTR's Special 301 determination and out-of-cycle review of China's IPR regime, we are taking a number of actions, including considering using WTO procedures to ensure China's compliance with its obligations, invoking transparency provisions within the WTO to request that China produce detailed information about its enforcement activities, and using the JCCT to secure new, specific commitments to significantly improve IPR protection and the enforcement environment in China.

We are also urging China to take a responsible role with regard to its exchange rate policy. As Treasury Secretary Snow noted in his most recent report, China's current exchange rate policy is "highly distortionary," and poses risks to the Chinese economy and global economic growth. The Chinese leadership has committed to adopting a more flexible, market-oriented exchange rate regime; we believe the time is right for them to do so.

China's leaders say they do not want economic and trade frictions to spill over into other aspects of our growing relationship. That will only be the case if we hold firm to our insistence on China's fulfilling the obligations it took on when it joined the WTO and the commitments it has made in bilateral and multilateral discussions since then.

### **China in the Asia-Pacific**

There are two main drivers behind China's emergence in Asia: a dynamic view of how trade and investment fuels its own domestic development; and a desire to match its growing economic weight with political influence to allow China to help shape the regional system to its advantage, where possible.

#### Trade and Investment

The ability to bring economic growth and prosperity to its citizens is a key function that defines the legitimacy of any government; in recent years, as China has gone from a strict command economy to one in which market forces have played an increasing role, China's leadership has been successful in reducing poverty and delivering a better way of life for the majority of its citizens. The economy has grown an astounding 9% per year for the past 25 years; of course, this growth is coming from a very low base. China's economic orientation remains largely domestic – focusing on domestic investment, infrastructure development, and renewal – as the country tries to create the equivalent of 2 million new jobs a month for a growing workforce. However, a significant part of China's economic growth now depends on its outreach to the Asia-Pacific region and to the rest of the world to secure inputs, especially raw materials and commodities and energy, and markets. This growth has inevitably meant increasing global engagement and expansion of China's national interests.

At this point, China's growing demand for resource inputs has contributed to sometimes significant price increases on world markets, but does not appear to have distorted international markets and caused physical shortages or debilitating price spikes, and China is working with international bodies such as the International Energy Agency on management best practices. The biggest impact on U.S. national interests is China's willingness to invest in and trade with problem states (Iran, Sudan, Burma). We are concerned that China's needs for energy and other resources could make China an obstacle to U.S. and international efforts to enforce norms of acceptable behavior and encourage China's participation in international organizations to counter this tendency.

China's most dramatic diplomatic, political, and economic gains of the past few years have been in Southeast Asia. Two years ago China signed the ASEAN Treaty of Amity and Cooperation and last year it took steps to complete the China-ASEAN Free Trade Agreement. Following an initial lackluster response to the tragic tsunami in South and Southeast Asia last December, China, like the United States, gained a large measure of regional goodwill by offering considerable government and public aid, and providing medical teams to help in hospitals and displaced persons camps.

China has become one of the largest traders and investors with many Asian countries. Trade with ASEAN nations grew over 30% and surpassed \$100 billion dollars in 2004. China became South Korea's top trading partner in 2004: their two-way trade China grew nearly 40% last year to US\$ 79 billion. China also became Japan's largest merchandise trading partner last year, with total two-way trade reaching US\$ 214 billion.

Nonetheless, U.S. trade with these and other Asian nations remains robust. U.S.-ASEAN trade tops \$136 billion; U.S. two-way trade with Korea totaled US\$ 72 billion; and our two-way trade with Japan reached \$183 billion in 2004. U.S. trade and investment in the region is also qualitatively different from what China has to offer. Our comparative advantage remains in high-tech, research and development laden, goods, services and agricultural products. China exports primarily consumer goods that, for the most part, do not compete directly with U.S. products.

China isn't just trading; it is also investing in the region. China recently became one of the largest investors in Indonesia, buying into oil and gas interests. China's investment in Indonesia's energy sector now exceeds US\$1.2 billion. And China is the largest foreign investor in some of the smaller economies in Southeast Asia; for example, China has recently become Cambodia's largest investor. Even so, China's outward investment pales in comparison with that of the U.S. China's cumulative realized investments overseas totaled approximately US\$ 37 billion for all countries at the end of 2004; U.S. direct investment abroad stands at over US\$ 2 trillion. In ASEAN countries, the U.S. has invested over US\$ 85 billion; Chinese investment doesn't yet reach US\$ 2 billion.

China's approach to its Asian neighbors reflects recognition of its strategic considerations. By proposing to negotiate a free trade agreement with the ASEAN countries, China offered to share the benefits of its economic growth – while reminding the region of its growing reliance on China. We welcome China's willingness to expand the benefits of growth to others.

At the same time, the United States is working to strengthen its trade and investment ties with the region. In October, 2002, the President announced the Enterprise for ASEAN Initiative, which offers the prospect of Free Trade Agreements to ASEAN countries that are committed to reform and liberalization. Under this initiative, we have already completed an FTA with Singapore, are negotiating an FTA with Thailand, and have strengthened our trade ties with ASEAN countries like Malaysia, Brunei and Vietnam. We are also working together within APEC to bring down barriers to trade and investment throughout the region.

### Political Influence

China also uses its growing trade and investment ties to achieve its political ends, which include continuing to isolate Taiwan. China's size and expanding economic integration ensure that its already significant role in East Asian security calculations will become larger in the years to come. China is a nuclear power with a large standing army and has become more of a "status quo" player in Asia. Its economic modernization increases its economic impact and enhances its political influence. Its military modernization aims at greater professionalism, upgraded aerial, naval and missile capabilities, enhanced command and control functions, and a rapid-deployment conventional force.

However, China's growing security and military relationships with traditional U.S. Asian allies should not suggest that somehow U.S. influence or capabilities in the region have been diminished. U.S. policy toward Asia is anchored in our strong and enduring alliances with Japan, Australia, South Korea, Thailand, and the Philippines, which continue to provide unprecedented stability and prosperity in the region, and is reinforced by friendships with others in the region. Our allies throughout the Asia-Pacific region believe good U.S.-China relations are important to regional peace, prosperity, and stability. Our efforts to work with China in key regional groups like the ASEAN Regional Forum and the Asia Pacific Economic Cooperation organization will enhance, not impair, our regional alliances, which are the primary guarantors of security in Asia.

China's relationships with Taiwan, North Korea, and Japan deserve mention here.

The P.R.C. strategy on **Taiwan** is based on a refusal to renounce the use of force while simultaneously encouraging economic integration by making itself attractive to Taiwan investors. China also seeks to leverage its economic influence with countries of the Asia-Pacific region and beyond to generate support for the P.R.C.'s stand on Taiwan. We saw this recently when a number of countries like Burma, Cambodia, and Laos issued statements in March welcoming China's unhelpful Anti-secession Law.

The longstanding U.S. position, based on our one-China policy and commitments under the joint communiques and the Taiwan Relations Act, has been that cross-Strait differences must be resolved peacefully through dialogue in a manner that meets the aspirations of people on both sides of the Strait. To that end, the USG strongly encourages cross-Strait dialogue of all forms. The anti-secession legislation adopted by China's National People's Congress was an unfortunate and unhelpful step that did not contribute to cross-Strait stability. Under Secretary Burns testified before this Committee on the actions the U.S. Government took to dissuade China from pursuing the legislation and register our disappointment upon its passage. Since then, China has reached out to opposition figures on Taiwan, culminating in the historic visits to Beijing by leaders of the Kuomintang (KMT) and People First Party (PFP). We encourage any form of cross-Strait dialogue and believe that the unofficial KMT and PFP visits have the potential to serve as an important first step in the resumption of a dialogue between Beijing and Taipei. It is crucial, however, that China take the important next step of reaching out to elected representatives on Taiwan. We believe that recently stated positions on both sides of the Strait incorporate elements of flexibility that could form the basis of substantive dialogue.

For the most part, China's political goals need not be viewed as antithetical to our own. China has been very supportive of the Six-Party process in its role as host of the Talks. China has made clear on numerous occasions at the highest levels that it shares our goal of a Korean Peninsula free of nuclear weapons. Our main problem is a **North Korea** that has boycotted the Six-Party process for almost a year. China has the closest relationship with North Korea of any of the Six Parties and it is for this reason that we continue to engage the Chinese leadership on the North's lack of willingness to make a non-nuclear Korean Peninsula a reality. It is incumbent on each of the Parties, particularly China, to make very clear to North Korea that the time has come for it to return to the talks in a way that demonstrates that it is ready to make a strategic choice about its programs.

Unresolved tensions between China and **Japan** reemerge from time to time, causing disruptions in the development of a relationship that is of great importance to the region. As we witnessed recently, grievances about Japan's wartime legacy periodically erupt in China, most recently over changes to Japanese history textbooks that led to anti-Japanese violence. While Japan and China are more integrated than ever on the trade front, recent controversies over the Senkaku Islands, East China Sea energy exploration, China's posture toward Taiwan, and China's public opposition to Japan's bid for a permanent seat on the UN Security Council have chilled the relationship. The recent violent demonstrations in China against Japanese diplomatic and business facilities only serve to prolong ill will among neighbors. Disputes should be resolved through peaceful dialogue and discussion.

Healthy China-Japan relations are essential to stability and prosperity in East Asia. The two nations have many common interests, and we encourage stable relations between them and engagement on a full range of issues. Recent senior government discussions between them were useful, but regrettably, a much-anticipated meeting between Prime Minister Koizumi and Vice Premier Wu Yi did not take place. We support high-level dialogue between the two countries to work through all concerns.

### Some Final Observations

Let me conclude with a couple of observations.

**First**, China's global emergence is a natural consequence of economic growth and development.

**Second**, we must work with China, and with our partners around the world, to ensure that its emergence takes place within strong regional and global security, economic and political arrangements and I believe that this will be one of the key objectives of the new U.S.-China dialogue to be led by our Deputy, Bob Zoellick.

**Finally**, we must guard against actions that threaten to disrupt our economic and security interests. I assure you that a strong, secure United States and a strong, secure, prosperous and stable Asia-Pacific remain our goal, and a continuing reality.

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