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TRANSCRIPT

Energy 360°

“The Transition: Energy & Climate in the U.S.-China Relationship”

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Quill Robinson: Welcome to Energy 360: The Transition, a CSIS miniseries exploring the energy implications of Donald Trump's victory in the 2024 election. China is the largest emitter of greenhouse gases and the leading global renewable energy manufacturer. The U.S. is the second largest contributor of greenhouse gas emissions and the world's top producer of oil and gas. Any discussion of climate change and energy security must include the world's two great powers. This week, Joseph and I discussed the importance of energy and climate change in the U.S. China relationship with two top experts. Frank Fannon is the managing director of Fannon Global Advisors and a senior adviser with the CSIS Critical Mineral Security Program. He previously served as the First Assistant Secretary of State for Energy Resources under President Donald Trump. Ilaria Mazzocco is the Deputy Director and Senior Fellow with the CSIS Trustee Chair in Chinese Business and Economics. Let's dive in.

Energy and climate policy are at the heart of the U.S. and China relationship. Ilaria, Frank, Joseph, I want to start by just doing a level setting exercise here today. What is the state of the U.S. - China relationship in a word at this moment? Frank, I'll start with you.

Frank Fannon: Terminal decline.

Quill Robinson: Terminal decline. Ilaria?

Ilaria Mazzocco: Tense, and yet, surprisingly, still very interdependent.

Quill Robinson: And Joseph?

Joseph Majkut: I was going to say ambiguous, which I feel like is the combination of what we've just heard from our two colleagues. I mean Ilaria tense but still interdependent. How do you square that with the idea that our relationship may be in terminal decline?

Ilaria Mazzocco: I mean, it may be right, but I'm saying it is definitely very tense and I think it has been on a downward trajectory. And yet I think when you look at all the ties that still remain on the commercial side of things, on the investment, U.S. companies, even on the cultural side of things, if you think of even maybe personal ties that people have, the people to people exchanges, I think it reflects the fact that the two countries have really developed very deep ties over the past 40 years and even before that frankly. And that's very difficult to disentangle and to cut back on. And so despite having had the policies of de-risking and decoupling over the past few years, depending how you want to interpret the various policies that have happened, I would definitely say the U.S. has had a much harsher line on China over the past couple of

administrations, yet we still see that it's a huge, the relationship is still really important. Dependencies are still there and it's still I think going to be a huge challenge to manage this responsibly for the incoming administration.

Quill Robinson: Ilaria, just on the language there real quick. We've heard de-risking, we've heard decoupling. Have we been de-risking or are we headed towards decoupling? What is the right language we should be using here?

Ilaria Mazzocco: Oh, that's a tough question there. I mean, I think in part there's a question of language and then there's a question of actual policies, right? And so I think there's been a shift towards de-risking, which reflected the Biden administration's preference to at least portray its policies as much more targeted rather than a sledgehammer to the full cutting at all dependencies. But of course their de-risking policies have been quite comprehensive and quite broad in their targets. Decoupling has also been a popular term, I think among those who are more hawkish on China, I think both Republicans and Democrats. But I think it's probably more popular among some people that may be going into the Trump administration. That's going to be something to watch. Is that more of the language we're using and does that reflect maybe more of a comprehensive policy on trade, for example? Certainly I think 60% tariffs on all trade with China would reflect more about decoupling strategy rather than a de-risking run.

The risking probably being more focused on strategic technologies rather than overall trade. And so I think that's not something to watch in who gets finally appointed to certain, we're still watching who's going to be appointed to treasury, not, we don't have full confirmation on where Bob Lighthizer is going, which is interesting. I think for months we've all been seeing that's the person we knew was going to be very influential in this administration. He probably still will be, but we still don't have final confirmation if he's going to USTR or exactly what position he'll have. But I think watching that will also tell us more about whether we'll see a prioritization of sort of that technology side of things and the dependencies there or the trade deficit and more of the economic issues and how that will be balanced.

Quill Robinson: So Frank, Ilaria has given us a good overview of the state of the U.S. - China relationship. I want to understand how energy fits into this picture and how the U.S. and China respectively think about energy and what their relationship is with energy. I mean, obviously the U.S. is a net energy exporter. China is a net importer. Could you dive into that a little bit more and explain how that shapes their approach to this very, very important vector of power?

Frank Fannon: You bet. I'd first like to just comment on the language discussion. My goodness. Do we find ourselves with utilization of tortured language to say something that's clearly evident? The reason why we go through these lengths, and not just us, the United States, but the Europeans as well, coming up with new terms to state the obvious. I think we ought to look at what China's actually doing versus what we're saying. And I think that why we do go through this torture language is because I think of something that Ilaria pointed to, which is the commercial links and our companies are the ones who are helping to drive that kind of obfuscation of what's clear. But all of the intelligence reports are quite clear. The FBI China threat webpage is clear. They're behaving in a way that's contrary to our values and seeking to unseat the United States, whether it's de-risking decoupling, we ought to start talking about things less euphemistically and more pragmatically, and I expect that switch going to see with Trump administration.

And in terms of the energy, I would say that the U.S. approach has generally been somewhat inconsistent over time. It's really tied to when does the U.S. have energy and when do we not have energy? And the relative security lens that we approach energy kind of goes back and forth. Now we talk a lot about energy security because we have a lot of energy in the United States, the Chinese, however, I would say that they've been consistent throughout history and that's been especially focused on security. The CCP has directed a policy to develop alternative sources of energy and to leverage existing endowments to the extent to which they have that. In 1987, Deng Xiaoping famously said, the Middle East has oil. We have rare earths. They developed an industry around that.

Similarly, they have domestic coal resources. It's really dirty, but they continue to use it. Last year, China accounted for 95% of the total world's new coal construction that represented 70 gigawatts of new capacity in China compared to less than four gigawatts. The rest of the world, if they have it, they will use it. They're not looking at this through a climate lens. It's wholly within a security lens. And that also has led to the build out of a clean energy supply chain, which is certainly now the envy of the world. From the mine site to the manufacturing of clean technologies, it's all about control to not rely on the U.S. naval protectorate of oil sea lanes and that diversification push. Whereas America is the world's loan superpower, China is the world's super polluter, and they do that not out of a support for or an antagonism against environmental performance, but because they're focused, really focused on security.

Quill Robinson: Joseph, so Frank has helped us kind of understand each country's relationship with energy. How do you think that affects China in particular, but also the U.S.'s view of energy as an international issue, but then also when it comes to climate and international climate negotiations?

Joseph Majkut: I think the most important thing that a lot of our peers don't quite see is a lot of the progress that China makes when deploying renewables, building out EV fleets are not just climate considerations. It is also the economic security and energy security strategy of the Chinese government to reduce its need, imports of sensitive energy commodities, in particular oil, and to develop the manufacturing capacity to supply the energy systems of the future. So solar panels, wind farms, EVs and batteries, but the reality is the Chinese economy is large, still requires still very import dependent. And when we think about the bilateral relationship, Chinese buyers are often anchor clients for things like U.S. LNG export facilities, and when I hear our colleagues talk about terminal decline, I wonder how much is that political versus commercial and how do we, Frank, I'd love to hear your thoughts on how you see those things evolving.

Frank Fannon: No, I think it's a really important point, and let me be clear. I'm looking at China's action, not necessarily some of the commercial relationships. As Trump 1.0 did I reasonably anticipate Trump 2.0 will also call for more LNG exports to places like China? And frankly, I think that's in our interest, it's on our interest to create that linkage that not only advances bilateral opportunity for discussion, but also demonstrates some degree of alignment somewhere, which I think the Biden administration was frustrated with when they really, really had a very strong push to try to do that on the climate change question. Multiple times then secretary or special envoy, Carrie would go to Beijing and meet with leadership, sometimes would get a meeting, sometimes not, but always really trying, really trying. And for each point, the Chinese effectively rebuffed and said that they do not look at this as an area to compartmentalize. They saw it as part of the broader relationship. Would LNG be one of those areas that they would be able to have a collaborative productive dialogue around? I'm hopeful for that. I think that's a great thing.

What I'm speaking about in terms of terminal decline is in part the energy question, what have they been doing on critical minerals and my expectation that the Trump administration we'll call, which was kind of like a burgeoning clarion call, reciprocity, what you do here we should be able to allow us to do there and vice versa, and if it's prohibited for a U.S. company in China, then we need to think twice whether we should permit it in the United States. I suspect that will be kind of one of the

real signals going forward to really see what do the Chinese do. I saw Xi Jinping almost effectively trolling President Trump when he's telling President Biden, he intends to work with the Trump administration on climate change the same day that article comes out. Media reports that China State initiated a dramatic cyber espionage campaign of U.S. telecom systems, so let's see what they actually are doing versus what they're saying.

Quill Robinson: I want to explore what may happen and what President Trump may do more. But before we do that, I am interested in understanding what the Biden administration was attempting to do and what worked and what did not. My sense is that the Biden administration when they came in realized that climate policy alone was not a uniting enough initiative and wasn't enough to transform the political economy of the United States. And so underpinning of this project with the Inflation Reduction Act and the IIJA as well was an effort to not only advance global decarbonization but also industrialize the U.S. and create jobs and de-risk from China, sort of this three-legged stool to remake the United States' political economy. My sense is that the Trump administration and with Trump's worldview, there's alignment on two of those legs of that stool when it comes to China de-risking or decoupling, but also the reindustrialization of the U.S. perhaps not so much on decarbonization. Joseph, do you get that sense as well? Is there alignment on two out of three or is there something that I'm missing here?

Joseph Majkut: There has been real alignment. We've seen real alignment in certain political imperatives, reshoring manufacturing, but the challenge when you think about the relationship with China that I see for the administration shift or the difference is that the Biden administration, particularly on matters of climate, really wanted to cooperate. That's the biggest emitter in the world and we can't have a successful global response to climate change without Chinese cooperation is the theory of change that the Biden administration had. The Trump administration of course is going to be, we'll acknowledge the same fact base, but we much less concerned about using carrots of cooperation to get emissions reductions from China. Instead, I think we'll see a much more concerted effort to either wave off the issue entirely or try to use relatively more aggressive implements to force Chinese decarbonization, whether that is sort of nascent conversations around carbon tariffs or carbon border adjustments or pushing hard to get the supply chains or value chains that serve American consumers to run X China.

Ilaria Mazzocco: I think one thing to keep in mind is that I think climate cooperation was certainly a goal under the Biden administration, but they really struggled to achieve it. I think part of the reason for that was that trade

and maybe also investment issues were kind of off the table, so they were talking more about this parallel action, which I think was really modeled in this sort of pre-Paris agreement kind of era where the U.S.'s role was to push China to commit more, but now China does commit more and arguably has done actually better than the US and aligning some of its industrial policy with its climate policy. They did well, I think on methane pushing China to come up with a methane plan and they did establish some collaborations on carbon capture. I want to give credit where credit's due, but I think the big elephant of the room remained trade right over capacity or investment, all these different issues which won't be discussed. I think that under the Trump administration, those are going to be the issues that are probably going to be far more central and those are quite important for the energy sector, and I think that's going to be a really sort of exciting area if you actually can get some deals done in that area.

Quill Robinson: Do you see alignment between the Biden administration and the Trump administration on the two of those things?

Ilaria Mazzocco: Potentially some alignment on reindustrialization and whether we want to call it de-risking or decoupling or whatever it is, right? There might be some potential alignment. I don't think the tools will look the same, and I think the tools do matter in terms of where we end up, so I think you are probably going to see a lot more potential negotiation. I think the word negotiation is important and Frank used it and there wasn't a lot of negotiation to be honest during the Biden administration. There was a lot of de-risking for de-risking its purpose not to actually get to a sort of an endpoint of saying, well, we want reciprocity or something of the sort, so not a lot of deal making, let's say. So there's potentially usage of trade. The question is how ready are the Chinese to withstand maybe a trade shock, and that's an open question which we'll have to see. It's possible that they're actually much more resilient than many people in Washington think. That is definitely a possibility, and they've been preparing now I think for four years for this, they're going to be fully prepared to deal with it, which they definitely will not during a Trump one administration. I think the other question is does the version of industrial policy that we'll see under the Trump administration does it work? And I think there's a lot of questions over whether the IRA or the IJIA worked, but I think a different approach which maybe will likely have more deregulation, less subsidies, it will actually stimulate manufacturing in sort of the technologies that we're probably interested on in this podcast is an open question.

Quill Robinson: Frank, I wonder how the Trump administration will view certain technologies as strategic or not strategic. Take solar for example, since

the Obama administration, there's been a steady ramping up of tariffs on Chinese solar under the Biden administration, there was a lot of investment in domestic manufacturing and reshoring that manufacturing. I imagine there's not going to be as much enthusiasm for building up a domestic solar industry under a Trump administration, but could we extrapolate that a little bit? How is the Trump administration going to say technology X is strategic, we need to build it versus technology Y let them have it. It doesn't matter all that much.

Frank Fannon: First, let me be cognizant that I don't know. I can tell you my best guess what the Trump administration 2.0 will do. What I would suspect is what Joseph was alluding to really was speaking to what is the organizing principle of an administration. The Trump 1.0 organizing principle was security. I would also say that that's in part why the continuation of "drill baby drill" as a tagline, because we have the energy here, yes, it's a jobs program and it's also a domestic energy security program. The Biden Harris administration sought as its organizing principle of climate change for the U.S. government to achieve its goal of mitigating climate change. It required China, the world's super polluter to change its behavior, which also explained the outreach by Secretary Kerry and others throughout the course of the administration. Now of course, world events interrupted best laid plans. Russia's invasion of Ukraine changed the European's view of LNG imports.

As Mike Tyson said, what is it? Everyone has a plan until you get punched in the face? Well, there were multiple punches, and so we have to anticipate that kind of going forward. Perhaps the most bipartisan sensibility is the threat that China faces. We even have a special subcommittee or special select committee in the house focused on that, and as a result of that, I think that that's pushed certain provisions including in the Inflation Reduction Act with respect to the opposition or prohibition against U.S. taxpayer money going to foreign entities of concern. The Biden administration, their objective was to accelerate clean energy deployment to address climate change as quickly and cheaply as possible. So we saw this bit of a different interpretation of the black letter of the law to allow some, whether it's 25% up to 25% could come from or the permission to allow Chinese graphite to come into the U.S. market to be able to qualify for U.S. taxpayer subsidies through 2027.

You see this kind of trying to be focused on the security imperative, which has considerable bipartisan appeal as well as advancing climate change that'll play out in the technology space as well. I think the solar example is a good one in that is a cautionary tale. We had at one time,

America did have at one time an opportunity to build up solar industry, but we seeded that ground and now China is by far dominant, so can we do that in other technologies? I think the critical minerals question and creating domestic refining of those minerals as well as free trade countries and allies is going to be the next window of opportunity. We don't have a lot of time to achieve real inroads. China's already far ahead.

Quill Robinson: So the Trump administration is very cognizant of how big fossil fuels, how big their role still is in the global and the domestic energy system, and they're very eager to use the geopolitical and economic power of oil and natural gas and so on and so forth. Yet when it comes to these clean energy technologies, it's clear that they're playing a bigger role in the global energy system and the domestic energy system. Ilaria, I know you've spent a lot of time thinking about the electric vehicle sector, about batteries. In the last year or so, there's been controversy around a Chinese firm, CATL, launching this joint venture with Ford in Michigan. This question of joint ventures and foreign direct investment from China, from these companies in China that have great expertise on these technologies. I can see this becoming a flashpoint in the next administration. What should we be paying attention to when it comes to JVs and FDI and where Chinese companies might come in or will they be allowed to?

Ilaria Mazzocco: Well, so there's a variety of different ways in which Chinese companies and Chinese technology I would say is used by American companies or operates in the United States. You have fully owned factories, not as many of those, but then you do have some joint ventures, and then you have CTL is actually a licensing deal, so there's actually no Chinese ownership. Then there's strategic investments. There's a broad variety actually ways in which, and then there's obviously suppliers that may not even be in the United States that American companies rely on, and I think that's what in part I was pointing at in my initial remarks that the two countries are still highly interdependent and when you dig deep into a lot of value chains, there's still a lot of Chinese presence. There's two questions. One is, I think Frank pointed to this, is the actual sort of if there's incentives and subsidies and they go to at least part of that subsidy goes to a Chinese company, is that going to be okay or not?

I think probably likely. I think the most controversial side of things in a way that kind of goes away is some of these subsidies are removed. That issue is not quite as salient, but that also removes a pretty big tool in the hands of the government where you can actually direct which companies get what. And of course a lot of Chinese companies, they are in a position of advantage in terms of where they are with their technology and they may in some cases have more ability to invest

abroad because they have somewhat more flexible or ability to tap into state funds in China. The interesting thing with clean tech, and I think this is why it should be interesting to people that even people who don't care about climate is this is clearly the one area where China has a sort strategic advantage compared to United States in technology, and so the real dilemma is do we try and do it on our own without any sort of Chinese involvement or reliance on China, which is going to be much more costly. It's unclear that we'll get to the same sort of level as China, it's a catchup game, or do we figure out a way in which we can strategically leverage Chinese technology and at the same time limit the national security vulnerabilities that may emerge, and I think that the Biden administration really struggled with that. I think they went back and forth. I think there was also an image problem and CATL deal I think was very emblematic of that, and there's certainly a lot of people now going to be staffing the Trump administration who had a very negative view on this, right? Certainly Marco Rubio was very, I think, negative on the CATL deal, and there's been a lot of attacks on the Gotion factories. Actually, the factory, the Michigan one is the one that gets attacked. The Illinois one by all counts is up and running and doing all right, and apparently very popular with the local community, and ironically, the Michigan factory would be making the components that would allow the batteries they're being produced in Illinois to be made with components made in the United States rather than be imported from China.

So I think that points to the complexity of this, and I think this points to me to the challenge and whether you prioritize economic goals or national security goals, right? And if you want to prioritize economic goals, it makes complete sense to incentivize foreign direct investment technology transfer, whatever. You can structure it however you want, but it makes sense to leverage that even if it comes from a country that you might have a fraught, let's say, or a rivalry with it. But if it's a national security concern and certainly we do have national security concerns, then I think it becomes a lot more challenging.

Quill Robinson: So Ilaria, that's a really important insight on domestic situation here. I want to make sure that we get to the international energy landscape before we wrap here, and so Frank, the U.S. represents 11% of global greenhouse gas emissions. We're not going to solve this issue by ourselves. Obviously, China plays an important role with that, but of course energy technologies and building energy infrastructure is a really important form of soft power and influence. Where is China's comparative advantage and where is ours when it comes to enabling access to energy in the rest of the world?

Frank Fannon: China has integrated its investments internationally through of course, this marquee Belt and Road Initiative, which celebrated recently 10-year anniversary and had spent over a trillion dollars around the world, usually mostly in the southern hemisphere to link infrastructure and to advance their own economic interests. The way China invests is really tied to their own economic interests. It's really like in the mining space, it tends to be a shovel and ship kind of approach. Everything. Going back to the PRC, they tend to go into countries, they'll identify what their real end game is, and then they'll hide that fact and they'll go in and establish different things like building infrastructure, telling countries like in the case of Ecuador, to give their oil, which some of which was used for power generation and swap the oil for hydropower, which the Chinese will come and build, and then they do oftentimes do a poor job of that.

It certainly was the case of the Coca Codo dam and Ecuador, and now the country is kind of worse off as a result of that. Of course, that is the story in many African countries as well, where the mainstay of a U.S. company, we spent a lot of time here talking about the mobilization of domestic workforces, contribution and support of local communities, these kind of concepts. The Chinese tend not to operate that way. They tend to bring in their own workers and have their own camps of people. Local government will get some revenue from the project, but the people don't benefit as a result of that. Over this 10 year experiment of belt and road, they really are starting to get a lot of backlash in a lot of these countries. The U.S., by contrast, is investing in these countries. They're not doing it enough. We haven't mobilized our international financing in a way to really unlock the private industry. Of course, government in the west only does so much. It's really the private sector does the job, but the government can lay the foundation and mobilize capital to unlock private sector. We need more of that, not less of it. Now's the opportunity. The Belt and Road story is turning out to be a bit of a sad one for a lot of the countries.

Quill Robinson: Joseph, Frank, Ilaria, thank you so much for joining for this very important conversation. Thanks so much for joining us on the transition. We'll see you next episode.

(END.)