



**Statement before the House Committee on Foreign Affairs
Subcommittee on Asia and the Pacific**

***“U.S. ECONOMIC OPPORTUNITIES AND
CHALLENGES IN THE ASIA PACIFIC”***

A Statement by:

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Introduction

Mr. Chairman, Mr. Ranking Member, Members of the Subcommittee, thank you for this opportunity to offer my thoughts on U.S. economic opportunities and challenges in the Asia-Pacific region.

Economics is at the heart of American engagement in the Asia Pacific. Trade, investment, and other economic ties across the Pacific today are measured in the trillions of dollars and make an essential contribution to U.S. growth and jobs. No other region of the world presents as many opportunities and challenges for the U.S. economy—and for U.S. international economic policy.

Like administrations before it, the Obama Administration has put economics at the center of its Asia-Pacific strategy. Indeed, the overall success of the Administration's policy of "rebalancing" to Asia rests on its ability to carry out a successful economic strategy in the region, in particular completion of a high-standard Trans-Pacific Partnership (TPP) trade agreement.

Asia's Economic Gravity

The United States is drawn to the Asia Pacific by strong economic forces. In 2014, the 21 member economies of the Asia-Pacific Economic Cooperation (APEC) grouping, which includes the United States, accounted for 58 percent of global gross domestic product (GDP).¹ The region is home to the world's three largest economies by GDP – the United States, China, and Japan – and 8 of its 15 trillion-dollar economies. Moreover, the International Monetary Fund (IMF) projects that emerging and developing Asia will grow 6.4 percent in 2015, making it the world's fastest-growing region, as it has been consistently for nearly a decade.² By 2030, it is expected that Asia will be home to over three billion middle-class consumers, who will account for over 40 percent of global middle-class consumption.³

These trends will lead to increased international commerce in a region where trade is already substantial. Last year, more than \$10 trillion in goods and services flowed around the Pacific, and the APEC region accounted for 44 percent of total global trade.⁴ Six of America's top 10 trading partners are in APEC, and our exports to the grouping as a whole have more than doubled over the past decade. In 2013, APEC economies absorbed nearly 62 percent of total U.S. exports. As the region – and its middle class – continues to grow, this will lead to even greater

¹ White House Office of the Press Secretary, "Fact Sheet: 22nd Annual APEC Economic Leaders' Meeting," November 11, 2014, <http://www.whitehouse.gov/the-press-office/2014/11/11/fact-sheet-22nd-annual-apec-economic-leaders-meeting>. APEC is discussed further below as a centerpiece of U.S. regional economic strategy.

² International Monetary Fund, "January Update: Cross Currents," *World Economic Outlook*, January 2015, <https://www.imf.org/external/pubs/ft/weo/2015/update/01/>.

³ David Rohde, "The Swelling Middle," January, 2012, <http://www.reuters.com/middle-class-infographic>. This figure includes India, and other Asian economies not members of APEC.

⁴ White House Office of the Press Secretary, *op cit*.

demand for high-quality American goods and services, from our beef, pork, and soybeans, to our aircraft, software, and healthcare services.

We are also tied to the Asia Pacific through both direct and portfolio investment. The stock of U.S. direct investment in Asia on a historical-cost basis totaled almost \$700 billion at the end of 2013, having grown by an average of more than \$40 billion per year for the past half-decade.⁵ Over the same period, investment from Asia-Pacific countries into the United States rose by almost \$150 billion, adding to an accumulated stock that now totals more than \$450 billion.⁶ China and Japan each hold over \$1 trillion in U.S. Treasury securities,⁷ and Asians and Americans have trillions of dollars invested in each other's stock markets and other private financial instruments.

All of this economic activity across the Pacific means jobs at home. The International Trade Administration estimates that exports to Asia and the Pacific supported 3.2 million jobs across the United States in 2013, the largest share of any single region.⁸ That same year, Asian companies invested in the United States directly employed nearly one million Americans, with many more jobs supported indirectly by these operations.⁹

In addition to the opportunities, we also face major policy challenges in our economic engagement with Asia. The United States continues to run large and persistent trade deficits with many Asian economies, including a \$327 billion trade deficit with China in 2013.¹⁰ While tariffs across the region have been lowered by an average of 10 percent since APEC's founding in 1989, American companies continue to face an array of barriers and unfair trade practices both at and behind the border in many Asian countries, from regulatory impediments to theft of intellectual property. Meanwhile, excess savings in many Asian economies, while supporting American consumption and the ability of the Federal government to borrow at low rates in the near term, contribute to macroeconomic imbalances that can be destabilizing over time. Currency manipulation by some countries in the region has exacerbated this problem.

⁵ Bureau of Economic Analysis, "Balance of Payments and Direct Investment Position Data," U.S. Department of Commerce, http://www.bea.gov/iTable/index_MNC.cfm.

⁶ *Ibid.*

⁷ U.S. Department of the Treasury, "Major Foreign Holders of Treasury Securities," January 2015, <http://www.treasury.gov/resource-center/data-chart-center/tic/Documents/mfh.txt>.

⁸ Chris Rasmussen and Elizabeth Schaefer, "Jobs Supported by Export Destination 2013," International Trade Administration, U.S. Department of Commerce, July 7, 2014, http://www.trade.gov/mas/ian/build/groups/public/@tg_ian/documents/webcontent/tg_ian_005372.pdf.

⁹ Organization for International Investment, "Insourcing Facts," August 2012, <http://www.ofii.org/resources/insourcing-facts>. Estimate based on Asia's share of overall U.S. inbound FDI.

¹⁰ Bureau of Economic Analysis, "International Transactions, International Services, and International Investment Position (IIP) Tables," U.S. Department of Commerce, http://www.bea.gov/iTable/index_ita.cfm.

Addressing these challenges and maximizing the economic opportunities that the Asia Pacific presents require a robust U.S. economic diplomacy in the region.

U.S. Economic Strategy in the Asia Pacific

The United States is a Pacific power, and economics has been intertwined with our diplomatic and security engagement in the region since the dawn of the republic. The first U.S. merchant ship set sail from New York bound for Canton in 1784, bearing ginseng, cotton, and lead to trade for Chinese tea, tableware, silk, and spice; it also carried the first U.S. consul to be stationed in China. In 1853, Commodore Matthew Perry arrived in Tokyo Bay in his “black ships” seeking open trade with Japan and refueling rights for the American whaling fleet.

Since the end of World War II, economics has played a vital role in underpinning the network of U.S. security alliances in the Asia Pacific. As the Cold War deepened, the United States first supported the revival of the Japanese, Korean, and Taiwanese economies as part of its efforts to develop durable bulwarks against the spread of communism. In 1972, the Nixon Administration engineered a dramatic opening to China, creating the opportunity for an explosive increase in economic engagement when the world’s most populous country entered its period of “reform and opening” later that decade. The broad contours of this strategy of engagement have been upheld by every Republican and Democratic administration since.

Beginning in the late 1980s, bilateral economic engagement in the Asia Pacific has been complemented by efforts to promote regional economic integration. The APEC forum has been the organizing principle for these efforts. President George H.W. Bush’s Secretary of State James Baker embraced an Australian proposal to create APEC in 1989 as a venue for foreign ministers from around the region to discuss trade and investment liberalization and capacity-building. The underlying logic of APEC was to channel the aspirations of East Asian countries for regional economic integration into a trans-Pacific framework that included the United States (as well as other Pacific-facing nations such as Canada, Mexico, Peru, and Chile). President Bill Clinton invited his APEC counterparts to a summit on Blake Island off Seattle in 1993, lending top-level political support to APEC’s mission of regional economic integration.

APEC has also been at the heart of the Obama Administration’s strategy of “rebalancing” to Asia. The rebalance has military, diplomatic, economic, and people-to-people components, each of which underpins and enhances the other elements. As discussed further below, the economic dimension of the rebalance centers on negotiation of a TPP trade agreement among a subset of APEC economies.

Over successive administrations, U.S. economic strategy in the Asia Pacific has been guided by three broad objectives. The first is growth and jobs. As discussed above, the Asia Pacific is the world’s largest and fastest-growing economic area. Stronger demand and rising purchasing power in Asia means more opportunities for U.S. exporters, which translates into growth and jobs at home.

The second objective is upholding and updating the rules of the international economic order. Since World War II, Washington has championed an open, rules-based system of trade and investment, which has yielded enormous benefits for the United States and the rest of the world. However, the rules have grown increasingly out of step with the realities of today's global economy. They reflect a 19th century model of arms-length trade in goods, rather than 21st century phenomena such as e-commerce and integrated value chains. TPP is designed to address this gap by establishing updated rules governing not only tariffs and other border measures but also behind-the-border issues such as the market behavior of state-owned enterprises, regulatory transparency, labor and environmental standards, and intellectual property protection.

The third enduring objective of U.S. economic strategy in the Asia Pacific is supporting America's long-term presence in the region. The United States is a Pacific power but not an Asian nation. Thus successive administrations have worked to embed the United States in the region through a host of political, security, and economic arrangements, while opposing efforts that would "draw a line down the middle of the Pacific," in the words of former Secretary of State Baker. U.S. alliances with Japan, South Korea, Australia, and others, as well as the American troops and ships deployed across the region, are the most visible manifestation of this policy. Binding trade arrangements such as the U.S.-Korea free trade agreement (KORUS FTA) and TPP provide a crucial economic equivalent. They enmesh the United States in regional affairs, give Asia-Pacific countries an increased stake in each other's prosperity and security, and help reassure our allies and potential adversaries of Washington's continued commitment to robust engagement with the region.

A New Reality in Asia

The Obama Administration's rebalancing strategy is partly motivated by what is undoubtedly the single greatest trend shaping regional – and global – economic dynamics: China's rise. At the start of the 21st century, the Chinese economy was only one-quarter the size of the Japanese economy, and roughly one-ninth the size of the U.S. economy. Today, China is the world's second-largest economy, having passed Japan in 2010, and on current trends, it could reemerge as the largest economy in nominal terms as soon as 2021.¹¹ The rapidity of China's ascent, its latent potential as the world's most populous nation, and its ambitions to resume its historical position as the "Middle Kingdom" at the heart of Asia are challenging the established regional economic order.

To date Beijing has largely been a rule taker within the international economic order. It joined the World Trade Organization (WTO) in 2001, played a constructive role in the G20 during the early days of the global financial crisis, and has become deeply integrated within regional and global value chains. It supported a U.S. initiative in APEC in 2011 to lower member economies' tariffs on

¹¹ "Catching the eagle," *The Economist*, August 22, 2014, <http://www.economist.com/blogs/graphicdetail/2014/08/chinese-and-american-gdp-forecasts>.

environmental goods and services. During its own host year in 2014, Beijing put forward an ambitious agenda for advancing trans-Pacific regional economic integration by pushing for faster progress towards a Free Trade Area of the Asia-Pacific (FTAAP)—another U.S.-proposed initiative. And, despite initially rejecting TPP as an effort by Washington to “contain” China, Beijing has shifted in recent years toward seeking a better understanding of the initiative. Through negotiations with the United States over a high-standard bilateral investment treaty (BIT), Beijing has even shown its own interest in preparing the ground for eventual participation in a high-standard trade agreement.

At the same time, China has been selective in its compliance with international economic rules and norms. It has failed to honor the spirit of many of its WTO commitments and continues to restrict the activities of U.S. companies in key sectors of American comparative advantage. Through an array of subsidies, regulatory barriers, and the uneven application of domestic laws, China has given preferential treatment to its firms over U.S. companies operating within its market – particularly in sectors it deems of strategic importance, such as high technology.¹² Lack of intellectual property protection, including cyber-theft of U.S. trade secrets, has been a persistent problem for American interests.

Moreover, under the Xi Jinping administration, Beijing is clearly seeking a greater voice in setting international rules and standards and imbuing them with “Chinese characteristics.” To an extent, this is understandable: historically, China was at the center of the Asian economic order. Moreover, it is true that Beijing is underrepresented in many existing institutions of global economic governance. Its voting share in the IMF, for example, is roughly equivalent to the combined share of Belgium and the Netherlands – despite having an economy seven times their combined size.

But Beijing’s growing assertiveness in international economic rule-making comes with certain risks. For example, through the Regional Comprehensive Economic Partnership (RCEP), an alternative trade arrangement to TPP bringing together 16 Asian countries, Beijing is advancing a lower-standards model of regional economic integration that could put American commercial interests at a disadvantage when competing in the region. Meanwhile, Beijing has championed new initiatives such as the Asian Infrastructure Investment Bank (AIIB) and the Silk Road Fund, in an effort to establish its centrality in the region’s institutional architecture. These new institutions could weaken established rules and norms for best practices in development assistance – such as environmentally sound lending standards and protection of vulnerable populations – that the existing Bretton Woods institutions have developed over many decades.

¹² For one discussion of these issues, see Usha C. V. Haley and George T. Haley, *Subsidies to Chinese Industry: State Capitalism, Business Strategy, and Trade Policy*, Oxford University Press, April 25, 2013.

China's new position, policies, and ambitions in the Asia Pacific have raised the stakes for the United States to pursue a robust economic agenda in the region. This includes engaging with China directly to cooperate on issues of mutual concern, manage competition where necessary, and advance the full range of American interests in the region. It also means working with America's regional allies and partners to strengthen the rules-based order – including through initiatives like TPP – and to offer Beijing “carrots” to encourage constructive engagement and integration into the established order, and “sticks” to discourage zero-sum economic behavior.

The Trans-Pacific Partnership

As mentioned earlier, TPP is the centerpiece of the Obama Administration's rebalancing strategy to Asia. U.S. involvement in TPP dates to the waning days of the Bush Administration in late 2008, when the White House notified Congress of its intention to negotiate a trade agreement with four small APEC economies – Brunei, Chile, New Zealand, and Singapore. The Obama Administration formally embraced TPP in late 2009. Australia, Peru, and Vietnam joined the effort shortly thereafter, and negotiations among the eight original member countries began in March 2010. The initiative has since attracted four additional members: Malaysia later in 2010; Canada and Mexico in 2012; and Japan in the summer of 2013. Together the 12 TPP negotiating partners represent a combined 40 percent of the global economy by GDP and almost one-third of world exports.

TPP serves all three enduring objectives of U.S. economic strategy in Asia. First, it holds the promise of substantial economic gains. The Peterson Institute for International Economics has estimated \$223.4 billion in annual global welfare gains from a concluded TPP in 2025, including \$76.6 billion in GDP gains for the United States and a \$123.5 billion increase in U.S. exports relative to the baseline scenario.¹³

Second, a completed TPP agreement would update the rules of regional trade. As President Obama said in announcing his support for the initiative, TPP is designed to produce “the high standards worthy of a 21st-century trade agreement.”¹⁴ In addition to lowering border barriers, a successful TPP will establish an array of behind-the-border rules to facilitate regional trade and investment, including disciplines on state-owned enterprises, high labor and environment standards, strengthened intellectual property protections, and more transparent regulation. Moreover, TPP's open architecture will allow it to

¹³ From Peter A. Petri, Michael G. Plummer, Fan Zhai, *The Trans-Pacific Partnership and Asia-Pacific Integration: A Quantitative Assessment*, Peterson Institute for International Economics and East-West Center, Updated May, 2013, <http://asiapacifictrade.org/wp-content/uploads/2013/05/Adding-Japan-and-Korea-to-TPP.pdf>.

¹⁴ White House, “Remarks by President Barack Obama at Suntory Hall,” news release, November 14, 2009, www.whitehouse.gov/the-press-office/remarks-president-barack-obama-suntory-hall

incorporate new members after its conclusion, strengthening its potential as a driver and *de facto* template for a new multilateral system of rules.

A new high-standard regime would have positive effects for U.S. economic and commercial interests, positive spillover effects for our allies and partners in the region, and create new incentives for countries to seek to upgrade their own standards. This includes China, which, as an APEC member, is theoretically eligible for eventual TPP participation. However, the standards of the agreement, such as the aforementioned disciplines on state-owned enterprises, are designed to ensure that if China were to join TPP, it would have to offer strong and enforceable guarantees of a fair and level playing field in its domestic market.

Third, TPP would embed the United States more deeply in the Asia-Pacific region and reinvigorate American leadership there. It would strengthen trade and investment ties across the Pacific and deepen regional economic integration. It would also demonstrate a long-term American commitment to the region that complements our security presence there. Our Asian partners want the U.S. military to remain as a source of stability in the region, but they do not want only that; they also seek our markets, capital, ideas, and leadership in championing the economic rules of the road.

By all accounts, TPP is entering the endgame. The United States and Japan are reportedly close to agreement on a bilateral market-access deal that is widely considered a precondition to a broader deal among the 12 parties. TPP chief negotiators will meet early next month in an effort to prepare the ground for a potentially decisive meeting of TPP ministers in mid-April. There is now an emerging consensus among trade analysts that a final TPP deal can be completed and brought to Congress for a vote before the end of this year.

The stakes could not be higher for the Obama Administration. Conclusion of TPP is the *sine qua non* of success not only for the Administration's regional economic policy but arguably for the entire Asia rebalancing strategy, insofar as it is a necessary complement to the U.S. security and diplomatic presence in the region.

Conclusion

America's interests in the Asia Pacific are broad, deep, and enduring. None is more important than our economic stake in the region. As former Secretary of State Hillary Clinton explained in laying out the rationale for the rebalancing strategy in 2011, "Harnessing Asia's growth and dynamism is central to American economic and strategic interests and a key priority for President Obama. Open markets in Asia provide the United States with unprecedented opportunities for investment, trade, and access to cutting-edge technology. Our economic recovery at home will depend

on exports and the ability of American firms to tap into the vast and growing consumer base of Asia.”¹⁵

A successful economic strategy in the Asia Pacific is essential to sustaining American growth and jobs into the 21st century. It is also central to Washington’s efforts to remain a champion of the global rules-based order. And it underpins America’s long-term presence in the region, which in turn contributes importantly to the region’s security and prosperity.

Thank you for your attention.

¹⁵ Hillary Clinton, “America’s Pacific Century,” *Foreign Policy*, October 11, 2011, <http://foreignpolicy.com/2011/10/11/americas-pacific-century>.