

FREEMAN REPORT

December 2008

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Quote Of The Month

"We hope the U.S. can take all necessary measures to stabilize its financial markets and economy as soon as possible and ensure the safety of China's assets and investments in the U.S." ~ Chinese Vice Premier, **Wang Qishan**, speaking at the U.S.-China Strategic Economic Dialogue meetings in Beijing. The fifth round of the economic talks was dominated by the global crisis. Vice Premier Wang's comments came as U.S. Treasury Secretary Henry Paulson praised China's "responsible role" in combating the crisis. He further commented, *"To work together to tackle the financial crisis is the most pressing task that we are facing."*

Source: Bloomberg, December 18, 2008

Trivia Question

How many Chinese students are studying in U.S. universities? (cont pg 3)

The Freeman Report provides an open forum for individual opinions and commentaries on China. All opinions expressed in the feature essay of the report are those of the author.

FEATURE ESSAY

Heeding the Lessons of Failure

BY CHARLES W. FREEMAN III

"We must learn to do economic work from all who know how, no matter who they are. We must esteem them as teachers, learning from them respectfully and conscientiously. We must not pretend to know when we do not know." -- Chairman Mao Zedong, June 30, 1949

China's reaction to the current economic crisis has been an odyssey of emotion, from denial to shock to anger to resolve. An early smug triumphalism among many Chinese at America's big stumble gave way quickly to anxiety about its impact on China; then to anger at those responsible in the United States for bringing about the global collapse; and now, increasingly, to grim acceptance marked by a certain gallows humor.

These emotions all remain to varying degrees among Chinese officials and many in the general public, as does a distinct intention to overcome the current difficulties. What seems to have been ripped from the Chinese psyche by the crisis is an acceptance of the American model's financial and economic superiority. To paraphrase China's Vice Premier Wang Qishan's pointed comments to his counterpart, Treasury Secretary Hank Paulson, at the July meeting of the U.S.-China Strategic Economic Dialogue, "We've been listening to you as your students and now we find out our teacher has problems."

Vice Premier Wang's observation was far from inapt. For many years, official American interaction with Chinese counterparts has been marked by a tendency to lecture. Official U.S. talking points, diligently prepared in close consultation with representatives of (cont pg 2)

In The News

BEIJING French President Nicolas Sarkozy's recent meeting with the Dalai Lama at a gathering of Nobel Peace Prize winners in Poland has infuriated Beijing. In protest against the meeting, Chinese government canceled an E.U.-China summit, which France was to host. China has also warned bilateral trade ties could be damaged, but so far there have been no reports of canceled contracts. Relations between China and France remain to be strained. Sarkozy's meeting has reportedly sparked widespread nationalist sentiment in China. Despite Beijing's stern denunciation of the meeting, the Chinese authorities seem keen to keep the nationalist sentiment as low key as is political feasible, given China's trade surplus with France.

BEIJING Chinese authorities are likely to face a tough task of maintaining social stability amid the global downturn. Faltering economic conditions have raised the specter of China's growth falling below 8 percent, which the government regards as a benchmark to create enough jobs and ensure social stability. With labor strikes and small-scale protests already cropping up across the country, Beijing has become increasingly concerned about a potential massive social turmoil caused by rising unemployment and the economic slowdown.

U.S. interest groups and distilled through a vigorous interagency process, are tutorials in the inviolability of the American Way of Doing Things. How to best secure the human rights of one's own people, how to manage one's agricultural and industrial trade regimes, and yes, even how to build a sound and efficient financial system.

China has never appreciated the meddlesome style of U.S. engagement. To one extent, the primary lesson Chinese officials have drawn from these lectures has been to arm themselves with an equally forceful set of talking points of their own. Yet China has always come back to the classroom that has been the official U.S.-Chinese relationship because, by and large, the benefits of showing up for the lectures have always outweighed the pain. China's economic rise has been occasioned by China's commitment to engage with, learn the lessons from, build stakes in and increasingly conform to the U.S.-led economic order.

That order has been good to China over the years. Small wonder that, as China's economic reforms have progressed, Chinese policymakers have drawn liberally – if selectively – from American economic models. While Chinese reformers have always attempted to refine such policy tools to the unique Chinese context, they have frequently begun their efforts with a presumption that the ultimate adoption of the economic norms and policies of the order's leader was at least a desirable long-term goal.

One of Hank Paulson's priorities during the Strategic Economic Dialogue over the past few years has been to push China toward greater financial liberalization. Paulson, a veteran of China deal-making from his time at Goldman Sachs, was careful to moderate the lecturing tone of his talking points, presenting them as respectful advice from someone more experienced, but not necessarily superior. More teachers' aide than teacher, perhaps. Under his watch, China did indeed move slowly but inexorably down the path to financial reform, making cautious moves to reform its exchange rate policy and easing the ability of financial institutions to play more broadly in China's and international capital markets. Following the crisis, the wisdom of these moves, and the quality of the advice that preceded them, is now coming squarely into question.

Proclaiming China's development model to be an alternative to that of the United States – the so-called *Beijing Consensus* – has become fashionable over the years. Yet while China has certainly never embraced the *Washington Consensus*, it has been content to pursue its own development goals within the framework of the U.S.-led economic order and under the security afforded by American leadership in the Pacific. And while China has been selective in adopting the precepts of the *Washington Consensus* for its own purposes and to fit its own goals, it has rarely challenged the fundamental efficacy of those precepts. In the wake of the current crisis, and particularly as Washington continues its spree of government intervention in banks, markets and enterprises in an effort to stem the economic decline, the *Washington Consensus* is looking increasingly fragile. China's tacit recognition of the advanced nature of U.S. economic norms is, if not already wiped away, therefore certainly in jeopardy.

On a recent trip to Beijing, a casual acquaintance asked me whether Americans felt bad that our crisis had wreaked such global havoc. "Things are bad everywhere, aren't they? A whole country, Iceland, went broke. Completely bust! A whole country!" he said, suddenly hysterical and then just as suddenly serious: "China isn't Iceland, you know. You can't bring us down that easily."

Given the extent to which China has stakes in the sanctity of the American-led order, one might imagine that China's economic leaders, in the wake of this great failure of the American financial model, might be feeling slightly rudderless. I doubt it. Anxious yes, at the challenges that lie ahead; disenchanting by the advice of their American "teachers"; and concerned about the value of their stake in the international architecture that has conditioned their economic rise. But there is also a palpable and increasing sense among Chinese policymakers that disillusionment with American economic models is not such a terrible thing for China's own international self-confidence.

American interaction with China therefore just became a lot more complex. Many important U.S. values, norms and policy prescriptions that are the leading edge of the U.S. agenda with China and that will be the subject of our engagement during the Obama administration and beyond have lost the benefit of the doubt with our Chinese interlocutors.

Robert Zoellick, now the President of the World Bank, famously urged China in 2005 to be a "responsible stakeholder" in global affairs. Given the blows dealt to the architecture of global affairs by the current crisis, Chinese leaders must be asking themselves now: "responsible stakeholder in what, exactly?" Their response will almost certainly be to seek a more active role in defining that architecture going forward, and be more skeptical of U.S. prescriptions in the process.

Charles W. Freeman III holds the Freeman Chair in China Studies at CSIS.

Publications

“Crafting U.S. Economic Strategy toward Asia: Lessons Learned from 30 Years of Experience,” CSIS Asia Economic Task Force Report, October 2008

By **Charles W. Freeman III**, Chairholder, CSIS Freeman Chair in China Studies, and **Matthew Goodman**, Managing Director, Stonebridge International

Among the many pressing realities that will confront a new U.S. Administration in January 2009 – whether Republican or Democratic – will be the need to manage the challenges and opportunities of a rising Asia. Drawing on the experience of a bipartisan group of former U.S. government officials and other experts who, among them, have been involved in all of the major Asian economic policy initiatives of the past three decades, a CSIS task force has produced a new report reviewing the most important lessons learned from that experience, in an effort to provide the new Administration with a practical “user’s guide” to managing U.S. economic relations with Asia.

China’s Rise: Challenges and Opportunities, Peterson Institute for International Economics and CSIS, (Washington, DC: September 2008)

By **C. Fred Bergsten**, **Charles W. Freeman III**, **Nicholas R. Lardy**, and **Derek J. Mitchell**

This book examines key aspects of China’s global role and U.S.-China relations, and is the publication of the China Balance Sheet project which has been conducted by the Peterson Institute and CSIS over the last three years. Our initial product, *China the Balance Sheet: What the World Needs to Know Now About the Emerging Superpower* was released in 2006. The new volume identifies the most important future areas of challenges and potential cooperation in U.S.-China relations.

Conferences & Events

December 9 *What About China? The High-Stakes Race to Shape the Next World Order*

This event is part of the CSIS Speaker Series focusing on U.S.-China relations. MPAA Chairman and CEO **Dan Glickman** delivered a keynote address on the fresh opportunity a new administration presents to open the next chapter in the U.S.-China relationship, one of mutual benefit to our two nations and the broader global information economy. Glickman specifically addressed trade issues and the increasingly shared stake in shoring up the intellectual property underpinnings of the modern global information economy. As a former Cabinet member in the Clinton Administration who supported China’s accession to the World Trade Organization, Glickman shared his perspective on the future of one of the most important diplomatic relationships of our nation in the 21st century. **Steven Schrage**, CSIS Scholl Chair in International Business, chaired the event.

November 19 *CSIS Press Briefing on APEC Summit*

CSIS hosted a press briefing on the Asia Pacific Economic Cooperation (APEC) summit. The briefing featured **Charles Freeman**, CSIS Freeman Chair in China Studies, **Sidney Weintraub**, CSIS Simon Chair in Political Economy, and **Steven Schrage**, CSIS Scholl Chair in International Business.

TRIVIA ANSWER

There are 624,000 Chinese students currently enrolled in U.S. universities. With an increase of 20 percent in 2007, enrollment of Chinese students has now reached its highest level ever, driven by aggressive recruiting, as well as a booming economy and a growing middle class in China.

Source: “China students head to U.S.,” *Associated Press*, November 17, 2008

PUBLICATIONS FROM THE FREEMAN CHAIR 2007/2008*

* Please visit our website to access archived publications dating back to 2002.

2008

October

"*Crafting U.S. Economic Strategy toward Asia: Lessons Learned from 30 Years of Experience*," CSIS Asia Economic Task Force Report, October 2008

By **Charles W. Freeman III**, Chairholder, CSIS Freeman Chair in China Studies, and **Matthew Goodman**, Managing Director, Stonebridge International

September

China's Rise: Challenges and Opportunities, Peterson Institute for International Economics and CSIS (Washington, DC: September 2008)

By **C. Fred Bergsten**, Director, Peterson Institute for International Economics, **Charles W. Freeman III**, Chairholder, Freeman Chair in China Studies, CSIS, **Nicholas R. Lardy**, Senior Fellow, Peterson Institute for International Economics, and **Derek J. Mitchell**, Senior Fellow for Asia, International Security Program, CSIS.

June

"*Assessing Chinese Government Response to the Challenge of Environment and Health*," CSIS, June 2008

By **Charles Freeman**, Chairholder, Freeman Chair in China Studies, CSIS, and **Xiaoqing Lu**, Research Associate, Freeman Chair in China Studies, CSIS

La Democrazia Gestita [Managed Democracy], *Aspenia*, No. 41, 2008, Aspen Institute Italia

By **Melissa Murphy** (contributing author), Research Associate, Freeman Chair in China Studies, CSIS

May

"*China-Europe Relations: Implications and Policy Responses for the United States*," CSIS, May 2008

By **Bates Gill**, Director, Stockholm International Peace Research Institute (SIPRI), and **Melissa Murphy**, Research Associate, Freeman Chair in China Studies, CSIS

February

Foresight: 2008, Exclusive Analysis Limited, London: 2007

By **Melissa Murphy** (Contributing Author), Research Associate, Freeman Chair in China Studies, CSIS

"Assessing China's Response to the Challenge of Environmental Health," *China Environment Series 9*, China Environment Forum, Woodrow Wilson International Center for Scholars, 2007

By **Xiaoqing Lu**, Research Associate, Freeman Chair in China Studies, CSIS, and **Bates Gill**, Director, Stockholm International Peace Research Institute

January

"Trade with China: The E.U. Speaks with an American Accent," *Atlantic Outlook*, vol. 2, no. 1, CSIS, January 29, 2008

By **Charles Freeman**, Freeman Chair in China Studies, CSIS

"*Critical Questions: China's Economy and the Subprime Crisis*," CSIS, January 29, 2008

By **Charles Freeman**, Freeman Chair in China Studies, CSIS

"*Decoding Chinese Politics: Intellectual Debates and Why They Matter*," CSIS, January 2008

By **Melissa Murphy**, Freeman Chair in China Studies, CSIS

2007

November

"*China: An Olympic Hangover?*," Global Forecast: The Top Security Challenges of 2008, CSIS, November 2007

By **Charles Freeman**, Freeman Chair in China Studies, CSIS

"*China's Civil Society Organizations: What Future in the Health Sector?*," CSIS, November 2007

By **Bates Gill**, Director, Stockholm International Peace Research Institute, **J. Stephen Morrison**, Director, Africa Program, CSIS, and **Xiaoqing Lu**, Research Associate, Freeman Chair in China Studies, CSIS

The China Report 2008

Melissa Murphy (contributing author), Exclusive Analysis Limited, London: 2007

FREEMAN FACTS:

China's 30 Years of Reform and Opening-up

1. From 1978 to 2007, China's GDP grew at an average rate of 9.8%, far higher than the 3% average annual world growth rate over the past three decades.
2. Chinese per capita income had risen to USD 2,360 in 2007, from USD 190 in 1978. China has moved from a low-income country to a lower-middle income country.
3. China's total import and export value soared to USD 2.17 trillion in 2007 from USD 20.6 billion in 1978, an increase of 104 times in three decades.
4. China has retained the third place in world trade since 2004. It ranked the 32nd at the beginning of the reform and opening-up policy.
5. China's foreign exchange reserves grew from USD 167 million in 1978 to USD 1.5 trillion in 2007.

Sources: Beijing Review, China National Bureau of Statistics

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Center for Strategic and International Studies 2007

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About the FREEMAN CHAIR IN CHINA STUDIES

The *Freeman Chair in China Studies* was established at the Center for Strategic and International Studies in 1994 to advance the study of China and to promote understanding between the United States and the countries of the Asia Pacific region. The Freeman Family—Luther Freeman as a clergyman, Mansfield Freeman as a scholar-business leader, and Houghton Freeman as a corporate executive in a global enterprise—have established a tradition of contributing to international understanding through practical experience in East Asia and China.

The United States has a long-standing relationship with China and the countries of East Asia, which play increasingly important roles in future international economics, politics, culture, and security. In the diplomatic, public policy, business, and government fields, the peoples of both China and the United States will benefit from greater mutual appreciation and understanding through broadly based international exchange.

The Freeman Chair's active policy-oriented agenda is dedicated to delivering informed public policy debates, expert briefings, and strategic policy recommendations on Greater China and East Asia to the diplomatic, policymaking, business, and government arenas.

Current Research Projects

- China's domestic challenges and their consequences for U.S.-China relations and U.S. strategic interests
- The emergence of Chinese civil society and nongovernmental organizations
- China's HIV/AIDS crisis and its implications for U.S.-China relations
- Examining the economic, trade, and financial tensions in U.S.-China relations
- China's relations with key regions—including Central Asia, Europe, and Africa—and their implications for the United States
- China's military modernization and its impact on regional security
- U.S-China-Taiwan relations

To learn more about our program and ongoing research projects, please visit our website at <http://www.csis.org/china/>