

## **Shanghai Forum, Fudan University, Shanghai, China**

Reuban Jeffery III

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Thank you to Fudan University for hosting this gathering. It is a great honor to be here, and to be representing both Yale University and the Center for Strategic & International Studies.

The Yale-China relationship is part of the broader educational partnership between the United States and China. More than 11,000 American students are studying in China. And there are more than 81,000 Chinese students in the United States, and the second highest representation of any country. These educational opportunities enrich the fabric of both countries, helping to break down cultural barriers while promoting mutual understanding and contributing to economic integration.

I am here today both in my capacity as a graduate of Yale, and as a Senior Advisor at the Center for Strategic and International Studies, a research organization based in Washington, DC that provides strategic insights and policy solutions to decision makers in government, international institutions, the private sector, and civil society.

Prior to joining CSIS, I served as Under Secretary of State for Economic, Energy and Agricultural Affairs, as well Chairman of the Commodity Futures Trading Commission. Having concluded my government service in January, this is my first opportunity to speak in public as a private citizen. I always enjoyed the privilege of speaking for the U.S. government and being involved in the diplomatic and economic policymaking process. But anyone who has served in government will know that there is some relief in being freed from some of the constraints of public office.

I know there's great interest throughout the world, and right here in China, in the Obama Administration's many policy initiatives. I think it would be premature at this stage to offer a running commentary on how the Administration is performing, so instead I'd like to explore some of the dynamics of the U.S.-China economic relationship. It is one of the most important bilateral relationships in the world – offering extraordinary benefits to both sides.

I will also touch on the global financial crisis and explore how China and the United States have cooperated to help mitigate what has become a global economic slowdown of unprecedented historic proportions.

And I will close with some suggestions for principles that might guide the U.S.-China relationship in years to come and help ensure that it remains a foundation for growth and security in both countries.

## **Bilateral Economic Relationship**

Let me start with some basic statistics that will help to illuminate the deep economic relationship between the United States and China.

- Total two-way trade between China and the United States was more than \$386 billion in 2007. In 1992, it was just \$33 billion.
- The United States is now China's second-largest trading partner, and China is now the third-largest trading partner for the United States, after Canada and Mexico.
- Over the past decade, the value of U.S. exports to China have grown six times as fast as our exports to the rest of the world – increasing 21% in 2005, 32% in 2006, and 18% in 2007. These exports totaled \$65.2 billion in 2007 – up from \$19 billion when China joined the World Trade Organization in 2001.
- Cumulative U.S. investment in China is estimated at \$57 billion, through the end of 2007, making the United States the sixth-largest foreign investor in China.

Here's my favorite statistic of all -- there are more than 800 McDonald's restaurants in China, and they sell over one million hamburgers a day.

This relationship benefits our two countries, while also contributing to global economic growth. In 2007, the United States and China together generated more than 30 percent of worldwide gross domestic product.

This deepening of our economic relationship both reflects the long record of economic expansion in both countries, and is contributing to that expansion. The deepening is also a tribute to the determination of China and the United States to liberalize trade and investment.

I won't try to speak for the Chinese, but the U.S. approach to its economic relationship with China has three main elements:

First, the United States seeks to fully integrate China into the global, rules-based economic and trading system. The Bush Administration believed, and I'm sure the Obama Administration does as well, that China's participation in the global economy will nurture the process of domestic economic reform, encourage China to take on responsibilities commensurate with its growing influence, and increase China's stake in the stability and prosperity of East Asia and the rest of the world.

Second, the United States seeks to expand U.S. exporters' and investors' access to the Chinese market. As China grows and develops, its needs for imported goods and services will grow even more rapidly. I expect the U.S. Government will continue to work with China's leadership to ensure full and timely conformity with China's commitments to the rules-based trading system – including effective protection of intellectual property rights – and to encourage China to move to a more flexible, market-based exchange rate adjustment mechanism.

Third, the U.S. strongly supports China's full integration in the financial market governance architecture, through responsible membership and active involvement in the International Monetary Fund, the World Bank, the G20, the Financial Stability Board, and other multilateral forums.

The flowering of our economic relationship has also built a level of trust that has strengthened our relations in other areas. I'm confident this cooperation will continue in the Obama Administration. The naming of Secretary Geithner and Secretary Clinton as the Special Representatives to the U.S.-China Strategic and Economic Dialogue indicates that the bilateral relationship will be a top priority at the highest levels of the U.S. government.

### **Financial Crisis in the United States**

I'd like to turn to the global financial crisis. Let me start by giving you some recent indicators from the United States:

- Last year, the wealth of American families plunged nearly 18%.
- Today, U.S. unemployment is at a 25-year high -- 8.9%.
- And recent U.S. GDP figures showed the biggest six-month decline since 1958.
- Much of this turmoil has been reflected in the equity markets.
  - The first quarter of 2009 was the Dow's worst first quarter, in percentage terms, since 1939.
  - By early March, stocks had lost \$11 trillion in market value since the October 2007 peak.
- Set against this bad news has been just a bit of good news.
  - Between the beginning of March and first week of April, the Dow rose 22% -- its best five-week performance since 1938.

So what went wrong?

The truth is that there were many factors contributing to the turmoil. One succinct set of explanations is contained in a report issued a few months ago by the Chairman of Britain's Financial Services Authority. Known as the Turner Review, the report suggests that the financial crisis was the result of the interplay between three factors: first, the increasing macro-imbalances during a period of sustained global growth and low inflation; second, the rapid financial innovation and market development – specifically the expansion in scale and complexity of securitized credit markets and the rising importance of non-bank entities in performing banking functions; and third, the capital buffers that failed to moderate an unsustainable credit boom and asset price inflation, and also failed to prevent a self-reinforcing cycle of deleveraging, falling asset prices, and collapsing liquidity.

Throughout the crisis period, the U.S. Treasury, the Federal Reserve, and other parts of the U.S. government have been extremely aggressive in responding to the turmoil, and trying to curtail it. By one recent estimate, the U.S. government has spent, or pledged, nearly \$13 trillion to resuscitate the financial sector.

I'll resist the temptation to predict where the economy and the equity markets are going, keeping in mind Warren Buffett's admonition that forecasts of the future usually tell you more about the forecaster than the future. But it's safe to say that the picture is mixed. The Federal Reserve Chairman, Ben Bernanke, has pointed to signs of "green shoots" in the financial markets, and said just last week that, the pace of economic contraction may be slowing, and that there are "some tentative signs that final demand, especially demand by households, may be stabilizing." He added, however, "we are likely to see further sizable job losses and increased unemployment in coming months."

### **China and the Financial Crisis**

I know that the picture is mixed in China as well. As the head of the central bank said last month, "The Chinese economy has shown signs of recovery on the whole, but we are still in a tough fight with the global financial crisis."

Goldman Sachs recently cited three reasons for optimism about the Chinese economy. The first factor is the \$586 billion stimulus package, which conveyed the government's strong determination to confront the economic turmoil. The second factor is the government's announcement that it planned to implement a comprehensive health insurance policy for rural China by 2011, which would cover 90 percent of the population. This would help to discourage excess savings and promote consumption. The third factor is the central bank's loosening of monetary policy.

I can say, as an outside observer, that China's response to the financial turmoil has been forthright – demonstrating a seriousness of purpose and a recognition of the

consequences for the country, the region, and the world of standing still. And I know from my time in government that my colleagues and I were impressed with the speed and scale with which the government took action.

### **Silver Lining**

Economies and financial sectors throughout the world remain fragile, and we don't know when stability and growth will return. But if there's a silver lining amidst the dark clouds, it would be that the financial crisis has helped to cement, and strengthen the economic relationship between the United States and China.

Our two nations have worked together to address the financial crisis, both bilaterally, and through multilateral forums, such as the G-20. At the G-20 meeting in London last month, China and the U.S. played active leadership roles, and helped the assembled leaders to reach agreement on making available an additional \$850 billion of resources through the IMF and the multilateral development banks to support growth in emerging market and developing countries. These resources will help to finance counter-cyclical spending, bank recapitalization, infrastructure, trade finance, balance of payments support, debt rollover, and social support.

On a bilateral basis, the U.S. Export-Import Bank and the Export-Import Bank of China announced in December that they will provide funding to support over \$38 billion of finance for exports for emerging market countries. This will help address the acute decrease in available trade finance that has occurred as the crisis has unfolded.

The United States has also been vocal in supporting China's membership in the reconstituted Financial Stability Board, as well as quota reforms within the IMF that will give China and other growing nations more influence and a role that is more reflective of their presence in the global economy.

It's also noteworthy that in a period marked by trade tensions, China and the United States have largely resolved difficult trade and investment issues and staved off protectionist measures. And negotiations are underway on a new Bilateral Investment Treaty.

The challenge ahead for both countries is to continue to improve the quality of our economic relationship, even after we have moved beyond the financial crisis, and to focus on those issues that can deliver greater opportunity for growth.

### **Guiding Principles for Strengthening the U.S.-China Partnership**

Throughout the financial crisis, the United States and China have developed a constructive record of collaboration, and I'm confident this collaboration will

continue. I'd now like to step back and try to identify some principles that can help to guide policymakers as they continue to build on our long-term relationship.

*The first principle is to tend to the shared garden.* George Shultz, who served as Secretary of State for President Reagan, has compared diplomacy to gardening. He once wrote that, "if you tend your garden regularly, and get the weeds out when they are small, your plants will have a chance to thrive." This is a useful metaphor in the context of U.S.-China relations, as diplomacy between our two nations has sometimes been haphazard, and the effect has been the delivery of different – and sometimes conflicting – signals. This relationship deserves sustained attention at the highest levels of the U.S. government and the Chinese government.

*The second principle is to be patient.* In dealing with Chinese counterparts, U.S. officials must remember that China is a 5,000-year-old society, with not only a promising future but a glorious past that brought innovations that changed the face of the world—tea, paper, gunpowder and cast iron. China can contribute to produce the next game-changing technology and to develop solutions to today's global problems—sustainable economic growth, poverty alleviation, climate change, and regional peace and stability. Americans, however, need to keep in perspective the fact that China is an enormous society of 1.2 billion people with the full range of attendant political, social and economic complexities. Both countries need to take the long view.

*The third principle is to focus on the little things.* Often times it's the micro reforms that offer the biggest and longest payoff. China's move to make its trade laws fully transparent has promoted trade with the country, as companies can make business plans with reduced fear of tariff, or non-tariff, barriers being imposed arbitrarily. Similarly, the creation of relatively independent and professional regulatory agencies for banking, securities, and insurance has helped all three industries develop.

*The fourth principle is to encourage and facilitate the move to multilateralism.* While serving in government, my meetings with high-level Chinese officials served as a constant reminder of one thing: China wants a seat at the table of the major powers. That explains why it has affiliated with a number of multilateral institutions and agreements, from ASEAN to the Comprehensive Test Ban Treaty to the WTO. And it signals a growing willingness to conform to international norms. This is good for China, and good for the U.S., as membership in these institutions provides forums for communications and dispute-resolution.

*The fifth principle is to continue to focus on economic integration and development.* China's rapid economic growth over the past 30 years is a tribute to its embrace of free markets, rule of law, deregulation, privatization, and openness to foreign investment. With China's commitment to move to the next stage in the country's growth, there is an opportunity to work with the country on a package of reforms

that are in the interest of both countries, such as continuing to develop and liberalize the financial sector.

*The sixth, and final, principle is for the United States and China to acknowledge their interdependence.* The U.S. economy is highly dependent on China – the country is the second-largest holder of U.S. Treasury assets, which has helped us to finance our deficit and to keep our interest rates low. We also benefit by being able to purchase lower-priced goods from China; the investment bank Morgan Stanley has found that U.S. imports from China resulted in \$600 billion of savings to U.S. consumers from 1995-2005. The United States, in other words, has a significant stake in continued economic progress in China. As Hank Paulson observed during his tenure as Treasury Secretary, “the biggest risk we face is not that China will overtake the U.S., but that that China won’t move ahead with the reforms necessary to sustain its growth.” And, the Chinese economy is highly dependent on that in the U.S. as a major consumer of Chinese products. It is imperative that China and the U.S. move forward hand in hand, or, as the Chinese would say, *xieshou bingjin*. Each country needs to recognize the shared mutual interest we have in each other’s success.

Since establishing diplomatic relations 30 years ago, the Sino-U.S. relationship has flourished – benefiting both nations. Continued improvement in the bilateral relationship holds the promise of contributing to higher levels of global economic growth, cooperation on a range of complicated cross-border issues (such as the environment and the proliferation of weapons of mass destruction), and helping assure Asia’s continued evolution as an economic power.

## **Conclusion**

Going forward, policymakers in the U.S. and China need to remember that harmonious bilateral relations are not defined by the absence of competition but by skillful management of the issues, addressing areas of potential conflict while promoting cooperation in other fields. Neither the United States nor China should let differences on individual issues, as important as they may be, distort or detract from the overall relationship, since this is a mutually advantageous relationship that can deliver greater prosperity, and security, for people in these two nations, and in nations throughout the world.

Underpinning the U.S.-China relationship are the opportunities that come from education – enabling people in both of our countries to pursue their dreams and maximize, if not exceed, their potential. More than 200 years ago, Benjamin Franklin, one of America’s Founding Fathers, observed that, “An investment in knowledge always pays the best interest.” That’s even more true today, and it underscores the critical importance of institutions like Yale University, CSIS and Fudan University educating our citizens and laying the groundwork for the future.

Thank you for the opportunity to speak with you today and to participate in this year's Shanghai Forum.

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