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Consequential China: U.S.–China Relations in a Time of Transition

The Honorable Franklin L. Lavin

Abstract: *On April 20, 2011, long-time “China hand” Frank Lavin addressed an audience at The Heritage Foundation on the future of U.S.–China relations. How will the U.S. economic turmoil affect the Chinese economy? What is the impact of the “Jasmine spring”? Which effects will China’s leadership transition have on relations between the two countries? What is the future of economic nationalism in China? Ambassador Lavin lays out a measured—and optimistic—view.*

Glad to spend some time today to talk about China. I have had the privilege of devoting most of my professional life to China, whether in academia, business or the public sector, and it is a double pleasure to have this discussion at The Heritage Foundation where we have a terrific combination of very serious policy experts and a lot of younger people who are starting to think seriously about policy. As we know, the magic that takes place at Heritage is not just the pure policy analysis, but also its application. I have had a chance to tell Heritage’s president, Ed Feulner, and other people in Heritage leadership, that it is the extraordinary timeliness and succinctness of Heritage papers that have such an impact on people in government. Heritage papers were always an important reference point for me when I served in government—to be able to put your hands on something very timely and concise, and to go through it and have that as a foundation as you come to policy tradeoffs yourself. So it is a pleasure for me to pay respect to Heritage, to a

Talking Points

- China has climbed out of the misery of the past century and is forging a modern nation, with the fastest-growing economy in the world, a burgeoning middle class, more university graduates than ever, growing international political reach, more Internet users than any nation in the world, and the most powerful military China has ever seen.
- This new era for China also brings with it foreign policy management challenges for China and for the U.S.
- Chinese policymaking can be constrained by domestic bureaucratic and political requirements that reduce flexibility and ignore cost-benefit analysis. This sometimes leads to policies contrary to China’s own long-term interests.
- Nonetheless, the U.S. and China do not have adversarial interests and Sino–American relations have gradually improved in the 40 years since modern diplomatic relations began.

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group that has been a good partner in the policy business all these many years.

I mentioned that I have had the privilege of spending much of my professional life dealing with China and China-related matters, and maybe that is what makes me, in a broad sense, an optimist about China and U.S.–China relations. I think the more one watches China and works on U.S.–China relations, the more reason for optimism one sees, because China is going through quite significant changes, and I think they are overwhelmingly positive changes—not just for the people of China but also for U.S.–Chinese relations. But the size of China, as well as the size and complexity of the United States, means that this relationship might become the most complicated diplomatic relationship in the world.

There are any number of differences, challenges, and even friction points in the bilateral relations, but I want to underscore my optimism because the policy emphasis is such that it requires that most of our time be spent discussing the problems or challenges. However, before I get to that, I want to talk a bit about what is working. For example, it is interesting to me that both China and the U.S. have a national-interest-focused foreign policy. Neither country, I think, subscribes to a philosophy that threatens the other. Neither country, as they say in China, tries to put sand in the other's rice bowl. So I think there is a reasonably positive functional relationship between the two countries.

From a U.S. point of view, if we look over the modern era, since the Nixon-to-China moment, we have about four decades of relations, across eight presidents, both political parties, a range of philosophies, different challenges, and different times. But, there is a high degree of continuity in that relationship and I think there are two pillars that allow for that continuity. One is the pillar of engagement that, regardless of the issue or the challenge, we were not going to break off or try to diminish relations but always try to find a way to improve them. The second pillar is respect for China's one-China policy, that we would not seek to undermine that, although we certainly have interests *vis à vis* Taiwan. But we never tried to directly do something to diminish the one-China policy.

With that background in mind, let me turn to the U.S.–China relationship and some of the tests this relationship might encounter. That takes us really to the topic under discussion today and to my mind, “Consequential China” is a good way of framing the challenge. It is a challenge for both China and the U.S., and what I mean by this is simply that China is now, by virtue of economic success and other elements of state policy, more consequential than it has ever been. This new role, in which China is a leading economic and political power, does present a challenge to both China and the U.S. in terms of foreign policy management.

I would also say that I do not believe that either country has an extensive geo-political tradition. The United States was generally an isolationist power until the Cold War, when it was forced to assume a global leadership position. I would say that holds true for much of China's history as well—that as a massive continental power, it focused on a range of domestic problems. When we look throughout China's history, much of Chinese foreign policy really comes down to simply dealing with border state issues. The Chinese wanted stability on their borders and did not necessarily have broad foreign policy issues beyond that. In recent times, China went through a century of decline and turmoil, which further limited its ability to look at foreign policy.

But now we have a new China. Over the last few decades, China has climbed out of the misery of the past century and is in the process of forging a modern nation—the fastest-growing economy in the world, a burgeoning middle class, more university graduates than ever, growing international political reach, more Internet users than any nation in the world, and the most powerful military China has ever seen. So there is a China that has extraordinary capabilities and a much greater sense of self-confidence.

And remember, all of this takes place against the backdrop of the financial turmoil the West has faced over the past two years. It is, then, not simply that China has been outperforming global economic norms; for the last two years the U.S. and other Western countries have been underperforming. To my mind, the set of developments in China is probably the most significant development in interna-

tional relations since the end of the Cold War and the impact of that is something with which we are still grappling.

I would like to divide up the issues that come with that into two sets of issues, systemic and particular. Systemic issues are those that come about with the rise of a major power, and we could go through international relations history and come to any number of moments where the emergence of a new power had consequences for that country and for other countries as well. What I would like to focus on are the particular issues—issues that are particular to China's rise that might present a greater management challenge. I think these issues are all manageable, but that there are some challenges. Let me offer some illustrations.

The Primacy of Domestic Requirements

The core of foreign policy management for China is external equilibrium: How do you achieve your goals in a peaceful setting? But the policy decisions are driven by internal equilibrium, so we have an internal set of factors that limit, constrain and define policy options, but those policy options are projected externally. It is not necessarily a contradiction, but it is a constraint. In other words, China seeks to advance its foreign policy goals through a set of policies and tools, but a primary determinant of these foreign policy decisions are domestic political and bureaucratic requirements. China is not alone in this respect; this is a phenomenon in the United States as well, but sometimes the disconnect between internal requirements and external goals can be striking. To illustrate this point, let us look at some policy statements China made about South Korea late last year.

One of the key regional relationships for China is its relationship with South Korea, even though China has had a longer relationship with North Korea. In many respects, China has done a good job of cultivating South Korea, and there have been much closer economic and cultural ties with South Korea over the years than with North Korea. But late last year, a senior Chinese official gave a speech to a People's Liberation Army (PLA) audience at a Korean War anniversary event, where he stated that

the war was, "A great and just war for safeguarding peace and resisting aggression." He went on to praise the People's Republic of China's and North Korean actions as "a great victory in the pursuit of world peace and human progress." Well, let us just say that such remarks are unlikely to contribute to better relations with South Korea, and it raises the question of what would prompt these comments. Notably, the remarks did not contain even a courtesy reference to South Korea that we might expect, such as that even though this war was fought for the right reasons but it was over a long time ago and it does not define our relations today, or something of that nature, just some kind of gracious comment toward the other side. But those were not part of the remarks.

I think the answer is that, although these comments do not contribute to better relations with South Korea, they are a very powerful signal to the PLA, that the leadership understands and respects the PLA's role. So the internal requirement prevailed over the external goals.

Let me touch on how domestic political and bureaucratic requirements serve as a constraint on China policy formulation. I want to touch on five examples: internal cohesion, personalities, silos, amplification, and the Internet.

Internal Cohesion

Another example of the primacy of bureaucratic politics in China is that the number one criterion in the Chinese government is internal cohesion. One could argue that there is essentially one question during a job interview with the Chinese government, and it is a very simple one: Are you one of us? A capable Chinese government official essentially spends his entire life demonstrating that the answer to this question is "yes." Life is a job interview. Indeed, when you reflect on the raucous nature of the U.S. political process, it might strike the Chinese as very perplexing. Not only do U.S. political candidates avoid questions like, "Are you one of us," in some respects they are trying assiduously to demonstrate that they are contrarian or anti-establishment or representing a change, and the thrust of the campaign can very much be at odds with the established order and policies. However, in China,

you must be able to demonstrate that you will be a responsible member of the team. The first question is not how capable you are or how creative you are or what your ideas are. The first question is: Are you one of us? You can call that the dead hand of Leninism because it forces on the system a high degree of homogeneity. This does not always get you the best outcome, and it militates against people who want to try a slightly different direction or throw in a different idea. Thus, China does not have much in the way of bottom-up experimentation, and you really have changes from the top down. And people have a need to demonstrate to a broader audience that they are part of the team. In fact, to go back to the Korean example, we might even have a circumstance in which a government official enhances his internal stature by consciously provoking criticism from South Korea or the U.S.

Personalities

A related phenomenon of which we should be aware is the end of the personality-led system and the emergence of a bureaucratic state in China. In some respects this could be reassuring because of the excesses of historic personality-led systems, but in some respects it can also augur a foreign policy drift, because it can require a strong personality at the top of the Chinese system to help shape outcomes that are in China's best interest. Think for a second what classic international relations theory teaches about ascendant powers: that if you are a country on the rise, it is in your best interest to defer challenges and problems for as long as possible. There is no strong argument for prematurely forcing an issue if your capabilities are on the upswing. The longer you put off an issue, the better off you are. Indeed, to most observers, this approach was captured pretty effectively by Deng Xiaoping during his tenure in leadership, what was typically in the U.S. referred as the Charm Offensive, and what Deng himself called *Tao Guan Yang Hui* (韬光养晦)—to, basically, bide your time.

Yet when we look at the issues that have bubbled up over the last year or two, it looks as if there is almost a deliberate pattern of surfacing issues that did not need to be surfaced: harassment of U.S. ships in the South China Sea, the overly hostile reaction to U.S. arms sales to Taiwan, some of the un-

neighborly remarks by Chinese officials to foreign ministers from the Association of Southeast Asian Nations (ASEAN), the ramming of a Japanese coast guard vessel by a Chinese fishing boat. Any one of these actions from the Chinese side could have been stopped by a dominant personality, but, unfortunately, I think, for China, what transpired over the past few years was a series of arguably minor steps that cumulatively created a perception of a country that was taking an aggressive posture in the region.

There are different theories as to why China abandoned this seemingly successful Charm Offensive, which, to my mind, helped them a great deal in Southeast Asia. I believe there has been a combination of factors, some of which I have just articulated, along with the role of silos and the amplification effect.

Silos

By silos, I am referring to the fact that the Chinese government is more compartmentalized than other large governments, with ministries responsible for relatively narrow areas and without many inter-agency mechanisms for coordination. It is not always easy in the Chinese system to think through and argue costs and benefits of various government initiatives. There is a particular challenge if there are short-term or nominal benefits for one ministry and perhaps long-term costs borne by another ministry. For example, if a PLA navy vessel harasses a foreign ship in the South China Sea, that might help the naval command demonstrate that it is committed, that it is part of the team. However, this action could work very much to the long-term detriment of China's foreign policy. Still, the Foreign Ministry cannot countermand a PLA navy decision.

Amplification

There is also an amplification effect, by which I mean that people tend not just to echo established policy but to amplify it in order to signal their allegiance to that policy. Thus, bad policy gets amplified through the system, not toned down as one would hope. It was interesting to me to try to understand what transpired in China after Liu Xiaobo was awarded the Nobel Peace Prize. From the Chinese point of view it was understandable that the award of the Nobel Prize was seen as a severe

public insult, and their starting point was that they wanted to respond in kind, criticizing Liu Xiaobo and the Nobel Committee. But in what respects did that help them or hurt them? What other steps did they take and what were the eventual consequences of this for China's foreign policy? Not only did they not have to respond to the public criticism, but this did play to a domestic constituency and did play to that cohesion point mentioned earlier. Then, after they went through the public criticism, they conjured up their own international prize, the Confucian Peace Prize, and awarded it to a Taiwanese dignitary who had not even been informed he had won. It was a somewhat embarrassing moment, I believe, for the people who orchestrated that event and even worse for Beijing—it just kept the issue alive. Instead of letting the issue fade, they responded because of the cohesion requirement, and matters were made worse because of the amplification effect. They ended up setting into play a set of activities which were not in their own self interest.

The Internet

Let me make a final point on a policy constraint—the emergence of the Internet in China. In general, it has been a positive force and it certainly provides more latitude for discussion than we've ever seen. I am sure there are many people here who click around on Chinese blogs and chat rooms, and it is very interesting to follow some of the discussions. But I think we should also note that in some respects it might also serve as a constraint on policy because Internet chatter in China tends to be a bit unbalanced. On some sets of issues, open criticism of government policy is prohibited, so the audience only receives one point of view.

Beyond that, the Internet itself tends to be a medium, which, for whatever set of reasons, promotes comments that tend to be a bit emotional and maybe even a bit nationalistic. So, instead of thoughtful examination of an issue or the pros and cons, you can get this cheerleading effect. It was interesting to me when I looked at some of the discussions in the chat rooms about the incident when the Chinese fishing boat hit the Japan Coast Guard—that virtually none of the discussion had to do with cost and benefit. Was the incident help-

ful? What was the ultimate accomplishment? What is our goal, and did this take us to our goal? None of this discussion had to do with what we would say was a normal analytical approach. Almost all the comments were just cheerleading.

Some of this emotional response is to be expected because it is the Internet, not a graduate school seminar. But I do think that, cumulatively, this kind of emotionalism does not help China move to more productive outcomes in foreign policy management.

Let me close by saying that I think the Chinese system has many strengths. I think it provides a lot of consistency in foreign policy management. I think the Chinese government typically demonstrates a pretty strong understanding of national self-interest. I do think this understanding provides some strength to China and other countries who are trying to develop good relations with China. You always know where China stands on a set of issues.

My conclusion is that China and the U.S. face twin challenges when it comes to foreign policy management. As China emerges into this new major power role, I think it is going to enhance its own prospects for a successful foreign policy, showing subtlety and restraint that all great powers have to show, and I think this is difficult to do given China's domestic political environment. For its part, the United States needs to be able to display flexibility and goodwill in trying to work with China.

I think the biggest mistake China could make in foreign policy would be simply to assert its foreign policy goals without regard to other parties. An assertion of a point of view is not the same as the adoption of policies that would help you reach your objectives. Sometimes, I think those different concepts are blurred in China. We can understand that domestically they may be somewhat the same. You have a top-down system and if you assert a domestic policy goal, that is an important step on the way to achieving that policy goal. But, it does not work that way in foreign policy as there are other parties involved.

The United States has responsibilities as well. I think the biggest mistake the United States could make in dealing with China would be to view China through a deterministic lens, that China's economic

rise inevitably means hostility. Sino–American relations are a mosaic of a thousand policies, initiatives, gestures, and meetings across a range of government and private sector activities. Relations are not pre-determined by GDP growth rates. Given the size and complexities of the two countries and the many differences between the two governments, it is no surprise there are different points of view and even occasional points of friction, but I also see significant progress in the relationship. If there is as much positive movement over the next 40 years as in the past 40 years, the leaders in both countries should be congratulated for their statesmanship.

Thank you very much for letting me talk with you.

—*Ambassador Franklin Lavin lives in Hong Kong, where he serves as chairman of public affairs for Edelman Asia Pacific. He previously served as Undersecretary for International Trade at the U.S. Department of Commerce, where he was lead negotiator for China. He has also served as U.S. Ambassador to Singapore (2001–2005). In 2010, he chaired the Steering Committee for the USA Pavilion at the Shanghai Expo.*

Questions & Answers

WALTER LOHMAN: For all of the cohesion-based explanations, there are alternative explanations for any of these actions, such as on the Korean peninsula. An interest-based explanation would say that the Chinese never want to see reunification of Korea, and so whatever serves to block reunification is good for them, and a close relationship with the North helps. I'm always surprised by the amount of heat that the South China Sea dispute generates in China. There you have the same sort of dynamic. They're catering to a domestic constituency and so that has prevented them from clarifying exactly what their position is in the South China Sea, but the other answer could be, that they simply want the whole thing. So how do you address that?

FRANK LAVIN: To look at it from a Chinese perspective, from a *realpolitik* perspective, there is an argument to be made that it behooves a country to state a maximalist position. There is some value in that; the value being you never know what you might get if you adopt an aggressive negotiating posture. If you say it is all mine, it might all

be yours. My point is that in the Chinese system you tend to see more of that, or maybe you tend to see that more exclusively because of that need for cohesion in this process and because of the amplification effect. So if someone from China says, I have interests in the South China Sea, no one else from China can come in and say: Actually, there are shared interests and other countries have concerns there as well. People in China have to say, you are right and I will raise you one. You have interests in the South China Sea and I will say that even louder and more fervently and we will keep echoing each others' comments and keep ramping that up. It is very difficult for anyone to tone down and say, actually, historically this is an area of shared interests and it is not surprising that other countries seek a role as well.

KATY WANG: I'm Katy Wang with New Tang Dynasty Television. We have seen more and more riots or strikes in China; it keeps on increasing every year. Also, recently, China started to crack down on activists because of the Jasmine revolution. They are afraid that it will influence China. So I'm wondering how do you evaluate the inner stability of the Chinese Communist Party?

LAVIN: I might disappoint you with my answer, but I would say that China has a high degree of inner stability, even though we know there is a lot of workplace disruption, workplace turmoil, and also know that China has cracked down in the wake of this Jasmine spring in the Mid-East and has tightened up some human rights policies. I have spent a fair amount of time studying the workplace stability issue, and what's important to note is that, essentially, none of this has a political dimension. It sometimes can be directed against local political corruption, but the point is it is not political in the sense of what we saw in the Middle East. It is not motivated by people's views of Beijing; it's typically very local workplace issues. People think they've been treated unfairly, maybe there is local corruption. There is instability in that jurisdiction because of those local issues.

But it is not a broad national political issue and one of the challenges in China is that what we could call the normal workplace elements that allow disputes to be resolved do not exist; normal negotia-

tions on wage-related activity do not exist in the same way. You are just going to see more friction and more strikes and more direct worker reaction than you see in the United States. I would not draw any conclusions about national stability from those set of activities.

DANA MARSHALL: There's been a lot in the press recently, in fact, I think there's an article in today's *Post* and, I think, this week's *Economist* about this \$1.3 trillion hoard that the Chinese have. A lot of questions about that, but I guess one question is: If you are sort of trying to follow the money and their foreign policy, what do you think we might expect will be the use of those enormous funds which effectively are unlimited as far as being able to do almost anything you want? Will they be tapping those to advance their own foreign policy interests? If so, in what directions might you see them? And would those be more likely to be consistent with U.S. interests or not?

LAVIN: Dana, I think we have to distinguish between the sovereign wealth funds themselves and government budget items, because what we're seeing within the formal government budget is more of an effort, for example, to expand soft-power capabilities to take Chinese television global. There are government initiatives to give China a bigger voice on the world stage. But those are formal government initiatives, not the use of the sovereign wealth funds. I cannot think, offhand, of any initiative with the sovereign wealth fund that was essentially political in nature. I think there is a high degree of financial integrity behind those funds. Those funds are there to earn returns. What you might see are constraints in terms of not going into certain places or not doing certain things because there might be some potential business partners that are politically sensitive. So there might be sins of omission if you will, but I haven't seen any sins of commission.

RALPH WINNEY: I'm with the Eurasia center. Two questions. (1) Do you have a perspective on the evolution of the rule of law in Chinese society and dealing with issues such as Liu Xiaobo and the Jasmine revolution? (2) And also, the issue with the Standard & Poor's rating. Do you see the Chinese looking for ways to divest themselves away from the dollar and what kind of reaction do you see being

generated in China regards to U.S. policy and dealing with human rights and business-related issues?

LAVIN: On the first set of issues, I think if you referring to commercial law or contract law, there has been a lot of development in this area. If you are buying or selling in China, if you are developing a shopping mall, if you are undertaking investment in China, I think you will find a reasonably secure commercial environment. I would still encourage companies to look at insurance policies, so to speak, but you will find a legal environment where you can operate and prosper. Indeed, there is an enormous amount of U.S. and international business that takes place in China. If you are asking to what extent can somebody in China use the legal mechanism to protect himself in protesting or politically challenging the government, I would not put much hope in that approach. I think it is just not going to be permitted. I think the government is committed to maintaining its power and it will not entertain a legal challenge. There have been some publicized incidents where attorneys have tried to use different legal approaches and there's no patience or tolerance for that kind of approach, so I would not hold on to any hopes for that approach being successful.

WINNEY: A couple of days ago, Standard & Poor's gave the U.S. a very negative rating in terms of dealing with the debt. How do you see China reacting to that?

LAVIN: The problem for China is there is no place else to go. The yen does not look that promising. The euro does not look that promising. Other countries just do not have the depth. They are not going to go into Australian dollars, pounds sterling, Swiss francs, so I think you are right. I think they would say we would not mind diversification or some kind of rebalance, and there has been some of that at the margin, but there are not more attractive alternatives. I do not think the U.S. dollar is in question, the Chinese are not in the U.S. dollar for sentimental reasons or political reasons; they are in the U.S. dollar because it is the best currency to be in. If that deteriorates, if that changes even at the margin, then it behooves Chinese leadership to adjust accordingly. So my advice to U.S. policy-makers is: Run your economy so you are always the most attractive currency and you can command that

kind of inward investment from around the world and people seek your currency as their currency of choice. But if you stray from that kind of performance you can only expect other countries to adjust.

KELLY CURRY: From the Project 2049 Institute. You laid out how the internal dynamics of the regime drive external policymaking in terms of foreign policy. But, in thinking about this further, doesn't the fact that China is run by an authoritarian regime that has these characteristics that you described, doesn't that place some structural limits on the relationship between the United States and China on some level?

LAVIN: Yes, I think it does. I think it is unfortunate. By the way, I think the relationship is growing nicely and there are a lot of positive elements to it, but it is probably doing the best in the areas outside of formal government purview. So, economic, finance, trade relationships are booming; educational and academic student exchanges and cultural activity is booming. But, government-to-government contacts are not growing as rapidly; they are still developing. There are still things going on, but Americans are just going to feel more comfortable collaborating with like-minded countries. So, things move more slowly.

LOHMAN: Let me ask you a question if I could, because you talked about how the system works in China. How does good advice make its way up through the chain in China, and I ask because we have think tanks that come here all the time and a lot of bright people in think tanks, a whole array of them. But I wonder, who is the guy that walks into the State Council and says: Guys, you're doing this wrong. Does that happen? And it has real consequences, most recently, I think, with the calculation the leadership made on the prospects of President Obama one day selling arms to Taiwan. Chinese leadership clearly thought that wasn't going to happen. And now I see the same things happening on the prospects of a Democratic Progressive Party (DPP) victory in Taiwan. It's actually a real prospect, but most of the Chinese you talk to dismiss it. Who's the guy that walks in and says: Hey guys, this might happen, you should get ready for it?

LAVIN: I think you might have put your finger on one of the challenges. I agree with you; there are a

lot of challenges in information flow in China. There are a lot of people you can have very thoughtful discussions with. And it is encouraging that the kind of discussion we're having in this room, that you can do trade-offs. What are your interests where are you trying to go? How might those impinge on my interests? In what ways can we collaborate? That's normal give and take of foreign policy, but it's easier to have that on a track two channel than a track one. Track one tends to be a bit more formal maybe a bit more dogmatic a bit more maximalist and so forth, so it is a bit harder to have useful discussions.

But I spent a long time in formal negotiating rounds with China. One of our rules of thumb was that at least the first round of trade negotiations was done for domestic consumption. That participants had to go into this room and say that here is what I do not like about you and here is what I need and here is why I will not go along with you, and they had to be all out there on the table in order for them to then be able to say, What can we work on and what do we have to do? So information does not flow as readily as it could in that system. And there is a problem, I think, with hierarchy and there is a problem with filtering mechanisms.

I would say the senior people in U.S. government, whatever their faults and defects might be, they are at least aware of the core argumentation of the alternative point of view. In the course of the discussion someone will articulate a contrary position: Here is why what you are doing is wrong. I do not mean a screaming match, I mean somebody actually saying: Here is an alternative approach. Let me say something in defense of China: My sense is that when you are away from the most sensitive international issues, such as when you are talking about municipal planning, or to what extent we should subsidize development of rural areas, you will have a much more open debate about this and that is not as sensitive politically.

QUESTION: I'm from the Middle East Media Research Institute. How do you see China's rise affecting U.S. policy in South Asia, especially in view of China's military presence in Pakistan, of China's aggressive policy in Kashmir, and against India on other issues?

LAVIN: I think we can make a general point

here. I have talked about systemic points. I think whenever a new power emerges, neighbors are generally not going to look upon that with favor. It does not mean they are hostile or negative, but it does not mean they welcome it either. So, I think there is a burden on the rising power to make an extra effort to communicate. I do not mean just communicate in terms of messages; I mean their military doctrine and their military budget and confidence-building measures that would reassure neighbors that the increased military capacity does not indicate any kind of hostile intention. My advice to my friends in Beijing, then, would be to put an extra effort in that kind of military diplomacy, because people are more inclined to draw negative inferences from the rise of another country than positive.

BEN YU: With the *Duo Wei Times*. I hope to continue with your discussion of your comment on there being no alternative to the U.S. dollar. Lately in the Boao Forum in Hainan, the BRIC countries [Brazil, Russia, India, China] have released a joint leader release on the desire to see an alternative framework for international reserves, for emphasis on the possibility of special drawing rights serving as an international currency.

LAVIN: Does that not mean that they basically agree with me, that there is no alternative? Their statement was they wish there were an alternative, if there was an alternative we would use it.

YU: My question is, do you see this raising any eyebrows in Washington? This is my first question, my second question is on the particular issues you mentioned with regard to U.S.–Sino relations: You didn't seem to mention much about Taiwan, which has lately been off the radar, but to those concerned, such as the U.S.–Taiwan Business Council, which has been pushing for military sales of the F-16 C/D and A/B upgrades, I was wondering if you could comment on this and the progress.

LAVIN: I took this BRIC statement as a somewhat symbolic statement of what you say if you're trapped. If your policy constraints are limited, you pass a resolution saying we wish we had alternatives. It didn't seem to be an alternative to what I said; it seemed to validate what I said. The U.S. dollar is still the best currency to use even if the Chinese are less enamored now than they might have been five

years ago. But there is no alternative, so they get together and pass resolutions saying we ought to have an alternative. You would not have passed that resolution if you actually had an alternative.

So I think they are just agreeing with me. But, they are doing it from a political posture. South Africa, for instance, wishes it could diversify and not have its reserves disproportionately in U.S. dollars. But there was not even a map or a program or a timetable or steps to take.

Here is my view of Taiwan. This is a very sensitive area and I sometimes have disagreements with friends in Beijing on this point, but we have seen two parallel trends in this issue over recent years. One is a very welcome improvement in cross-strait ties. As you suggest, it is not necessarily government-to-government, but it is in commercial and human contact and social exchanges and so forth and that is helpful on several levels. But we have also seen a strong role in Taipei–Washington ties. So my message to friends in Beijing is: Do not view a moment when Taiwan takes a step toward Washington as taking a step away from Beijing—because, in fact, it is the U.S. commitment to Taiwan and the U.S. relationship with Taiwan that gives Taiwan the self-confidence to engage more closely with China. Having the U.S. in the picture is helpful to Beijing from my point of view. If you imagine for a second a hypothetical, if the United States was out of the picture and ended all its relationship with Taiwan, would that induce Taiwan to move closer to Beijing or not? To my mind, it would be very harmful to Beijing because that would freeze Taiwan.

Taiwan itself also has domestic political constraints. The Taiwanese have to act out of a sense of self-confidence as well and that relationship with the U.S. helps give them that self-confidence. I would say, then, do not view these as trade-offs or an inimical policy approach, because having the U.S. in the picture has been helpful to Beijing.

TERRY CAMPO: I'm a private attorney. I'm wondering, do you find in your dealings a significant difference in doing business between the state-owned companies and other PLA-owned enterprises?

LAVIN: I do not know. I do not do any business with PLA enterprises. There might be a passing shareholder in a shopping mall or something, but I

have never knowingly done business with any PLA enterprises. I have got to tell you, day-to-day business in China is highly regularized and there is a strong commercial logic that flows through transactions. If you are new to the market, you need to be thoughtful and it is easy for transactions to go wrong, but it is a good place to do business, I am very bullish on China as a business operating environment.

Let me give you one set of statistics. Last year, France was the U.S.'s 11th-largest export market, with something like \$28 billion in exports, not a surprising number because France has a huge modern economy. I thought that was an interesting number for the purpose of this discussion because the growth in U.S. exports to China, last year, was also \$28 billion. We grew in one year by an entire France. I was talking yesterday to a person from a multinational corporation and he was talking about their French trade strategy. I said I am all for it; you need a French trade strategy. China, in terms of U.S. exports, is creating a France every single year. Develop a French strategy, of course, but you better have a China strategy because every 12 months you have a new France in trade terms. It is just as important, then, that U.S. companies develop a China strategy and get serious about the China market and devote their resources and efforts to finding success there—and, boy, U.S. companies do it every day.

DEAN CHENG: I'm with The Heritage Foundation. Welcome back. The Chinese themselves have described last year as *annus horribilis* in their foreign policy, and apparently there was a foreign ministry conference led by Hu Jintao that basically said we need to reassess how we do things. From where you are out there, what have you seen with regards to Chinese reset, have you seen, substantively speaking, a remodulation, a reorientation? If not, given how deeply into the hole they've managed to dig themselves, how much do you think they can do in this situation?

LAVIN: By the way, Dean, I think you are right: The Chinese ended up overshooting on a number of these issues; they ended up creating a fair amount of ill will that, as the other question from South Asia suggested, if you do this in that context of growing military capability, you are setting yourself up for a

negative reaction. And I do not think they have fully appreciated that it is a different world than even 10 years ago. I tell my friends in Beijing that over the next few years, China will receive more praise and more compliments than it ever received in history, but it will also receive more criticism than it ever received in history, and this is because it is a consequential nation. What China says and does ripples through the region and the world, and people respond to it, and I think that is a growing moment for foreign policy. It is a little bit like the BRIC special drawing rights question. Foreign policy is no longer a symbolic series of statements.

I mentioned in my remarks that you cannot simply assert policy and hope to find success, but you have got to come up with the steps that will take you there. By the way, those steps probably involve some trade-offs, some flexibility. You have to decide what is really important if you say: Here is where we are trying to go. But if you have 95 percent of that would that be okay, and if you have to give up something, this is what all other foreign ministries in the world do. But it is hard in the Chinese system to show that kind of subtlety. That is why the thrust of my remarks is that, unfortunately, this system has a lot of rigidity in it. That gives it some strengths, too, but I think it also constrains policy choices.

What I have seen since their reset is simply a more subdued approach to foreign policy. I would not quite say we are back to Tao Guan Yang Hui, but there is no desire to force these issues in the near term, and I think China has gotten better at some of the bread and butter diplomacy, whether it is taking Chinese television global, whether it is the reaction to Fukushima, and putting aid into Japan. These are just building blocks, but China is more adept than that. I remember that after the Indonesian tsunami, China sent a medical team down; good for them that they did that, but interestingly, nobody in the medical team—I met them—nobody on the medical team spoke English, or spoke Bahasa. So, it was the right gesture, but it was not a useful gesture. But in Fukushima, I think they are much more adept at helping out. I do not think there is been any real policy turns, but I think what we have seen is a more subdued look at policy and more of a focus on soft power.

LOHMAN: Just as follow up to that, what do you do with the statements that are already out there? Say, for instance, the South China Sea pronouncement, what do you do with it?

LAVIN: You are right, and I have talked to friends in China about that. By the way, that was not a formal government policy, but it was a statement by a government official. So you will hear that kind of statement, which I think is about as close as you will get in the Chinese system to saying: You know, we might have gotten that wrong. But, this is probably what Dean is suggesting, that we are all, in life, in foreign policy, in business, we are defined by our worst moment. If you act civilly to everyone in your office every day of the year but one day of the year you start swearing and cussing, nobody will say that 99 percent of the time Walter is a good guy; they will say this guy is a screaming lunatic, right? In business, it is the same thing; if you treat someone honestly 99 percent but dishonestly 1 percent, they will say you are a dishonest businessman.

The point is that foreign policy is the same too, so this is the very unfortunate incident at the ASEAN foreign ministers meeting where a very senior Chinese official, in the course of a debate, said, We are big and you are small. Which is, I think from an ASEAN point of view, very difficult to accept, because what that really means is that right and wrong do not matter, the legality of this position does not matter, the morality of it does not matter, what matters is that I can do it. And you cannot stop me.

It is not what you want to hear a neighbor say, and you can just imagine if a U.S. cabinet member went to the Caribbean in the course of a disagreement, a different point of view, and made a similar point. The U.S. tells its diplomats that a diplomat should be diplomatic. You have to listen to the other countries and, yes, they will have their point of view and you will have yours, and we do not have to dominate and prevail at every point. Let us decide what is important and get out there in a collegial sense. It would be a very different instruction to U.S. diplomats.