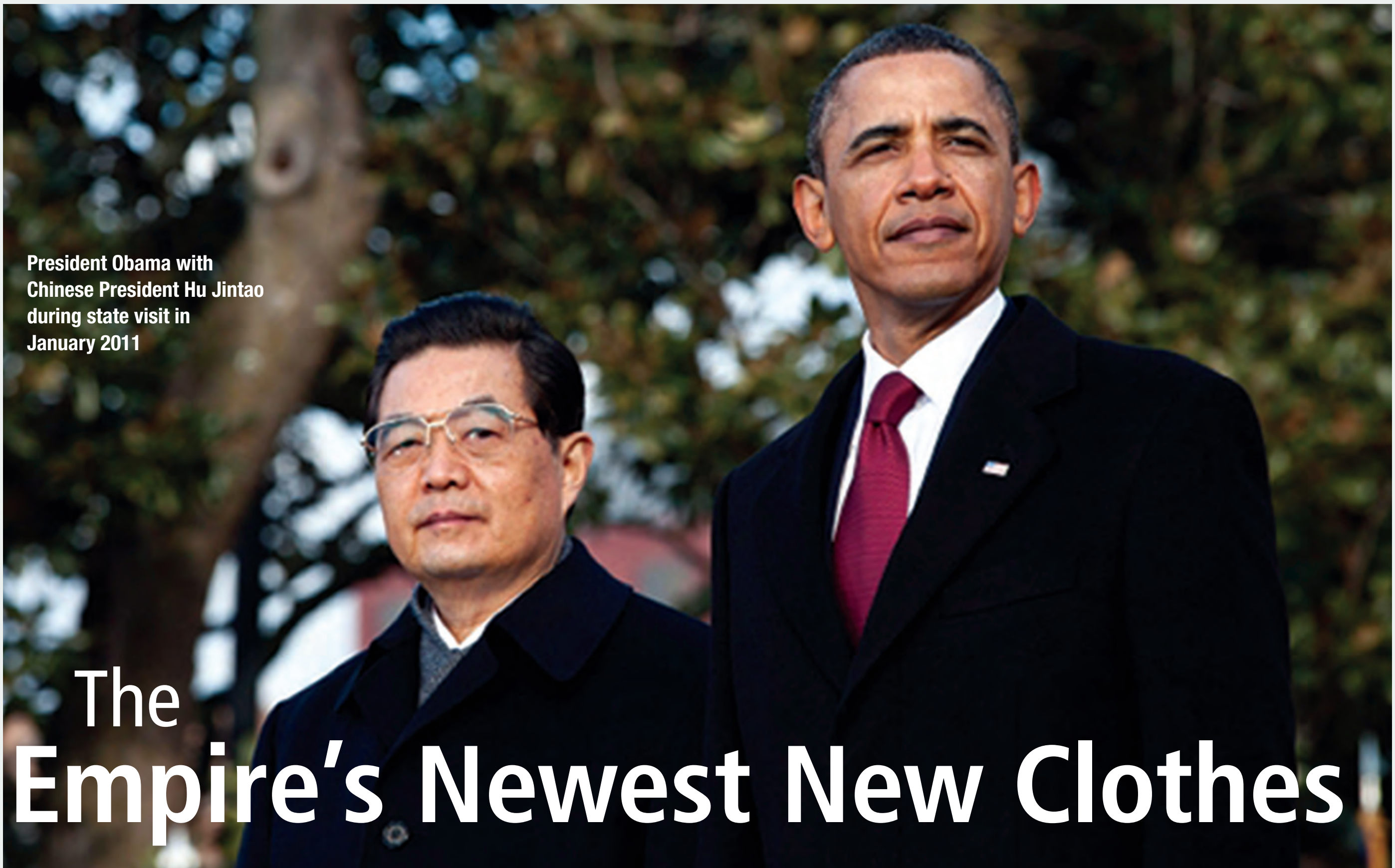

President Obama with Chinese President Hu Jintao during state visit in January 2011

White House (Pete Souza)

The Empire's Newest New Clothes

Overrating China

By STEVE COONEN

There is a potentially dangerous obsession in America regarding China. The Middle Kingdom's awe-inspiring climb from a state of backwardness and abject poverty to a thriving economy, second only to the United States, in just over 30 years has not merely inspired justifiable pride within the People's Republic; it has also provoked anxiety and fear in the West.

According to many, the "Chinese model" now serves as an enlightened beacon to other developing states, while the liberal free-market model languishes in disrepair along with its decrepit and lethargic American makers. China's overseas investment strategy in energy, minerals, and other resources is portrayed as parasitic in nature—ravaging the Earth of all that is useful in a competitive quest for domination, while its menacing purchase of America's debt-gone-wild is allegedly making American leaders increasingly beholden to their Chinese debt-masters' political manipulations. Meanwhile, China's rapidly expanding manufacturing base is moving beyond lead-based painted toys, poisoned pet food, and toxic drywall to supersonic stealthy fighters, high-speed rail, clean energy, and the world's fastest supercomputer.[1]

On the surface, fear is an understandable emotional response. The United States is seemingly losing to China in a no-holds-barred global economic competition, and there is no dearth of Cassandra-like assertions from government leaders, unions, the press, and academia portending doom, gloom, and America's decline. Even America's top diplomat pulled out the Chinese bogeyman card in an attempt to ward off Congress's penny-wise and pound-foolish proposed sacking of State Department public diplomacy programs.[2]

Assertions of Chinese dominance are beginning to ring true with the American public as well. By a margin of 60 to 27 percent, Americans see China's economic strength as more of a problem than their military strength, and 47 percent also incorrectly identified China as the world's largest economy (only 31 percent correctly identified the United States). Equally unsettling is the zero-sum perspective for 47 percent of Americans who consider China's growing economic power a bad thing.[3] The incessant sensationalism surrounding

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China's economic prowess almost obliges one to wonder where the United States derailed to have permitted China to climb to such heights, as though America can control China's destiny but not its own.

However, despite the outpouring of declarations claiming China's unstoppable ascent and its menacing nature, reality depicts something quite different. China is confronted with a number of significant economic and noneconomic challenges that will inevitably retard its continued growth. Yet China's troubles are no reason for America to rejoice; it is hardly in U.S. interests that China, or any state, fails to develop economically. Wealth tends to engender peace, stability, and, some contend, democratic reforms in autocratic societies.[4]

This article focuses on the two main challenges that limit a proper understanding of China's economic relationships and condition. First is the misunderstanding about the mutually beneficial nature of economic relations between the United States and China. Second is an underestimation of the economic challenges that China faces. The article concludes with U.S. policy recommendations that encourage China's return to market-based reforms.

Fears and Fallacies

Prior to delving into China's numerous problems, one should address those misleading assertions that depict Sino-American economic relations in a less than positive light or project them forward on a confrontational trajectory. Alarmist indictments taint America's perspective with negative biases and an adversarial mindset. If not understood, instead of responding with appropriate policies to address China's very real and growing problems, the United States risks focusing on falsehoods or flawed understandings of Sino-American trade relations, the market, and America's appropriate leadership role. These fears and fallacies need to be addressed and dismissed before moving on to China's more pressing challenges.

The list of imaginary economic perils that China poses to the United States is as lengthy as it is troubling. However, the bases for the alleged threats are laden with logical fallacies. The most significant misunderstanding surrounds the notion that if China is growing—winning—economically, the United States is somehow losing. Many are

Chinese Defense Minister in Singapore during 10th annual International Institute for Strategic Studies Asia Security Summit, June 2011

DOD (Cherie Cullen)

drawn to the misconception that the United States is in a zero-sum economic competition with China, overlooking the simple fact that companies compete, states do not.[5] The assertion assumes that wealth is finite and thus every dollar China earns can only come at a reciprocal loss to the United States. While this is certainly true in the casinos of Las Vegas or Macau, it is not true in the economic relations between nations.

This assumption ignores that wealth can be created and that trade can be mutually beneficial. These economic truths help to explain how the global economy grew from $22.8 trillion to $53.3 trillion between 1990 and 2007, or that there are "no examples of countries that have risen in the ranks of global living standards while being less open to trade and capital in the 1990s than in the 1960s."[6] In this light, China's economic growth should be viewed as wholly positive. Economically, it represents a growing market and wealthier trading partner for the United States. Morally, it means that millions of people are now living outside of chronic poverty. Politically, there is no reason why China should not follow the precedent of other former autocratic states whose oppressed citizens increasingly demanded a greater voice in how their newfound wealth was spent.

Commodities and Overseas Investments. Similarly, opinions about China's foreign direct investments (FDI) have taken on a troublesome tone in America. The misperceptions characterize Chinese FDI as a competition—a race for resources—that compels an equivalent U.S. response, or at minimum a dirigiste strategy, before the Chinese assume ownership and control of all the world's resources.

This anxiety demonstrates a fundamental misunderstanding concerning the nature of commodities. Commodities, such as oil, iron, and wheat, are fungible and are generally purchased on the world's commodity spot markets at prices that the markets bear. If China is able to assist states in the exploitation of natural resources through its overseas investments, then those who consume the commodities will likewise benefit from increased global supplies.

Nowhere has the misnomer of competition for resources been more pronounced than in the panic-stricken assertions of China's alleged attempt to corner the energy market. It is somehow imagined that Chinese national oil companies (NOCs), operating under Chinese Communist Party (CCP) direction, are gobbling up foreign energy assets and hoarding their output, flowing from the wells into Chinese tankers (which

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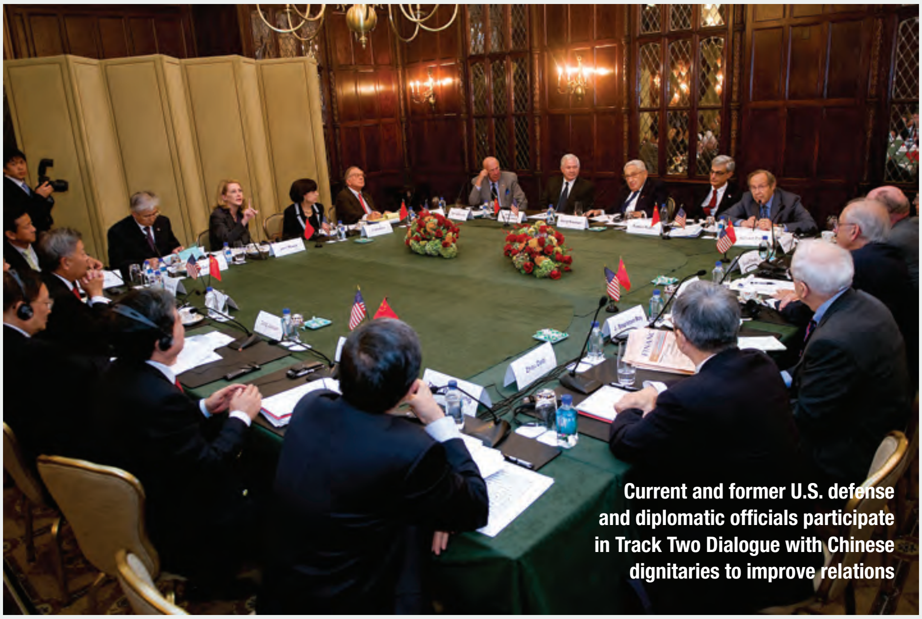
are virtually nonexistent) or pipelines to Chinese refineries before being prolifically consumed by over a billion of the proletariat.

The International Energy Agency describes a vastly different scenario. Like their American counterparts, Chinese oil companies' decisions directing the marketing of equity oil are largely based on commercial considerations. Even state-to-state energy arrangements are usually influenced by market conditions.[7] China's "new acquisitions do not translate neatly or exclusively into supplies flowing to China."[8] Erica Downs of the Brookings Institution observes what is apparently not obvious to many: "Any foreign oil production that China's NOCs send to China merely replaces oil that China would have to buy from other countries."[9] Thus, far from being a rapacious predator in the energy markets, China's acquisitions in the energy arena actually increase the global availability of oil.[10] This is also true for China's investments in other commodities.



DOD (Cherie Cullen)

Current and former U.S. defense and diplomatic officials participate in Track Two Dialogue with Chinese dignitaries to improve relations

Debtor-Creditor Relations. Fear that China can exert undue political influence over the United States as the largest single foreign owner of U.S. debt represents another misplaced worry.[11] The anxiety nonetheless seems logical—that the creditor would have a certain degree of influence over the debtor—and the greater the debt, the greater the influence. Yet when the specifics of the Sino-American credit-debt relationship are evaluated, the disconcerting aspects dissipate.

China "owns" just over 8 percent of U.S. debt.[12] The American public (individuals, institutions, and Social Security) actually holds the greatest portion, and yet their influence over U.S. policymakers is not derived from owning more than 2 out of every 3 dollars of government securities. Instead, their influence is wielded at the polls—a civic responsibility and privilege unavailable to foreign U.S. debt holders.

Nor is China actually lending America money as it is "depositing" or "investing" in U.S. treasuries.[13] In fact, with last year's historically low interest rates, investors were receiving a negative return on their U.S. treasury purchases; China was in reality paying for the privilege to purchase America's debt.[14] China consistently exports more than it imports and tends to attract more foreign investment than it sends abroad. The resulting trade and investment surpluses are enormous. China needs to park this excess capital somewhere and is fortunate that the United States is, for the time being, profligate enough to assist China with its excess reserves dilemma. JPMorgan Chase & Company predicts that China will keep buying U.S. treasuries "not only for the near-term stability of the global financial system, but also because there is no viable and liquid alternative market in which to invest China's massive and still growing reserves."[15] Purchasing U.S. treasuries is also one of the mechanisms by which China can keep its currency pegged to the dollar. The resulting dollar-yuan exchange rate is one of the keys for China to maintain its export-driven economic growth—an economic condition that the CCP views as vital in preserving a semblance of domestic stability. Ironically, China's leaders have begrudgingly little choice but to "Buy American"—in this case, debt.[16]

So how are Chinese debt-masters translating this alleged financial stranglehold over America's increasingly indebted policymakers? The actual details of the debtor-to-creditor political manipulation process are, not surprisingly, rather vague. Alas, despite owning over $1 trillion in U.S. treasuries, China has been unable to convert the threat of its heavily debt-laden sword of Damocles over the United States into any noteworthy acts of political compellence.[17] In his study, Daniel Drezner concludes that "the power of credit between great powers has been exaggerated."[18]

Still, today there seems to be a general sense of surrender to the economic myth that is China. When compared to the bashing of Japan and Germany in the early 1990s, there is a notable absence of counterarguments. It is as though at a certain level, America, bound by the grasp of recession, debt, and a general sense of overall economic malaise, has resigned itself to decline. The lack of a counter-response suggests apathy, resignation, or something else—but surprisingly not disbelief. Yet there should be an element of disbelief or at least a questioning of China's position relative to the United States, for China also has economic challenges. So, while the United States seems to be slowly coming out of a cyclical economic stupor and will continue to face grave challenges associated with its annual deficits and mounting debt into the foreseeable future, China is presented with more serious long-term structural issues that risk derailing its economic miracle altogether.

China's Economic Challenges

China's economic revival came on the heels of Mao Zedong's reform failures and could scarcely have started at a lower point. The Great Leap Forward was marked by economic regression and the deaths of tens of millions. A few years later, the Cultural Revolution again brought economic growth and education to a standstill and ensured a decade of political violence that set China back even further. It is out of this chaos that

UN (Eskinder Debebe)

Chinese guards with African Union–UN Hybrid Operation protect borehole operated by Chinese engineering company in Sudan

China could only improve, and it helps in understanding its sizable initial successes.[19]

The "Four Modernizations" announced in December 1978 was a watershed economic policy decision of Deng Xiaoping and the Central Committee of the CCP. It propelled China to amazingly rapid and relatively sustained economic growth. On paper, the reforms focused on applying science and technology to agriculture, industry, and national defense. In reality, the plan called for incorporating foreign investment and technology along with the education of Chinese students overseas.[20] China witnessed a liberalization in the factors of production: a "free movement of people" in its urbanization efforts; an attraction of foreign capital; and liberalized trade with the rest of the world—ultimately relying more and more on market forces rather than CCP production quotas or other command-economy principles, which were quickly abandoned. The autocratic nature of the reforms, while not representing ideal free-market conditions, were nonetheless liberalizing enough that when applied to a country of 1.3 billion, most of whom were living in poverty, they launched China to unprecedented levels of continuous economic growth.

As less productive rural labor migrated to a dynamic urban manufacturing base, wages and living standards rose rapidly. China's record in reducing poverty was impressive. It is difficult to imagine that as recently as 1996, China had the largest number of poor people in the world. Remarkably, in 2007, the World Bank claimed that "extreme poverty, in the sense of not being able to meet the most elementary food and clothing needs, has almost been eliminated [in China]."[21]

China's economic success is a unique phenomenon that defies precise labeling. Richard McGregor suggests that the "multiple, head-spinning contradictions about modern China" make attempts to describe its system or model extremely difficult. Nonetheless, two things are certain. First, economically, China straddles the free-market and command-economy models. The economic success it has enjoyed to date was generated by Deng's reforms to liberalize its economy. Furthermore, to meet its political objectives, the CCP still interjects itself through state-owned enterprises (SOEs) and the state-controlled financial system. Second, politically, China remains firmly under the autocratic rule of the CCP. The CCP's primary purpose in exercising its leadership over China's economy is "to ensure the survival and viability of the party." This axiom indicates why China's leaders are turning away from the very market-based reforms that permitted its astounding economic growth in the first place. From the CCP's perspective, the firm grip of tyranny cannot be entrusted to an "invisible hand."

Shift Away from Market Economy. The uneasiness of relying on something invisible must be unsettling to leaders of despotic regimes. Moreover, why should autocratic leaders trust it? Regarding the recent demise of the advanced Western democracies and their so-called free-market model, authoritarianism as a reasonable economic model seems to have rebounded with China's rise. Many in the West have become enamored with the mystique of Confucianism and apparent superiority of the Beijing Consensus. Or, if not infatuated with the model, they despairingly describe its ascendancy as preordained.[22]

However, attributing the recent financial meltdown to market failure demonstrates a fundamental misunderstanding of the root causes that led to the crisis. One could easily highlight the genesis of the West's economic challenges not as market failure, but rather as the failure of states in regulating new speculative financial instruments and encouraging irresponsible lending practices by diminishing market risk in guaranteeing private mortgages. For China's leaders to base the perceived superiority of their model on misleading and false assumptions of the free market, and move even further to the left of their increasingly illiberal model, is done at a great peril to their own continued economic development.

China's economic success is a unique phenomenon that defies precise labeling

When Hu Jintao came to power in 2002, many had hoped that he would move even faster and further in the market reform efforts initiated by his predecessors. Instead, Hu moved in the opposite direction.[23] With the economic calamities that struck the West, China's leaders are now even more enthralled with their Eastern version of economic success. Today, this attitude means that the CCP and its leaders are perhaps more inclined to divert even further from past liberal reforms measures, even if China's membership in the World Trade Organization (WTO) and other multilateral and bilateral economic fora should temper drastic changes or oblige them to maintain certain market-based principles.

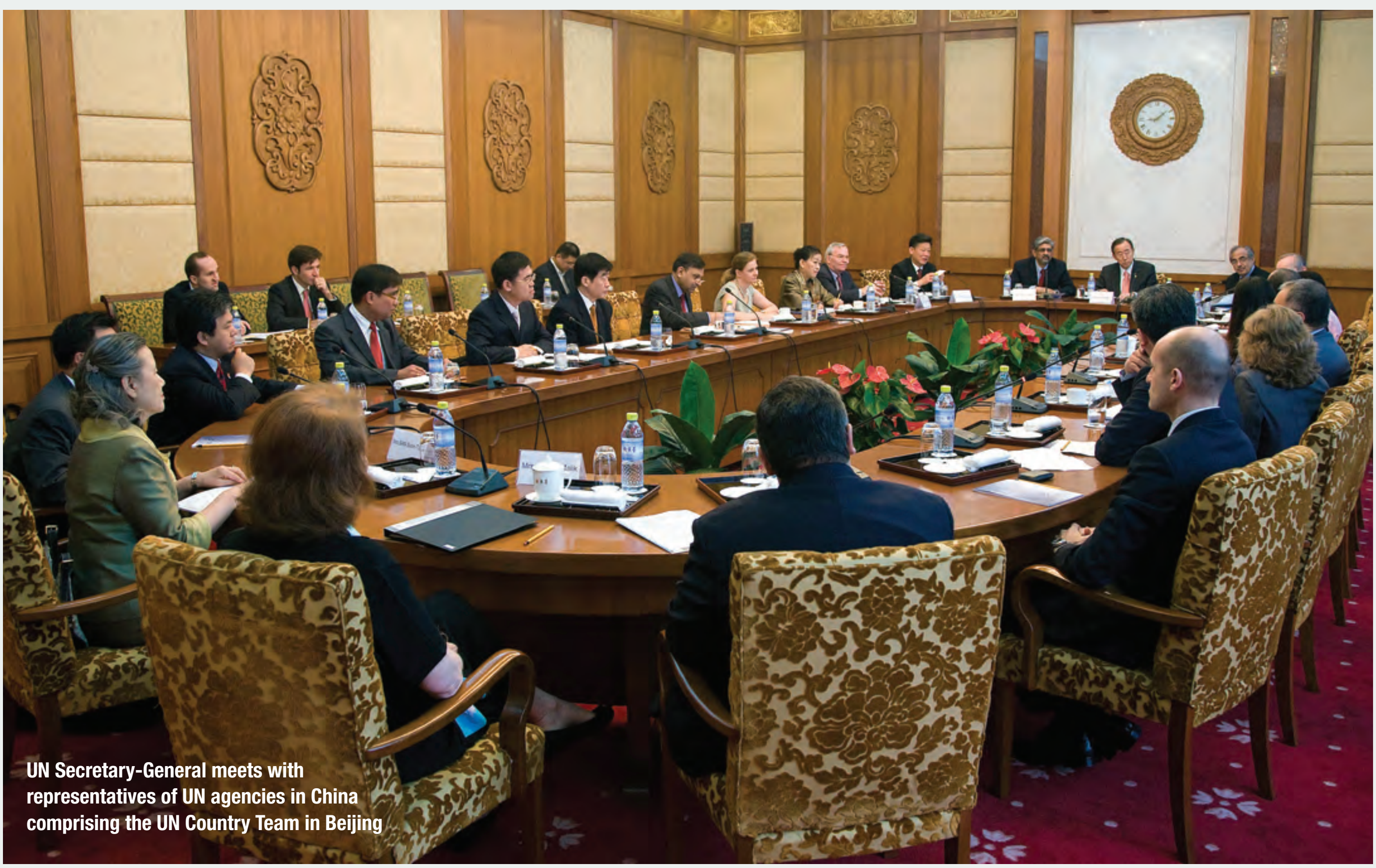
Many observers have noted this shift. The government owns almost all major banks and oil, telecommunications, and media companies in China. Assets of SOEs total about $6 trillion, or 133 percent of China's gross domestic product (GDP).[24] The less-than-visible hand of the CCP is increasingly clawing back major portions of the Chinese economy: from championing command-economy–style monopolistic SOEs to reimplementing price controls.[25]

Domestically, Jialin Zhang writes that the state sector is making a comeback after decades of official encouragement of private enterprise. He suggests this backpedaling is jeopardizing China's relatively nascent market economy. In 2009, the CCP's revitalization plan for 10 industries encouraged SOEs to merge with medium and small enterprises.[26] Eventually, this increase in state-owned monopolies will limit market competition, weaken innovation and technological progress, further contribute to corruption, make investments riskier, and result in more bad loans—in short, it will become a greater impediment to China's continued growth. Notwithstanding the CCP's focus on SOEs, domestic private enterprises are still an important element of China's economic growth. Yet the state is increasingly diverting a greater portion of resources away from private hands and allocating them to largely inefficient SOEs.

Internationally, the CCP's underhandedness and further movement away from previous liberalizing reforms through the championing of huge SOEs are affecting the perceptions and bottom lines of foreign firms. For example, foreign car makers see Beijing's push for joint ventures as nothing more than a "technology shakedown" to gain the capability and eventually become rivals. The actions of the CCP risk choking off future foreign investment and technologies that are necessary for China's continued growth. "There is still a lot of optimism, but there are industry leaders talking about the challenges of doing business in China in a way they would not have 10 years ago."[27] These challenges are increasingly painting China as an economic pariah. Given this unfriendly business environment, some international firms are reluctantly giving up on the prospect of investing in China despite the size of China's domestic market and its potential for significant returns, unquestionably to each party's detriment.

What could possibly have caused CCP leaders to depart from reforms that permitted the party to lead their people out of poverty, regain national pride, and reestablish China as a regional and potential global power? Why would they move backward to a more centrally controlled economy that has no historic long-term precedents of success, but only misery and failure? The answer lies in the party's top priority: to remain in power. The party leadership needs to maintain social stability; leaving continued economic growth to the whims of the market is a risk that the CCP is apparently unwilling to take. Nowhere is this reversal better reflected than in the state's increased role in the allocation of resources through state-owned financial institutions.

China's Weak Financial System. Ownership of financial institutions is dominated by the state, leaving one to question the financial sector's ability to serve the private sector and whether lending decisions are based purely on commercial considerations or the whims of the party.[28] McGregor remarks that Chinese banks are not just commercial institutions; they are also "instruments of national economic policy."[29] It is revealing that in 2009, when confronted with possible major economic decline, the CCP ordered the state-owned and "controlled"



U.S. Army (Jonathan J. Springer)

UN Secretary-General meets with representatives of UN agencies in China comprising the UN Country Team in Beijing banks to further open their already wasteful lending spigots. Banks lent nearly 50 percent more in 6 months than they had in all of 2008. However, the incestuous relationships that SOEs had with their financial confreres through their party affiliations helped them soak up a vast majority of the funds, leaving household consumers and private enterprises with just 15 percent.[30] Zhang adds that fewer than 10 huge conglomerates provide 80 percent of the profits earned by centrally controlled SOEs, leaving most other SOEs relying on government subsidies and credits to survive, and also increasing structural imbalances in the economy. The CCP may hope in "Chinese exceptionalism," but history indicates that governments have exceptionally poor track records in allocating resources efficiently.

In 2009, Derek Scissors of the Heritage Foundation speculated that the CCP's obsession with growth might overheat the economy. Over the previous 4 years, the CCP directed the lending of trillions of dollars through its banks, primarily to SOEs. With today's inflationary pressure in China and probable increase of nonperforming loans that were extended to unprofitable SOEs, Scissors may be getting an answer to the rhetorical question he raised 2 years ago: whether state-directed investment can increase by 25 to 30 percent every year without "crippling waste and a warped, fragile economy."

This waste is often translated into increased corruption along with its associated bedfellows of feeble government regulatory enforcement and substandard quality. These conditions also contribute to China's questionable economic condition and point to serious systemic shortfalls in governance.

Corruption, Substandard Quality, and Slack Regulatory Enforcement. "Made in China" has an automatic, yet justifiable, negative connotation. The poor life expectancy of Chinese products is attributed to shoddy craftsmanship, dismal quality control, or poor regulatory oversight. Not only are the well-noted phenomena of recalls and poor performance having a negative economic impact on companies and individuals that market and purchase Chinese goods; there are also health and safety risks. Corruption feeds these bad practices in production as manufacturers bribe local officials to turn a blind eye on otherwise well-established guidelines and standards.

In 2007 alone, the U.S. Food and Drug Administration issued recalls or warnings on pet food, toothpaste, and farm-raised seafood—all from China. More serious health issues occurred in 2008: poorly manufactured heparin (an anticoagulant) resulted in 246 deaths between January 2007 and May 2008, and contaminated infant formula required the recall of products containing milk imported from China.[31] The Consumer Product Safety Commission has also issued numerous alerts and recalls on products from China.[32]

China is second only to the United States in its share of billionaires

Even as corruption weighs on the domestic economy, it also negatively impacts U.S. investment decisions in China. Extensive government approvals are required for even the most routine processes, including those in banking, finance, government procurement, and construction.[33] Corruption is also alleged to be pervasive among senior officials and their family members, who are rarely investigated. When this level of systemic corruption and slack government oversight that produces unsafe products or environmental conditions is coupled with CCP-led financial and economic cronyism in an increasingly SOE-focused economy, it cannot bode well for long-term growth and efficiencies. It can also incite outrage and unrest among the masses.

Inequality and Unrest. "The correct leadership of CCP Central Committee and State Council, local government at all levels were in accordance with the scientific concept of development and building a harmonious socialist society."[34] Notwithstanding the CCP's "correct" leadership, China's inequities continue to widen. The contradictions that define China cannot be more pronounced than in the income inequalities within a so-called communist state. Amazingly, China is second only to the United States in its share of billionaires. Yet while China's economic boom years between 1997 and 2007 birthed many of its billionaires, the share of workers' wages fell from 53 percent of GDP to 40 percent.[35]

Inequalities and other social ills are causing an increase in domestic unrest and strikes. Most of the unrest is linked either directly or indirectly to corruption, pollution, land seizures, or the impression among the rural poor that others are getting rich because they have connections with government officials. Francis Fukuyama suggests that China's growing inequalities may lead to a revolt of the middle class, which finds its aspirations stymied.[36] Regardless of the sources of unrest, they are becoming more frequent, larger, and more violent. It is undoubtedly disturbing for CCP leaders and adds to the growing list of challenges to stability, party control, and sustained economic growth.

Recommended U.S. Courses of Action

In welcoming President Hu Jintao to America in January 2011, President Barack Obama stated:

We have an enormous stake in each other's success. In an interconnected world, in a global economy, nations—including our own—will be more prosperous and more secure when we work together. The United States welcomes China's rise as a strong, prosperous and successful member of the community of nations. Indeed, China's success has brought with it economic benefits for our people as well as yours, and our cooperation on a range of issues has helped advance stability in the Asia Pacific and in the world.[37]

President Obama's comments reflect a pragmatic reality about the interdependent nature of Sino-American relations and the need for continued cooperation. Yet there is a growing number that clamor for more aggressive responses, such as a policy of containment. America's preeminent realist, John Mearsheimer, suggests that "U.S. interests would be best served by slowing Chinese growth rather than accelerating it."[38] Though China's continued growth is not necessarily inevitable, for the United States to actively seek to contain or prevent it would be foolhardy and risks backfiring.[39] Joseph Nye warns that "the best way to make an enemy of China is to treat it like one." In either case, the CCP leadership seems to be doing a good job of stifling growth without American interference.[40]

Rather than pursuing vague confrontational policies that risk cementing an adversarial bilateral relationship, U.S. policymakers would be better served to heed the Chinese proverb "The ox is slow but the earth is patient" and simply bide time while adhering to and encouraging the very broad principles that define America: liberal democracy and free markets. McGregor intimates potential fissures in the CCP's continued grip on power as its ability to transform with rapid change fails to keep pace with the demands of an upwardly mobile and divergent society. Bilateral efforts should focus on the constructive: using tools of statecraft to encourage positive behavior and judiciously using public condemnations, which do little to change undesirable behavior or advance cooperation.

The United States should thus seek cooperative policies that would encourage China's leaders to return to the liberalizing reform efforts of the past as the best path for continued economic growth. This recommendation does not dismiss the numerous imbalances in Sino-American trade and finance arenas that require reconciliation: currency, capital exchange, and trade distortions associated with an undervalued yuan; and legitimate complaints by U.S. manufacturers regarding their trade relations with Chinese firms or government officials, including intellectual property rights protections, China's discriminatory practices, industrial policies to subsidize and protect domestic firms from foreign competition, and health and safety concerns associated with Chinese products.

But these challenges require scalpel-like redress as opposed to cutlass-like generalizations waved about willy-nilly, creating hostile domestic political environments in the United States and China. A negatively charged atmosphere limits maneuverability for those striving to resolve problems while emboldening nationalistic entrenchment on both sides of the Pacific. As such, the United States should pursue adjudication processes available through the WTO or other fora.

Unoccupied building under construction collapsed in Minxing District of Shanghai when flood prevention wall failed

Flickr

Not only does this assist in resolving issues in a relatively nonconfrontational manner, but it also further exposes and impresses upon China the good order obtained through international rule of law.

The U.S.-China Strategic and Economic Dialogue initiated under the George W. Bush administration and continued by President Obama is an excellent example of a useful forum to discuss and advance the bilateral economic issues and challenges listed above. Used appropriately, the dialogue can grow into a meaningful dispute resolution mechanism short of bringing cases before the WTO, or to advance cooperative programs and policies that would facilitate mutually beneficial trade relations between private U.S. and Chinese firms.

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It seems that whenever the United States slips economically, a new chorus of pundits forms, chanting its fall. During the economic downturns of the 1950s, it was the Soviets who were about to "crush" America. During the cyclical declines of the 1990s, a neo-axis of powers was aligned to overtake the United States in the name of Japan and Germany. Today, with chances of a robust recovery encumbered by historically high debt levels, China is proclaimed as the new emerging threat and dominant global power while the United States goes into its proverbial tailspin, taking the liberal market along with it. Alarmists assert myths and half-truths about Chinese economic perils to the West and propose harsh recommendations that would chart a collision course for Sino-American relations.

Yet the United States continues to grow economically and demographically. It continues to provide its citizens with significant wealth, freedoms, and security. In short, one finds the country on an upward, albeit flattening, trajectory. At the same time, China is confronted by a growing list of economic challenges. To make matters worse, China's leaders, bolstered by three decades of success and perceived Western decline, are moving further away from the free-market reforms that guided China's reemergence in the first place. The CCP is unwittingly jeopardizing continued growth and, as a consequence, the very stability that it so desperately desires to retain power. A Chinese society that enriches itself in a stable economic environment is more likely to transition toward peaceful democratic political reforms rather than ones borne out of chaos.

America should thus seek solutions and policies to the mutual benefit of its economic partners, of which China is arguably the most important. The philosophical basis for such an approach is not established on some elusive notion of American benevolence, but rather on the free-market liberal economic concepts and principles that have been the economic and foreign policy bedrock of the United States for generations. It would be unfortunate to depart from these principles because of unfounded fears or negative emotions. The United States has been down that road before, and it should be leery of policy proposals that repeat past mistakes, do not address the real issues of the day, or make a mildly antagonistic Sino-American relationship worse. **JFQ**

NOTES

[1] Don Clark, "Chinese Supercomputer Likely to Prompt Unease in U.S.," *Wall Street Journal Online*, October 28, 2010, available at <http://online.wsj.com/article/SB10001424052702303443904575579070132492654.html#ixzz1DC1uVMFc>.

[2] Secretary of State Hillary Clinton warned the Senate Foreign Relations Committee that "we are in a competition for influence with China; let's put aside the moral, humanitarian, do-good side of what we believe in, and let's just talk straight realpolitik." See Daniel Dombey, "U.S. Struggling to Hold Role as Global Leader, Clinton Says," *Financial Times*, March 3, 2011.

[3] Andrew Kohut, "Friend or Foe? How Americans See China; For the First Time, the Public

Thinks Asia Is More Vital to U.S. Interests Than Europe," *The Wall Street Journal*, January 12, 2011.

[4] See Bruce Bueno de Mesquita and George Downs, "Development and Democracy," *Foreign Affairs* (September–October 2005); or Minxin Pei, *Economic Institutions, Democracy and Development*, Carnegie Paper, World Bank Conference, February 1999.

[5] Paul Krugman, "Competitiveness: A Dangerous Obsession," *Foreign Affairs* (March–April 1994).

[6] Fareed Zakaria, *The Post American World* (New York: W.W. Norton & Co., 2008), 20; and Martin Wolf, *Why Globalization Works* (New Haven: Yale University Press, 2004), 82.

[7] Julie Jiang and Jonathan Sinton, "Overseas Investments by Chinese National Oil Companies," International Energy Agency Information Paper, February 2011. Erica Downs also confirms that "contrary to conventional wisdom, China's NOCs are not merely puppets of the Chinese party-state that are expanding internationally for the sole purpose of assuaging Beijing's concerns about energy security." See Erica S. Downs, "Who's Afraid of China's Oil Companies?" Brookings Institution, available at <www.brookings.edu/~/media/Files/rc/papers/2010/07_china_oil_downs/07_china_oil_downs.pdf>.

[8] The International Energy Agency reports that only a portion of its equity oil was actually shipped to China and was sold to local or international markets instead. See Jiang and Sinton.

[9] Downs.

[10] Jonathan Pollack, "Energy Insecurity with Chinese and American Characteristics," in *China's Energy Strategy*, ed. Gabriel Collins et al. (Annapolis, MD: Naval Institute Press, 2008), 445.

[11] See, for example, Ken Miller's "Coping with China's Financial Power," *Foreign Affairs* (July–August 2010).

[12] China owns $1.16 trillion of a total $14.16 trillion American debt, Japan owns $882.3 billion, and the United Kingdom is the third largest foreign holder of U.S. treasuries at $272.1 billion; U.S. Treasury Department, available at <www.treasury.gov/resource-center/data-chart-center/tic/Documents/mfh.txt>.

[13] Arthur Kroeber, "Five Myths About China's Economy," *The Washington Post*, April 11, 2010; Derek Scissors, "10 China Myths for the New Decade," *Backgrounder*, The Heritage Foundation, January 28, 2010.

[14] Aline van Duyn, Michael Mackenzie, and Nicole Bullock, "U.S. Treasury Sells Negative-Rate Bonds," *Financial Times*, October 26, 2010, available at <www.ft.com/cms/s/0/dfa5ee7c-e08e-11df-abc1-00144feabdc0.html#ixzz1GLwcFMVX>.

[15] Indira A.R. Lakshmanan, "Clinton Urges China to Keep Buying U.S. Treasury Securities," *Bloomberg*, February 22, 2009, available at <www.bloomberg.com/apps/news?pid=newsarchive&sid=apSqGtcNsqSY&refer=news>.

[16] Chinese leaders are concerned about the dollar's staying power in light of the economic decline and corresponding large increases in American deficit spending and debt accumulation. China's Prime Minister Wen Jiabao has expressed concern in the past: "We have lent a huge amount of money to the U.S. Of course we are concerned about the safety of our assets. To be honest, I am definitely a little worried." See Keith Bradsher, "China Grows More Picky About Debt," *The New York Times*, May 20, 2009.

[17] For reasons mentioned above, it seems China will continue to purchase U.S. treasuries. Should China be tempted to dump its current U.S. debt holdings, not only would it be painful for the United States in higher interest rates, but the price China would obtain from such a sale would be deeply discounted, at which time the U.S. Federal Reserve would invariably purchase back the debt at a significantly reduced cost; Derek Scissors, presentation to National War College Chinese field studies class, January 20, 2011.

[18] Daniel Drezner, "Bad Debts," *International Security* 34, no. 2 (Fall 2009).

[19] Paul Krugman, "The Myth of Asia's Miracle," *Foreign Affairs* 73, no. 6 (November–December 1994).

[20] Jonathan D. Spence, *The Search for Modern China* (New York: W.W. Norton & Co., 1999), 619.

[21] Laurence Chandy and Geoffrey Gertz, "Poverty in Numbers: The Changing State of Global Poverty from 2005 to 2015," Policy Brief 2011–01, Brookings Institution, 12, available at <www.brookings.edu/~/media/Files/rc/papers/2011/01_global_poverty_chandy/01_global_poverty_chandy.pdf>.

[22] The title of Stefan Halper's book *The Beijing Consensus: How China's Authoritarian Model Will Dominate the Twenty-First Century* (New York: Basic Books, 2010) is sufficient for understanding his claims.

[23] Scissors, presentation to National War College class.

[24] Compare China's 133 percent of gross domestic product to 28 percent for France, arguably a Western economy with one of biggest state sectors; Jason Dean, Andrew Brown, and Shai Oster, "China's 'State Capitalism' Sparks a Global Backlash," *The Wall Street Journal*, November 16, 2010.

[25] Scissors notes the State Council "sets and re-sets the prices for all key services: utilities and health care, education, and transportation" as well as control over energy and grains (food); Derek Scissors, "Liberalization in Reverse," The Heritage Foundation, May 4, 2009.

[26] In the early 1990s, Beijing held onto the major state-owned enterprises (SOEs) while letting the smaller ones sink or swim. In 1999, the party announced SOEs could only remain in three industries: national security, natural resources, and those that produced public goods and social welfare. This shift resulted in the share of industrial production for SOEs falling from 80 percent in 1999 to 30 percent in 2008.

[27] H. Schneider, "China Has 'Thumbed Nose' at Spirit of Free Trade," *The Washington Post*, January 18, 2011.

[28] Richard Herd, Charles Pigott, and Sam Hill, "China's Financial Sector Reforms," *OECD White Paper*, February 1, 2010, available at <www.oecd.org/officialdocuments/displaydocumentpdf/?cote=eco/wkp(2010)3&doclanguage=en>.

[29] Richard McGregor, *The Party: The Secret World of China's Communist Rulers* (New York: Harper, 2010), 52.

[30] Ibid., 68.

[31] The Chinese government reported that 6 children had been killed and 294,000 sickened (51,900 requiring hospitalization); Wayne Morrison, *China-U.S. Trade Issues* (Washington, DC: Congressional Research Service, January 7, 2011), 28–29.

[32] Ibid.

[33] The PRS Group, Inc., *China Country Report* (update), August 10, 2010, 15.

[34] Statistical Communiqué on Labor and Social Security Development in 2008, National Bureau of Statistics of China, May 22, 2009, available at <www.stats.gov.cn/english/newsandcomingevents/t20090522_402560900.htm>.

[35] Richard McGregor, 56.

[36] Francis Fukuyama, "Is China's Regime Next to Fall?" *The Wall Street Journal*, March 12, 2011.

[37] Barack H. Obama, "Remarks by President Obama and President Hu of the People's Republic of China at Official Arrival Ceremony," January 19, 2011, available at <www.whitehouse.gov/the-press-office/2011/01/19/remarks-president-obama-and-president-hu-peoples-republic-china-official>.

[38] John J. Mearsheimer, "The Future of the American Pacifier," *Foreign Affairs* 80, no. 5 (September–October 2001).

[39] Robert Art, "The United States and the Rise of China: Implications for the Long Haul," *Political Science Quarterly* 125, no. 3 (Fall 2010), 362.

[40] Ibid.