

SERIOUS CHINA: The Rise of China and EU Implications

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My topic is the rise of China and its implications for the EU. My thesis is that China's rapid emergence as a major economic and political force is the most significant development of our era, and viewed against the backdrop of sustained underperforming economies in the EU, as well as the U.S. and Japan, the consequences of the rise of China is even more pronounced.

I would like to touch on four themes in my remarks: First, some historical context for the rise of China. Second, a discussion of China's economy and internal politics. Third, comments on China's foreign policy. And fourth, the implications for Europe.

THE HISTORICAL CONTEXT

I MENTIONED THE backdrop of economic performance of the US, EU, and Japan, but the more significant backdrop is that of China's history. China spent 30 years, from 1949-79, as perhaps the worst performing economy in the world, and it has spent the subsequent 30-plus years as perhaps the best performing economy in the world.

If we looked at China at almost any time in the century before the 1979 reforms, we would probably see very little basis for optimism. As China made its journey from Imperial decline and collapse, to the rise of Warlords, to the Republic of China, to Japanese invasion, to the Communist revolution and subsequent turmoil, China has seen only brief moments of hope across an extended period of time.

The world saw many different Chinas over that century: impoverished China, irrelevant China, brutalized China, angry China, defiant China, proud China, humiliated China, convulsed China, self-destructive China, revanchist China, and fragmented China.

But today we see a China no one alive today has ever seen: successful China, consequential China, serious China. China has climbed out of a century of misery and is building a modern nation, with the fastest-growing economy in the world, a burgeoning middle class, more university graduates than ever, growing international political reach, and the most powerful military ever.

CHINA'S ECONOMY AND DOMESTIC POLITICS

WE KNOW THAT China has about 12% of global GDP and that should pass 15% this decade. To put that in a European context, this means that China grows by an entire France about every 4-5 years. Or to look at some different figures, China's reserves are about equal to the capitalization of the entire London Stock Exchange.

This success is not to suggest that China is a country without challenges because China certainly has its share. As a developing nation, up to two-thirds of its citizens still live in very modest rural circumstances with limited access to education, employment, or health care. China also faces other challenges from environmental degradation and demographics to corruption and all of the problems of single-party rule. These challenges give rise to core questions about the sustainability of the Chinese model. Can economic growth stay on track? Will socio-politico stability be maintained?

These two questions alone have resulted in a vast literature of analysis and conjecture and either could command a lecture on its own, but let me take a few minutes to tackle each.

Regarding economic growth: China faces many macroeconomic challenges such as investment distortions, inefficiencies of SOEs, over-reliance on exports, and lack of competition and transparency. These are not merely my views, these comments will be found in most speeches by senior Chinese leaders. Despite these challenges, I believe China will be able to sustain very high rates of economic growth for some time to come. I see two positive trends that will govern economic performance: First, China will be able to take advantage of its developing nation attributes, driving improvements in output through marginal improvements in labour productivity. Second, the new China leadership is fixed on the need to keep economic growth on track. They have not yet promulgated their economic agenda, but it is clear they realize a status quo administration is not acceptable.

Regarding socio-political issues, I see a high degree of stability in the system for the near term. China might be

the only country in the world where the social contract is still being written. Questions long-settled in the West are still fresh in China, such as what are the government's obligations to its citizens? What rights do citizens have against their own government? Under what circumstances should citizens be able to change or even to criticize their government? In my view, these questions need to be addressed at some point. However, in the near term China is able to maintain social stability through high rates of economic growth and by gradual liberalization of personal space. It also has an effective security apparatus. Almost unnoticed, China has made the transition from totalitarian to authoritarian. Over the long run, this might make expectation management more difficult, but in the near-term it provides for a high degree of social stability.

FOREIGN POLICY

CHINA HAS AN extensive history of success with statecraft over its 5000 year history, but for most of that period statecraft usually related only to internal issues of governance, the challenges of administering a continent. For most of China's history, foreign policy simply meant border state management. There were times when this evolved into a more elaborate tributary state system and there were times when China had to deal with stronger foreign powers, but until recent years China could not be said to participate in an international political system. This is a new era for China in which it must participate in an international system, the members of which neither seek to dominate China nor to be dominated by it.

This is a new era for Europe as well. It is the first time since the Mongols that a power outside the western state system has the capabilities to shape outcomes in that system. This also means it is a new era for the U.S., though that is outside the scope of today's remarks.

As China grows in its international role, the world has witnessed increased assertiveness and even occasional truculence, with China involved in more territorial disputes than any other country in the world. This tendency, combined with a sustained military build-up and a lack of transparency and control in its military gives rise to questions about China's long-term goals in Asia and its ability

to work within an international system.

The good news is that China does not subscribe to a global ideology. There is no new Cold War. The challenge is that China appears to follow policies in the region that seem to work against its own interests. This suggests that foreign policy decision-makers lack the mechanism for advanced cost-benefit analysis, that the concept of enlightened self-interest is limited, and that much of China's current regional policies are determined by historical views of threat and tribute. Thus the paradox of China's foreign policy is that it seeks externally to promote reach and influence yet it is constrained by a domestic political environment that sometimes favours actions that undermine that same reach and influence. My analysis here is less optimistic than it is regarding economic success or domestic stability.

THE ROLE OF EUROPE

IN MY VIEW, Europe has an important contribution to make to this situation. China, and the U.S., will both benefit if Europe improves its reach regarding China. Also, in my view, Europe is seriously underweight in Asia. On a note of humility as a guest, let me close with four observations as to how Europe can play a more effective role..

First, economic success at home. It is difficult for China to take Europe seriously if it is not perceived as managing its own affairs intelligently. This means solving EMU problems and getting back to economic growth. Lest anyone think I am not a Europhile I readily admit the U.S. has essentially the same set of problems. We should also note that an EU-US Free Trade Agreement on an open architecture basis will not just help each market vis-à-vis the other, it will also help establish global technical and regulatory standards, helping China move the right way.

Second, less internal and more external orientation. The enormous success of the EU came through two historical triumphs - the Common Market and the integration of the Newly Independent States. Both of these were European-only policy initiatives. The future of the EU will not be the extent to which it is internally focused, but the ability to move beyond that to be primarily externally focused. My core suggestion to friends in Europe is the

situation requires a sharp rebalancing of attention toward Asia.

Third, engage with China not by engaging China alone, but also by engaging the system in which China operates. The EU needs to do more with China, but also with its near abroad and China's near abroad. Part of engagement with China is engagement with India, Indonesia, Japan, and the Philippines and Kazakhstan.

Fourth, technology and the size of the populations involved mean we need to think about order of magnitude shifts, not marginal or percentage shifts.

Let me take these four points and close with a few illustrations.

For example, in general education, what if the top three universities in each major European country established campuses in China, India, or elsewhere? If that is too elaborate, how much would it cost to take the core courses of a university and have them put into videos in Chinese and other language?

Similarly, NATO members would normally think about a handful of soldiers from the Philippines or Indonesia attending a staff course for a few weeks. What about 100 officers from each of these countries attending Nato courses or even 1000? What about the great military schools of Europe opening up summer schools in Asia for training purposes?

What about European media? I just caused some heartburn for a friend at the New York Times a while back when we discussed the Metro section of the paper. To my question, he told me that the Times had some 100-150 professionals in that section - journalists, photographers, and editors - all covering the news of New York City. My question to him was: what would happen if the NYT closed its Metro section and instead assigned 100-150 professionals to China and then put out at least some of its product in Chinese?

You can understand why he had heartburn as it was a somewhat radical suggestion – completely impractical but designed to make a point. Why are the great media

companies of Europe likewise so underweight in China? Can they not put more resources into China coverage and publish some material in Chinese? I am also pleased to relate that as of last year, the NYT does regularly publish Chinese-language material.

In conclusion, thank you for letting me briefly touch on the four themes – history, economic and social issues, foreign policy, and the role of the EU. I mentioned early in my remarks we are seeing, for the first time, a serious China. We need to make sure there is also a serious Europe.

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