



China's Bad Bet Against America

By Joseph S. Nye, Jr.

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China-US relations are, once again, in a downswing. China objected to President Barack Obama's receiving the Dalai Lama in the White House, as well as to the administration's arms sales to Taiwan. There was ample precedent for both decisions, but some Chinese leaders expected Obama to be more sensitive to what China sees as its "core interests" in national unity.

Things were not supposed to turn out this way. A year ago, the Obama administration made major efforts to reach out to China. Secretary of State Hillary Clinton referred to "being in the same boat," and that China and the United States would "rise and fall together." Treasury Secretary Timothy Geithner said he spent more time consulting his Chinese counterparts than those in any other country. Some observers even referred to a US-Chinese "G2" that would manage the world economy.

The G2 idea was always foolish. Europe has a larger economy than both the US and China, and Japan's economy is currently about the same size as China's. Their participation in the solution of global problems will be essential. Nonetheless, growing US-Chinese cooperation within the G20 last year was a positive sign of bilateral as well as multilateral cooperation.

Whatever the concerns regarding the recent events related to the Dalai Lama and Taiwan, it is important to note that the deterioration in US-Chinese relations began beforehand.

Many US congressmen, for example, complain that American jobs are being destroyed by China's intervention in currency markets to maintain an artificially low value for the yuan.

A second issue was China's decision not to cooperate at the United Nations conference on global climate change in Copenhagen last December. Not only did China resist measures that had been under negotiation for the preceding year, but Prime Minister Wen Jiabao's decision to send a low-level official to meet with and point a finger at Obama was downright insulting.

China behaved similarly when the five permanent members of the U.N. Security Council (plus Germany) met to discuss sanctions against Iran for violations of its obligations

to the International Atomic Energy Agency. Again, China sent a low-ranking official.

What happened to those promising early signs of cooperation? Two reasons for the change in Chinese behavior – seemingly inconsistent at first glance, but in fact perhaps mutually reinforcing – seem possible.

First, a political transition is expected in 2012, and, in a period of rising nationalism, no Chinese leader wants to look softer than his rivals. This helps to explain the recent crackdowns in Tibet and Xingjiang, as well as the detention of human rights lawyers.

In addition, China may be approaching an economic transition. Some Chinese argue that anything less than 8 percent growth would be inadequate to ensure sufficient job creation and fend off social instability. But, as America's savings rate begins to rise, China's export-led growth model, which has promoted employment in China at the cost of global trade imbalances, may no longer be possible. If China responds to entreaties to revalue the yuan, it may need to look tough on other issues to appease nationalist sentiment.

The second cause of China's recent behavior could be hubris and overconfidence. China is justly proud of its success in emerging from the world recession with a high rate of economic growth. It blames the US for producing the recession, and now holds some \$2 trillion in foreign-exchange reserves.

Many Chinese believe that this represents a shift in the global balance of power, and that China should be less deferential to other countries, including the US. Certain Chinese scholars are now writing about the decline of the US, with one identifying the year 2000 as the peak of US power.

This overconfidence in foreign policy, combined with insecurity in domestic affairs, may combine to explain the change in Chinese behavior in the latter part of 2009. If so, China is making a serious miscalculation.

First, the US is not in decline. Americans and others have been predicting decline regularly over the years: after the Soviets launched Sputnik in 1957; again when Nixon closed the gold window in 1971; and when the US rust-belt economy seemed to be overtaken by Japanese manufacturers in the 1980s.

But when one looks at the underlying strength of the US economy, it is not surprising that the World Economic Forum ranks the US second (just behind Switzerland) among the most competitive, while China ranks some 30 places below.

Second, the fact that China holds so many dollars is not a true source of power, because the interdependence in the economic relationship is symmetrical. True, if China dumped its dollars on world markets, it could bring the US economy to

its knees, but in doing so it would bring itself to its ankles. China would not only lose the value of its dollar reserves, but would suffer major unemployment. When interdependence is balanced, it does not constitute a source of power.

Third, despite Chinese complaints, the dollar is likely to remain the major global reserve currency, owing to the depth and breadth of US capital markets, which China cannot match without making the yuan fully convertible and reforming its banking system.

Finally, China has miscalculated by violating the wisdom of Deng Xiaoping, who advised that China should proceed cautiously and ``keep its light under a basket.”

As a senior Asian statesman told me recently, Deng would never have made this mistake. If Deng were in charge today, he would lead China back to the cooperative relations with the US that marked early 2009.

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