

# Introduction: Taking Stock of China's Rise

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## **Growing Interest and Concern**

China's steady rise to global prominence continues to amaze and even alarm, and it increasingly alters the way governments and citizens must look at their world. The country's extraordinary emergence will continue to be one of the most significant long-term foreign and economic policy challenges for every country, and especially for the United States, even as pressing and near-term problems and opportunities in U.S.-China relations arise with increasing regularity. This situation demands an informed and judicious response—globally, regionally, and in our own communities.

With that need in mind, our project culminated its first year with the publication of *China: The Balance Sheet: What the World Needs to Know Now about the Emerging Superpower* in April 2006. We examined and offered broad policy guidance on four principal areas related to China's rising influence in world affairs: China's domestic economic situation, domestic sociopolitical transformation, role in the international economic system, and foreign and security policy. Confirming our belief that there is an enormous and pressing interest in comprehensive, authoritative, and objective analysis about developments in China, *China: The Balance Sheet* gained widespread attention and praise from policymakers, specialists, and the interested public.

That volume concluded that China presents Americans with an increasingly complex mix of challenges and benefits: neither friend nor foe, neither ally nor enemy. We continue to believe the areas of common interest between the United States and China are more prevalent than the issues that divide the two countries. That said, we readily recognize areas of growing concern—China's lack of cooperation on certain economic and trade issues, military buildup (particularly opposite Taiwan), relationships with unsavory regimes, and persistent human rights problems—which will continue to raise unease and alarm in American circles and complicate the emergence of a more stable and constructive

relationship. Similar concerns about China are expressed elsewhere around the world, from Asia to Europe to Africa. Under these circumstances, U.S.-China ties remain subject to significant disagreements, mistrust, miscalculation, and even confrontation and potential military conflict.

We remain concerned that the United States—both in the public and private sectors—still has much work ahead to forge an informed and effective consensus in response to the critical challenges and opportunities China presents to American interests across a range of fields: economic, political, diplomatic, technological, and military. All the while, the U.S.-China relationship becomes increasingly complex and strategic in character.

Now more than ever the world needs to know, understand, and carefully respond to China's remarkable transformation at home and its growing role across the globe.

## Economic Developments

China's ongoing transformation, both at home and as a growing world power, has witnessed remarkable economic developments over the past year.

- China's economy grew at more than 10 percent in 2006, and the country now stands as the world's fourth-largest economy and third-largest trading nation.
- China's foreign exchange reserves surpassed \$1.2 trillion in the first quarter of 2007, far eclipsing Japan as the world's number one holder of official reserves.
- China was the world's largest emerging market recipient of foreign direct investment (FDI) in 2006, and number four globally, with almost \$70 billion of utilized FDI for 2006. Hong Kong, the British Virgin Islands, Japan, South Korea, and the United States were the top five sources of FDI for China in 2006; U.S. sources contributed just under \$3 billion in utilized FDI to China in that year.
- Over 2005–2006, the Chinese renminbi (RMB) appreciated against the U.S. dollar by about 6.5 percent. The RMB has actually *weakened* on a trade-weighted basis, however, and Beijing continued to intervene massively in the foreign exchange market to prevent the currency from rising more substantially. As a result, China's global current account surplus is estimated to have reached \$240 billion last year, far and away the world's largest, and its global trade surplus has doubled again in the first quarter of 2007.
- The U.S. bilateral trade deficit with China surpassed \$230 billion in 2006, accounting for more than a quarter of America's global trade deficit.
- In part sparked by trade and currency concerns, the United States and China launched an official Strategic Economic Dialogue in December 2006, an unprecedented ministerial-level effort to engage across a range of economic challenges—including trade imbalances, intellectual property rights violations, transparent financial markets, and bolstering China's ability to deliver public goods such as health care and social security and expand domestic consumption.

- Reflective of these growing economic concerns, in April 2007, the United States levied new import tariffs on Chinese coated paper to compensate for alleged Chinese government subsidization of such exports. It was the first time since the 1980s that Washington levied countervailing duties on exports from a “nonmarket” economy. Later in the month, the United States filed two formal requests to launch consultations within the World Trade Organization (WTO) to address Chinese intellectual property rights violations on books, films, and music. Congress is considering new initiatives vis-à-vis trade with China, especially to try to force more rapid appreciation of the RMB.

## Sociopolitical Developments

On China’s home front, the country’s leadership continued to grapple with the pluses and minuses of rapid economic and social change.

- The number of the country’s Internet users rose to some 137 million by the end of 2006, a number that will grow to nearly 200 million by 2010. At once a crucial factor for China’s modernization, as well as a channel to access vast amounts of largely unfiltered information, Internet use is guardedly permitted by Chinese authorities who employ sophisticated communications monitoring and filtering protocols to block access to sites considered “harmful” to the regime.
- China’s anticorruption efforts appeared to pick up pace in 2006, though problems persist. By early 2007, government sources revealed that 9 provincial and ministerial-level officials were among the 825 senior officials convicted of corruption. In September 2006, in one of the highest-profile cases to date, Shanghai party chief and Central Committee member Chen Liangyu—at the time thought to be one of the country’s rising political stars—was fired and arrested for corruption related to the city’s pension fund and shady real estate deals. Nevertheless, according to Transparency International, in 2006, China scored a 3.3 on a scale of 1 to 10, with 10 being least corrupt—ranking 70th out of 163 countries surveyed.
- In 2006, according to Ministry of Public Security sources, “public order disturbances” rose by 6.6 percent over 2005, to 87,000—an average of some 240 reported incidents a day. In March 2007, a large riot protesting increased fees for public transportation resulted in the death of one person and involved some 20,000 farmers and 1,700 police.
- Environmental problems persist in spite of heightened official rhetoric and investments in greener energy technologies. China failed to meet its target of improving energy efficiency by about 4 percent in 2006 and was unable to meet its goals of reducing sulfur dioxide emissions. China will surpass the United States as the world’s largest emitter of greenhouse gases in the next year or two.
- In promoting the notion of achieving a “harmonious society,” Chinese leaders increasingly acknowledge the positive role that civil society organizations—

such as nongovernmental organizations (NGOs) and places of worship—can play, as long as they are not deemed “political” or seen as critical of the party. Official statistics state there are approximately 3 million NGOs in China, but only one out of every 100 is able to receive official registration.

- In the run-up to the 2008 Beijing Olympics, Chinese government authorities announced in 2006 that foreign media would be permitted unfettered access to citizens and organizations to report on developments in China. Despite this step, Reporters Without Borders ranked China 163 out of 168 countries for its lack of press freedom in 2006; 31 Chinese journalists were jailed in 2006.
- Over the year ahead, China's senior leadership will undergo some change, most prominently during the upcoming 17th Chinese Communist Party Congress scheduled for the fall 2007. Such younger leaders as Li Keqiang, an economist and party secretary of Liaoning Province; Zhang Baoshun, an economist and governor of Shanxi Province; Xi Jinping, former Zhejiang party chief and new mayor of Shanghai; and Li Yuanchao, a lawyer and party secretary of Jiangsu Province are considered front runners for elevation to the central leadership. The current team of Hu Jintao (party chief, president, and head of the Central Military Commission) and Wen Jiabao (premier and likely to rise to the number two position in the party) will remain in place.

## Global Developments

China's growing impact on the international political, economic, and security scene continued unabated, raising new questions about its role in global markets, diplomatic circles, and security affairs.

- China is increasingly integrated in the global economic and financial system and increasingly dependent on its stability and success. Given its large size, rapid growth, and extraordinary openness to international trade and investment, China is a critical driver behind global economic growth.
- China's imports and exports are equivalent to nearly 70 percent of the country's GDP, an extremely high proportion that is more than twice that of the United States and a key indicator of its dependence on the global trading system.
- Beijing recently announced its intention to leverage its massive foreign reserves to realize greater returns on its overseas investments. China's FDI outflows increased by 32 percent in 2006 to \$16.1 billion and will continue to grow substantially in the years ahead.
- Internationally, China is a member of more than 130 intergovernmental organizations and a signatory to more than 250 multilateral treaties. China has taken the lead to build and strengthen a range of multilateral cooperative initiatives, including the Shanghai Cooperation Organization, the Forum on China-Africa Cooperation, and a free-trade arrangement between China and its neighbors in the Association of Southeast Asian Nations (ASEAN).

- China accounted for almost one-third of world oil consumption growth between 2004 and 2006 and is now the world's second-largest consumer of energy. Chinese corporations have deepened their investments in and access to natural resource extraction around the world, including such controversial locales as Angola, Sudan, Zimbabwe, Burma, and Iran.
- Beijing moved more assertively to unhinge the nuclear stalemate with North Korea. In response to North Korea's missile and nuclear device tests in 2006, China supported United Nations Security Council sanctions on Pyongyang, a remarkable move against its erstwhile ally reflecting Beijing's extraordinary frustration with North Korea. Beijing continued to host the six-party talks, which led to an agreement on February 13, 2007, outlining an implementation schedule for comprehensive settlement of security issues related to the Korean Peninsula.
- In December 2006, China announced deployment of the J-10 fighter jet, its first indigenously developed fourth-generation advanced fighter aircraft. In January 2007, China carried out a successful test of an antisatellite weapon. In March 2007, the Chinese military received its largest budget increase in five years—a 17.8 percent boost. The official Chinese defense budget now stands at about RMB 350 billion, or roughly \$45 billion at current exchange rates (although both the 2007 percentage increase and total budget figure have been subject to considerable question by outside observers). These and other developments over the past year have raised anew the persistent concerns in the United States and Asia about the scale and intent of the country's rapid military modernization drive.
- As of early 2007, China contributes more than 1,800 civilian police, military observers, and troops to 12 United Nations peacekeeping missions, mostly in Africa.

## **Digging Deeper into Critical Topics**

Given these critical developments, it is clearly in the interest of the United States, China, and others around the world to avoid a devolution into confrontation and to see a China emerge in the future that is more stable, open, and constructive in its relations with the world and the international system. The stakes in realizing those aims are enormously high and exceedingly complex. Not least, meeting those aims will require a significant change in the mindsets and comprehension of leaders and citizens in the United States and China. Hence the motivation for our project: to deepen understanding of China's rise and its implications for U.S. interests and to determine ways forward toward a more stable and mutually beneficial relationship.

Now into the second major phase of our joint project, for 2006–2007 we are delving deeper into a range of specific topics of concern to the United States. The collection of nine in-depth studies included in this compendium takes up

questions that are central to China's economic, social, and political development, to its foreign policy, and to U.S.-China relations.

The collection begins with two critical issues that are not only major economic and development challenges facing China but sources of potential frictions in U.S.-China relations as well. Nicholas R. Lardy offers a timely examination of China's domestic economic situation and makes the case for China to bolster its longer-term domestic consumption patterns—for example, through improvements in China's health care and social welfare systems. Dan Rosen and Trevor Houser take on another key development challenge for China—access to sufficient energy resources—and extensively detail the country's energy needs and the impact this quest will have for China's domestic and foreign policy.

The second set of studies in this collection assesses a number of important domestic developments that have been the subject of interest and controversy in U.S.-China relations. These studies delve deeper into some of the remarkable sociopolitical changes that are sweeping over China and examine the responses of the Chinese government and citizenry. In the first of these, Carl Minzner addresses China's rising incidence of unrest and assesses its implications for political and social stability in China. In the following study, James Mulvenon carefully examines the sensitive topic of Internet censorship in China, offering insights into the government's methods and the ability of the Chinese to circumvent them. In a third study, Jamie Horsley details and analyzes the range of steps taken by the Chinese government and employed by Chinese citizens to foster the rule of law, good governance, and official accountability.

This collection of in-depth research and analyses concludes with several different takes on China's most important foreign relationships, all of which are having an increasingly important impact on American interests. Derek J. Mitchell authors two papers—one on China's relations with the developing world and another on China-Russia relations—and is joined by Chietigj Bajpae in a third study on China-India relations. C. Fred Bergsten rounds out this collection of studies with an examination of China's increasingly active participation in Asian economic multilateralism and the impact China's deepening integration in the regional economy will have on the United States.

## Looking Ahead

In spite of the diversity of the subject matter, the studies included in this second stage of our *China: The Balance Sheet* project share several common themes and guidelines for the future U.S. relationship with China. As the two most consequential powers of the future, China and the United States will find themselves increasingly intertwined around the most critical issues of global and regional importance—including global political and economic governance, energy security, poverty alleviation, global health, nonproliferation, transnational terrorism, crime, and environmental degradation. To meet the demand for cooperation on these issues requires an even deeper, well-informed, and sustained effort to advance understanding in the United States about China's rise and to

build from that knowledge to craft a more effective strategy for U.S.-China relations.

These papers, and the conference held in May 2007 to consider them, are our project's latest contribution to meet those needs. As we enter the third phase of the project in 2007–2008, we will continually update our dedicated Web site (<http://www.chinabalancesheet.org>) and will issue in early 2008 an entirely revised and updated version of our flagship publication—*China: The Balance Sheet: What the World Needs to Know Now about the Emerging Superpower*. The 2008 edition of our book will feature new data and analysis on China and will place an even greater emphasis on policy guidance and recommendations. We aim to help frame the discussion and contribute usefully to the development of U.S. policy and U.S.-China relations during a critical election year in the United States.