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The Economic and Strategic Rise of China and India
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Featuring:

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Well it's a pleasure to be here. As Albert just said we have at FPA put a great deal of effort into the Great Decisions Series. We try very hard to present issues as objectively as we can, and what we try to do in the editorial board in the spring of the year before it's published is to try to identify the issues which we think are going to be the critical issues in the year or two ahead. And a number of you I'm sure are in discussion groups that use Great Decisions, but Noel Tief and the entire board is firmly behind the idea that we want to broaden the audience for Great Decisions. So we're delighted that Noel has been invited to hand Great Decisions to the debaters at tonight's debate in Florida.

Anyway, I wanted to start tonight talking about Asia with a story of the tiger walking through the jungle, and the tiger first came to a mouse and he said to the mouse "Mr. Mouse, can you tell me who is the strongest animal in the jungle?" And the mouse said "Oh, Mr. Tiger, there's no question you are the strongest animal in the jungle." So the tiger was quite pleased with himself, and we went a little farther into the jungle and he came to a gazelle, and it was a young female gazelle, and he was trying to decide whether to have her for breakfast or whether to ask her the same question, so he said "Miss Gazelle, could you tell me who is the strongest animal in the jungle?" And she was quivering and she said "oh, Mr. Tiger, there's no question about it. You're the strongest animal in the jungle. And, in addition, you're very handsome." So he was very pleased with himself and he went a little bit farther and he came into a clearing in the jungle, and there was this old elephant there who had a torn ear and she was blowing dust on herself and looked rather ratty, and so he went up to her and he said "Mrs. Elephant, could you tell me who is the strongest animal in the jungle?" And she just reached down with her trunk,

picked him up, and threw him against a tree and almost broke his back. So he was a little discomfited and sort of just brushed himself off and he turned to her and said “Don’t get so excited just because you don’t know the answer!”

Now, I think in many ways the United States is like that tiger. I think that there are very big changes ahead that the United States isn’t planning for. Certainly if one reads the defense planning guidance for the U.S. Government or major national security statements which have been put out in the last few years by the current administration they are really not cognizant of the fundamental changes which are ahead. So what I’m going to try to do tonight is give you a sense of how the economic vibrancy in Asia is likely to affect us; how it’s effecting change inside Asia but also how it’s likely to affect the United States.

What I’d like to do is just mention the three broad themes. The book that Elbrun mentioned of *The Rise of China and India* is upstairs if you’re interested to go into the details. It has lots of tables and some of you may not find that congenial but it provides the statistical backup for what I’m about to say. Also, in the handout that I’ve given you, which you are welcome to take home if you’d like obviously, you can get a preliminary idea of some of the issues I’m going to raise. But I basically have three broad themes. The first is that the rise of China and India is very significant, but its significance needs to be put in the context of the relative decline or stagnation of the Pacific Rim countries. If we had this discussion fifteen years ago the most popular book by an American author on Asia was Ezra Vogel’s book *Japan Is #1*. It focuses all on Japan; the bubble had burst in the Japanese real estate market but Japan still had a GDP that was five times China’s and it was without exception the leading economy in Asia, and it was certainly seen by many as a major threat to the United States. In the same way the dynamism of the smaller countries in Asia – South Korea, Taiwan, Hong Kong, Singapore, and then subsequently the ones in Southeast Asia – led to large number of books and articles on the Four Tigers, et cetera. All of us have been through that; but the first and really fundamental point that I want to make is that the rise of China and India are significant in and of themselves but they would have been much less noticeable if Japan had recovered quickly from its crash; if South Korea, Taiwan, and the Ascion countries in southeast Asia didn’t run into problems themselves.

My second major point is that China has changed its own strategy for dealing inside East Asia in a very significant way. It’s changed it militarily, it’s changed it diplomatically, and it’s changed it economically. Now when we get into the tables and we get into discussion I’ll give you more details, but in the late 1980’s China was taking a relatively pugilistic approach to dealing with its neighbors. When it wanted to move into the Skradley Islands it simply attacked the Vietnamese who were there and took over a place called Mischief Reef in 1988. When they were having trouble with the Taiwanese they fired some missiles off the Taiwan coast at the time of the election of 1996. And in general took a relatively harsh view towards its neighbors. That they have changed dramatically, and we can go into some of the reasons for it, but they have also dramatically changed the way in which they are dealing with their neighbors economically. If you looked at China in the

early 90's, the major view was this was a Marxist or Socialist economy going through transformation, the question was how quickly could it reform? But it was basically an inward-looking society and there were isolated pockets of modernization along the east coast. But certainly the dynamism and the modernization that we're all familiar with in China today had not been launched, and certainly at that stage China was not an open society. However by the early turn of the century, in 2000-2001, China becomes much more confident, opens itself dramatically to trade, and even offers a free trade agreement to all the countries of Southeast Asia, and actually moves ahead of Japan in terms of openness to countries in the region. And this has had an enormous effect within the region, and again we could get into this if you'd like.

Now, my third major theme is that the U.S. is headed for trouble ahead. The reason I mentioned the story of the tiger is that a country that has the world's largest trade deficit, is the world's largest debtor, has run a budget deficit for twenty-nine of the last thirty years, and has a very serious set of problems with its financial markets, is not a country who can necessarily tell others how to behave. So there's an enormous disconnect between the rhetoric and the assumptions of much of the foreign policy community and the economic underpinnings of what's happening in the U.S. to debt. And that's going to have a fundamental effect on the region. Secondly, Japan is still having problems. The Japanese economy is still twice the size of the Chinese economy, but Japan's problems are significant enough that it's not likely to move quickly into leadership again in the region, and China for a number of reasons has the diplomatic edge in negotiating. That leaves the smaller countries of the region – South Korea, Taiwan, Southeast Asia – looking for a protector, a guarantor. And that leads us to our conclusion, which is that there are two aspiring nations in the region, that where the political elites support major power status, where they want to play a larger role, where they have dynamic economies, and where they definitely want to move top center stage. And those two countries are China and India. So those are the major themes that we're going to turn to/

I'd like to just go quickly through some of the tables so you get a sense for the magnitudes. I'm not going to try to go into every detail, but it will give you an idea of what's involved. The first table looks at –are there extra tables? Anyway. The first total is for total gross domestic product. Again, during questions I'll be glad to go into any details you'd like, but the important thing to note here is that in 19980 China has a gross national product about like Indonesia's. So what we're talking about is just an enormous surge between 1980 and today; an enormous transformation of the region. The other countries are important; though India's economy is large India's economy is about the size of South Korea. I'll mention also, just to put these things in context, that now that the Soviet Union has fallen apart and we're talking about Russia, Russia's GDP is roughly the size of Belgium and Holland's together. So Russia is a very strange country: it's a nuclear superpower but a tiny economy. That of course is changing with oil and gas prices soaring, but whether they will stay high is something we can discuss.

Now, the second table is called The Double Dip Recession in Asia, and this is the key element that I'm talking about regarding the failure of the smaller countries in Asia to recover from the '97 recession. And if you look at that recovery line from '98-'99, if the Asian countries had been on that trajectory up, then the very large surge of foreign direct investment that went into China would have been more equally distributed within the region; China would have grown more slowly and the rest of the countries in the region would have grown more quickly. So we can discuss that in greater detail if you'd like. Now, in terms of restructuring, if you have an economic bent I'm glad to talk about the different restructuring problems in Asia. I am a deep skeptic of some of the arguments put forward by the *New York Times'* leading columnist on economics, where he has lumped all the countries of Asia together. It shows, I think, how little he knows about Asia. The countries in Asia each have distinct problems and I'm glad to go into them, but one can't categorize them all together.

The next table is the total GDP of the Asian powers. The reason why this is important is to get a sense again for what I mentioned earlier: for the fact that Russia is a nuclear superpower but is not an economic superpower and a country like South Korea, if it chooses to go ahead with a modernization and transformation of its military, can do many things that larger states have often been soon to do in the past.

Now the next table says Impact of Economic Alignments. Again I can go into this during questions, but what's important about that is to note that trade is shifting dramatically within Asia. If we'd had this talk five years ago the U.S. was the principal trading partner of almost every country in East Asia; today China is the principal trading partner for those same countries. Now the U.S. is still absolutely critical, and the irony is that the U.S. is the leading trading partner for China. So the other countries of Asia are trading to China; China is still very much focused on the U.S. Now the other element, and it's one of the themes that I'll try to bring out later as we discuss these issues, is that China's trade with the U.S. is growing at 30% a year, and China's dependence on trade -- in other words, the percent of its total GDP in trade -- is actually growing. So this is clearly an unsustainable situation as well. The U.S. can't absorb Chinese exports at that rate on a continuing basis. So when you read, there's a wonderful fluff piece in the current *Atlantic*; for those of you who are followers of the Lehrer show you have heard that piece promoted last night. I won't mention the author, but it's total fluff. China isn't going to be able to continue on strategy; China's going to have to change; they're going to have to increase their internal consumption; they're going to have to change the direction of their trade and big changes are ahead in that regard as well.

Now let me just end by mentioning the issue of Asian exports. This happens to be a UN table and therefore it has political euphemisms in it, so instead of China being highlighted China is listed under developing countries. The reason why this table is important is to get you to notice that if you were in southeast Asia and you were trying to decide where you wanted to export products there has been some modest increase in exports to the U.S. and Canada, to Europe and to Japan after '97, but the

big surge has been to China. So if you were a young person in Southeast Asia and you were trying to decide what languages do I want to learn, what contacts I want to build up, where do I want to focus my attention, it would be pretty simple to answer that question.

The next table deals with foreign direct investment. I won't go into that except to note this enormous sort of triangular shaped hat there. For those of you who are really China aficionados this is called the round-tripping event. This is when China allowed wealthy Chinese to take their money out of China and put it in Hong Kong. They left it there for six weeks and then they brought it back. They wanted to make sure they could put it in foreign banks. And so you see this big surge into Hong Kong and then all the money is taken out.

The regional institutions we can discuss. The critical element there is that China has gone from being a country which was seen as challenging and potentially a problem to a country that is helping them solve problems, and I'll try to explain that.

Now in terms of the strategic issues which I want to end on, so two more tables and you'll see the ability to sustain the rise to great power status. My argument is that Japan, China and India can all do that, but I think there's no question that China and India will do that; it's uncertain what the Japanese response will be.

Now in terms of strategic options, and this is where I want to end, I'm saying that there are essentially four very broad strategic options that could be pursued in Asia. The current administration is saying that U.S. dominance will be there indefinitely. There are some of the leading advisors to Democratic candidates, like Joseph Nye who has written a book called *Bound to Lead*, implying this is going to go on for a long time. My view is that it will not go on for a long time; there are going to be significant adjustments ahead, and I suggest three alternatives. One is some kind of leadership from the U.S., Japan, and India together in some kind of informal grouping. I don't think an alliance is very likely but I think some kind of informal groupings will be. Where the region is heading, unless a major intervention occurs, is essentially Chinese informal pre-eminence. The Chinese already dominate Burma, Cambodia, Laos and Vietnam, and the other countries of Southeast Asia are trying to decide where to go. Taiwan is also deeply torn; its economic future is clearly with the mainland but the Taiwanese want a greater autonomy. A third alternative, which is being promoted inside Asia, is called the Asian concert of powers. For those of you who are aficionados of Henry Kissinger you may know that he wrote his PhD dissertation on the Congress of Vienna and the concert of powers in Europe after 1815. There's a lot of discussion about whether Asia will be able to pursue that kind of direction itself. I think there are some pros and cons to that; I'm not convinced that it's a workable solution for everyone.

So why don't I end there and turn to your questions.