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**Opening Remarks:**

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**The Zhu Rongji Era:**

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**Third Plenum Reforms: Achievements and Challenges:**

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**U.S.-China Trade and Investment: Opportunities and Issues:**

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## P R O C E E D I N G S

MR. LI: My name is Cheng Li. I'm director and senior fellow at the John L. Thornton China Center here at Brookings. First I want to thank you all for braving the cold to attend today's conference. This is the China Center's first event in the new year, so Happy New Year. And what an auspicious beginning in the year as we launch the publication of the second English volume of *Zhu Rongji: On the Record*.

The second volume explores Premier Zhu Rongji's experiences as a very respected economic technocrat, assisting Deng Xiaoping from 1998 to 2003. While countless factors have contributed to China's dramatic economic transformation, the groundbreaking economic reform instituted by Zhu Rongji in these five years were critical in setting the stage for China to emerge as an economic powerhouse.

It is also interesting to note that the current leadership's bold reform agenda, whether it be a very strong anti-corruption campaign, the crackdown on inefficient SOEs, financial liberalization, or greater economic integration with the world economy, it can all be traced back to Premier Zhu Rongji's remarkable effort in these years. This raises a very important question. What lessons can China's current leaders learn from reforms over a quarter of a century ago?

Now, when we launched the first volume of Zhu Rongji's selected works, we held an event in New York City that was largely celebratory. Today is an equally exciting day. With the launch of the second volume, we decided to take a more academic and also more analytical approach to explore China's push for reform, both in Zhu's time and now. We'll begin with a panel on "The Zhu Rongji Era," featuring some U.S. policymakers who worked with Zhu Rongji and others who analyze him.

Then we will move on to a panel discussing progress on China's economic reform efforts that were announced largely from the Third Plenum and still

continuing in a very speedy manner since 2013 and now has been two years, almost one year and a half.

And finally, we will have a panel addressing the state of U.S.-China trade and investment.

Today's event wouldn't be possible without our friends at the Beijing Foreign Press. I hope that at least they will look at our website. And also the Brookings Press, who have embraced this project as a way to promote U.S.-China culture exchanges and inform English-speaking audiences about the lasting legacy of Premier Zhu Rongji.

Now, we are particularly pleased to be hosting so many prominent friends from Peking University and, you know, even one scholar is all the way from Canada. So it's really quite remarkable that we have this wonderful group of people from China travel all the way. And I would like to thank the National Committee on U.S.-China Relations for sponsoring the travel of these Chinese panelists here today.

Last but not least, I want to extend thanks to my distinguished colleagues at the China Center -- Ken Lieberthal, David Dollar, and Jeffrey Bader -- for their help in organizing today's event and for bringing together such a wonderful group of really internationally well-known scholars.

And now I invite to the stage the members of our first panel, moderated by my mentor, the founding director of our China Center and also a former U.S. negotiator, who has much contact with Premier Zhu Rongji, Dr. Jeff Bader. Welcome.  
(Applause)

MR. BADER: Good morning, everyone. Good to see so many people here on this cold and grim morning. If you can't hear me, just wave in the back. I think the mic is on.

Cheng Li already used the M word, "mentor," in describing me for some reason, but I appreciate that, Cheng Li. It's quite daunting for me to be on the panel here with two people who truly are mentors to me and a third who I wish had been a mentor to me. Nick Lardy taught me whatever I know about Chinese economics and Ken Lieberthal has taught me whatever I know about the Chinese system and the linkage between the political and economic systems. And I just wish I had had the opportunity to study with Justin down through the years.

This first panel is going to -- the way the day is structured, there's going to be a panel that's going to deal mostly with history, a panel that's going to deal mostly with what's going on now, and a panel that's going to deal with what's coming in the future. This panel will deal mostly with history and what happened from 1998 to 2003.

I will be clear, I'm not going to cut anyone off if they decide to talk about the present or if they make linkages between what happened then and what's going on in the present because I think that's very much a reality and it's something we all need to think about. So feel free to range far and wide.

I think, Nick, I'm not going to try to shape what our folks are going to talk about. I think Nick will talk, maybe Nick will go first, and focus largely on state-owned enterprise reform. Justin will concentrate on financial sector reform. And Ken, who was in the administration with me at the time, U.S. administration that is, will talk about the trade and investment issues that he had to deal with at the NSC at the time.

But let's just go down the line and start with Nick.

MR. LARDY: Okay, thank you, Jeff, and thanks to Brookings for organizing this. I think it's a very worthwhile project to bring all this material to an English-speaking audience.

I just wanted to begin on a personal note and say I first met Zhu Rongji in

Hawaii in 1987, the very end of the year, at a conference. We had breakfast together several mornings and on the third morning he told me the previous evening he'd gotten a phone call and that he was going to become the mayor of Shanghai. And then I interacted with him quite a few times over the years and certainly one of the more memorable occasions was when President Clinton hosted the State Dinner for Zhu Rongji and I got invited. Ken has never explained to me exactly, but I suspect he snuck into the Office of the Chief of Protocol and surreptitiously inserted my name on the invitation list. So that was another opportunity to interact with him.

I think SOE reform certainly is one of the major legacies of Zhu Rongji, his many legacies in many different domains. But in the enterprise reform which he launched I think was crucial, as Cheng Li said, to setting the foundation for China's rapid growth in the 2000s. And certainly, you can look at the standard metrics. The number of state firms declined dramatically. The number of people employed in state enterprises, both in the service sector and particularly in manufacturing, shrank dramatically. Employment went down by about 25 percent in the Zhu Rongji period. The number of industrial firms declined by half as firms were privatized or closed down. And this set the stage for a substantial resurgence in the state sector.

There were many, many money-losing state firms in the mid '90s when Zhu came and launched this program. The losses of these firms were quite substantial, about 1-1/2 percent of GDP. By the time he left office, they were down to about a half a percent of GDP, so it was roughly a two-thirds decline in the drag that these state-owned industrial enterprises were imposing on the economy.

This, I think, set the stage for some of the things that Justin might talk about on the financial side. It set the stage for eliminating so-called policy lending in which the Central Bank gave money to individual banks with the condition that it be un-

lent to certain state-owned enterprises. This was sometimes called policy lending, (Chinese term), or the other term that was frequently applied to it was relending, (Chinese term), because the Central Bank gave the money to the banks, which, in turn, had to give it to certain state-owned enterprises, in many cases to cover their operating losses.

So I think these reforms were very, very far-reaching. And in addition to cutting the losses, we saw a very substantial improvement in the return on assets of state-owned companies in the industrial sector. They had had terrible returns in the mid '90s and they began to rise in 1998 and then rose steadily for quite a few years based on the reforms that were undertaken. So capital was used more efficiently. Productivity went up. Losses were cut.

And I think the economy's also very successful in absorbing the number of people that lost employment in state-owned enterprises. There was a very concerted effort on re-employment and support for people that lost their jobs that meant that this massive transformation occurred in a fairly smooth manner from a political point of view. So I would certainly put SOE reform at or near the top of the list in terms of the legacy of Zhu when he was premier.

MR. LIN: Well, it's quite a pleasure for me to participate in this panel because I was considered one of the brain trusts of Zhu Rongji, so it's quite an honor for me to talk about his legacy in Chinese economic reform and transition. And one of the most challenging jobs for a planned economy to move to a market economy is the financial sector (inaudible).

As you know, in a planned economy actually there was no commercial financial sector at all because in a planned economy everything was allocated through administrative majors. And so even we have the banks, but the bank, actually, it's just a

branch of the Ministry of Finance. And so in the transition period, China started to build the banking sectors.

But at the beginning, as Nick just mentioned, there was no separation between policy lending and commercial lending. And when Zhu came to the central government in 1991, one of his first contributions was to set up three policy banks -- the China Development Bank, Ex-Im Bank, Agricultural Development Bank -- to separate the commercial function with the policy function. That was one of the main contributions.

And in the period that we are focusing today, from 1998 to 2003, when he was the prime minister, I think one of the main contributions was to deal with the nonperforming loan issues because, in 1998, China certainly was affected by the East Asian financial crisis. And the growth rate in China dropped from, you know, more than 10 percent down to around 7 to 8 percent. And with that kind of changes, you can imagine an economy heavily relied on bank lending to support (inaudible).

And so the nonperforming loans accumulate quickly. And according to Nick, the nonperforming loan in four major state owned banks reach as much as about 47 percent or 48 percent. So officially, China acknowledged the nonperforming loan was about 25 percent.

And with these kind of challenges, under the leadership of Zhu Rongji, he set up four asset management companies and took over those kind of nonperforming loans. Reducing the nonperforming loan ratio prepared those four banks to be listed in the Hong Kong stock market exchange and so in order to improve the governance of the banking sectors.

And we know that a powerful country must have powerful financial sectors. And because of this reform, now those four banks are all among the top 10 banks in the world. So I think that's one of the very important contributions.



In addition to dealing with the nonperforming loans, those four state banks actually also made a contribution to consolidate in the later 1990s about 4,000 small, local financial institutions. At that time, they encountered a similar situation of high nonperforming ratios. Some were even more serious than those four state banks. And he consolidated those around 4,000 financial institutions into 115 city banks, local city banks. And that also helped to stabilize the structural financial sector in China.

And I think that his contribution paved the way. After 2003, China continued to have about 10 years of great dynamic growth and become -- and now the nonperforming loans in those financial sectors are reduced down to about 2 percent, 3 percent at most. So I think that is one of the major contributions.

As I mentioned, without strong financial sectors, it's hard to have a strong economy. And because of the reform, that made it possible. But certainly, in a poor country, to have sustained growth you need to further improve financial structure of financial sectors. But anyway, his contribution laid down the foundation, allowed China to have further development in a much more healthy way. So let me stop here.

MR. LIEBERTHAL: Thank you. It's a real pleasure to have an opportunity to participate in this panel. I dealt with Premier Zhu primarily during the negotiation for the U.S.-China Bilateral Accession Agreement that really created the conditions for China's entry into the WTO in that everything that China negotiated with the U.S. became the starting point for rounding out the Bilateral Accession Agreement with all other countries. What you agreed to with any one country became part of your general accession agreement. And so all other countries basically felt that the U.S. should do 95 percent of it and then some others would pick up particular items that they needed to move on to show that they had met some particular needs of their own constituencies. So this was a very wide-ranging agreement and it was a very, very tough

negotiation.

I, frankly, read this book that just came out. I do want to note, as Cheng said, not only did we just publish this, but this event is, in part, to highlight that we just published this, and so we hope that you will have a chance to look at it. I read this book, which is overwhelmingly on the domestic side of what Premier Zhu did, with kind of a question in my mind as to how much did the style that I encountered in dealing with him on the WTO accession carry over to his style domestically because his accomplishments domestically were enormous.

I think of him largely as being the person -- if you think of it, that Deng Xiaoping marked the major transition away from the Maoist system and getting China on a long-term path of a much more successful type of development. But the policy problems built up over time so that by the late '90s there needed to be some major changes. You couldn't keep incrementally doing what they were doing. You needed to actually make structural changes and go against a lot of interests in the way the system then functioned in order to clear the path for the next decade or two.

And Zhu very early on in this book, talking in an internal talk, make very clear that if they didn't make the changes that he was seeking, and seeking with Jiang Zemin, that China would be in deep, deep trouble in the first decade of the next century. And so, in a sense, it resonates with where China is now, where they had enormous growth.

One of the things that always startled me as I went through this book is every time Premier Zhu used a number -- GDP, foreign exchange reserves, that kind of thing -- you sit back and it makes you realize that China then was enormously poorer than it is now. That the growth from then to now has been extraordinary. And yet, we're again at a point with the Xi Jinping leadership where the assessment, which I think is

correct, is that you need major changes, major structural reforms in order to clear the way for the next several decades.

So I was very curious to see how Premier Zhu came across in this. And, frankly, he was very consistent, very smart, very, very tough; used the experience that he got as mayor of Shanghai, which he refers to repeatedly, and then as vice premier deeply involved in the banking system to full effect as premier; focused, though, on what he learned in how to get things done in China during that period. And some of the lessons are ones that we need to keep in mind now.

Don't trust statistics. At one point, then Treasury Secretary Robert Rubin asked Zhu about his confidence in the statistics that China was publishing on its national economy, and Zhu said, you know, I can't tell you how accurate they are. The one thing I can assure you is that this year's statistics will be no less inaccurate than last year's. (Laughter) And it was not a bad rule to follow.

Investigate lower levels because local officials have their own incentives, and those incentives are not the same as those at the national level. So Zhu literally admonishes state council vice premiers and ministers in one of his earliest documents in this book that, let's face it, we know how to make good policies. We have smart people. We consult. We develop very good policies. The problem is they don't get implemented. And if you simply issue a document with a very clear policy and send it down, you'll be lucky if 20 percent of it is actually implemented at the local levels. You have to go down to the localities constantly to understand what they're dealing with and so they understand what you need. And then you have to establish criteria of success because if you don't have those criteria of success, frankly, you're not going to get there.

Dealt constantly with the problem of corruption, which he at one point made the comment on an inspection tour, he said, you know, I am always amazed at the

level of corruption. Many officials are so corrupt it is astonishing. And then the question is, how do you attack that problem effectively?

His agendas included, obviously, SOE reform and financial reform and corruption, but, more broadly, also reducing the size of government, making the government clean and lean -- two terms he used repeatedly -- so that it was less of a burden and just not too large to manage.

Stop focusing on GDP growth as the major driver of success or major criterion of success. You have to pay attention to the environment and you have to realize all the negative externalities of growth.

Stop doing big projects as the key kind of criterion for local officials, whether you're getting things done. Too many of the big projects are simply wasteful and end up losing money, which the local official doesn't care about, he comments, because the local official will have moved on by the time the cost has to be paid.

And then finally, a very strong stress on the interdependence in terms of China's success or failure of dealing with the international arena, especially in the international economy, and domestic reform. And that's where I think the WTO -- I'm sorry to take up all this on the domestic side rather than the WTO negotiations, but let me just conclude by saying that he saw joining WTO as absolutely crucial for providing the political leverage necessary to undertake the reforms domestically in China that he felt otherwise they could articulate, but they didn't have the political capital necessary to get them done to the extent necessary.

And I think with that as the motivator, he then negotiated, he was key to the negotiations, an accession agreement for China that made, frankly, a startling array of commitments that I think he took very seriously as providing leverage for where China really needed to go. And I'll stop there.

Wait, can I add one anecdote that he does in the book? One other thing that he used to startle, he was, A, often very sarcastic and very tough, but, B, he had a great sense of humor. And let me just highlight that with one exchange. This was in a meeting with Henry Kissinger and I'll just capture part of the dialogue. This is verbatim.

"Premier Zhu: We are still not" -- this was in April of 2002. "Premier Zhu: We are still not quite used to some of President Bush's ways.

"Kissinger: He comes from Texas in the Central United States and thinks differently from New Yorkers. He needs to reconcile the Chinese style with the Texan style. The Chinese style is more indirect while the Texan style is very direct.

"Zhu: So we should watch more westerners.

"Kissinger: That would help." (Laughter)

MR. BADER: I'd like to thank our panelists for getting us off to a great start. They each referred to their own experiences with Zhu Rongji and I'm just a mere moderator, but they've inspired me to tell my own anecdote, if I may be permitted to use or abuse my position as moderator.

Just to get a sense of the way Zhu Rongji got things done. I remember it was, I think, 1998 when we were stalled on the U.S.-China Bilateral Trade Agreement. USTR, in interagency meetings, was basically saying that China does not have the political will to close the agreement. So I was at the NSC at the time and I -- Alan Greenspan was going to China and by coincidence Chairman Greenspan called me over to talk about his forthcoming trip. This is relevant to the book because the conversation that Chairman Greenspan had with Zhu Rongji is in the book. That's one of the fascinating things about this book; you'll find verbatim conversations, kind of astonishingly candid and revealing conversations which Zhu Rongji has decided to dump

on the public in this book. And I remember this conversation very well.

So I saw Chairman Greenspan and his beat was not the bilateral agreement. And I said to him, we're stuck, do you think you could help out? Do you have a view on this?

And he said, well, this isn't really my beat, as you say, but I'm very much interested in seeing this come to a happy outcome, so I'll look for an opportunity to discuss this while I'm there. And I spoke to Ambassador Sasser and to his deputy chief of mission in the runoff and said, I hope there'll be an occasion to use the Greenspan visit, particularly the meeting with Zhu Rongji, to try to kick-start what's currently a dead negotiation.

Next day, Greenspan saw Zhu Rongji and I went to an interagency meeting and the USTR representative began by saying, an astonishing thing happened yesterday in Beijing. Zhu Rongji, during a meeting with Chairman Greenspan, turned to the chargé d'affaires and said, Americans, I understand, think that we don't have the political will to complete this agreement. I'm here to tell you that I do and we do. And let me illustrate that.

He then put on the table two or three significant I will call them concessions, I guess we can call them concessions now. I remember one of them was in the area of insurance, I think one was in the area of agriculture. And Greenspan nodded and our chargé nodded and this was duly reported back to Washington, to an astonished USTR, with whom, by the way, I had not coordinated. But anyway, that's what got that negotiation going and it moved very rapidly to closure after that.

The other thing I'd mention that I recall from that period in connection with this is the relationship between Zhu Rongji and Jiang Zemin was a complicated one and that's something that maybe should be the subject of another panel. Zhu Rongji

could do all kinds of things, but at the end of the day, Jiang Zemin was the General Secretary of the Communist Party and Zhu Rongji could not rule Jiang Zemin. He had to work through him and he had to work with him and so some of these efforts to get to closure, Zhu Rongji would be very forward-leaning and then, suddenly, you see him change his position. It wasn't because he had changed his position. It was because Jiang Zemin had said don't go there.

So, anyway, those are just a few comments prompted by reading the book and hearing my colleagues talk about their own Zhu Rongji experiences. Let me just throw out a question or two to kick off discussion here. Anyone should feel free to jump in on these, but let me address questions to one principle person and then others can chime in.

Nick, perhaps you could offer a view to us on we all know that Deng Xiaoping basically got the reforms rolling beginning in 1978 and then accelerated them again around 1992. In your view, what was left over? What did Deng not do that Zhu Rongji -- what was so important about the 1998 to 2003 period that Deng had left unfinished, for whatever reasons, that Zhu moved?

MR. LARDY: Well, I think it's in the domains we've talked about. Certainly, SOE reform was not very much -- well, it was on the agenda earlier, but not very much was accomplished. There were a lot of discussions about governance reforms and tweaking various aspects of the ministerial system that oversaw the very large number of state owned companies, but there was no, really, coming to grip with the underlying problems, which is that a very large share of these companies were losing amounts of money and were very inefficient and, certainly, that comes through over and over again in these speeches, including when he's going to the local levels.

You just can't borrow more money to keep things going. We have to

make sure that the funds allocated through the banking system are used more efficiently, and you can't rely on indiscriminate expansion of credit to stimulate economic growth. So this goes to the whole thing that Justin was talking about, China really didn't have a very effective commercially oriented banking system at the time. So I think those things really came in the Zhu Rongji period.

Nobody has mentioned, but it is worth noting that when he was vice premier, he was also simultaneously the governor of the Central Bank, I believe starting in '93, so this was very unusual. I don't believe in the history of China Central Bank that there has been a vice premier simultaneously serving as the governor of the Central Bank, so I think he gained an enormous amount of experience.

Remember, this was a period of very, very high inflation at the time he came into the bank. Remember, consumer price inflation reached 25 percent in 1994, he brought that under control and he was constantly subsequently worried about the possibility of a resurgence of inflation, which he found was one of his major challenges when he was governor of the Central Bank. So I think there was a lot -- Deng pushed things in the right direction, particularly in agriculture, but some of the core problems in the financial sector and the enterprise sector were, quite frankly, more or less papered over for quite a long time.

MR. LIEBERTHAL: Well, now you see Zhu referring, as premier in these papers, constantly back to his problems in 1993-94, that the economy became overheated, inflation grew, debts piled up, too much money was put out there, and so that was a searing experience for him and it was one that he certainly wanted to caution everyone against policies that might get them into that position again. It kind of resonates in some ways, as I read it, with the policies during the global financial crisis and the huge credit expansion and rapid building, and now the need to deal with many of



the consequences of that.

MR. BADER: Feel free to comment on that one, Justin --

MR. LIN: Yeah.

MR. BADER: -- but let me ask you a slightly different question. As you look at the current Third Plenum's agenda, financial sector -- financial service sector reforms is very high in the list of priorities. And there's an awful lot that hasn't happened yet in financial sector reform in terms of interest rate liberalization, in terms of creation of a more substantial private banking sector that goes beyond the big banks, in terms of creating very liquid capital markets that corporations and local localities can use to raise funds.

I guess why I'm asking this is what grade would you give to Zhu Rongji and the financial service sector reform in 1998 to 2003? Do you think he did all that reasonably could have been done at the time and that the challenge is now that this is just the way things are and we're in a different stage of development and that Zhu could not take these things on? Was Zhu as aggressive as he could have been and should have been on financial service sector reform? How would you evaluate?

MR. LIN: Well, I certainly will give him an A for what he has done because certainly there are many areas that require further reform now, but if you put the challenges that he had at the time, I think he did remarkably because in a transition to a market economy, China adopted a gradual dual-track approach and it continued to provide some subsidies and protections to the oldest state-owned sectors. They are not well because they were kept in transit out of one sector and China was still a poor country, as you mentioned, in the 1990s. Those kind of sector changes China did not have comparative advantage at all. And so, without protection and subsidies then they cannot survive and then the whole economy can collapse.

And under that kind of situation -- because we know that before '93, all the investment and operational costs of the (inaudible) sectors came from the fiscal appropriation. They didn't have any financial cost, but they still need to have some subsidies. And as a way to give those kind of (inaudible) sectors subsidies was to have some kind of financial reparation. So the interest rate needed to be controlled and cannot be really freely determined by the market exchange rate.

But under the kind of condition, he tried a way to reform the financial sectors. On the one hand, reducing the non-performing loan; on the other hand, visiting the banks and the stock market in order to improve the governance and also invite strategic investor in the small banks to create a competition. And under that I think he already achieved a lot, but certainly it really requires a certain kind of further reform because the situation in China changes.

China now is not a low-income, poor economy anymore. And many of those old sectors used to be against China's competitive advantages. Today they are China's competitive advantages, like in automobile sectors, the equipment/machinery sectors. And so subsidies in its own are not necessary now and so that allows in the Third Plenum to introduce further marketization of the financial sectors.

On the one hand, to liberalize the interest rate of lending and now, also, the interest rate of savings and to remove the financial inner repression. And he could not do that at the time. If he wanted to do that at the time, okay, he seemed to be very market-oriented. Well, the world can't have that many people outside China, but the result may be, you know, a crisis or even a collapse in China's system.

So, with this kind, he's a very pragmatic person. He understand what should be the direction of the changes in China, but he also has a very good control and understanding about what are the limitations in China to do that. But, anyway, he laid

down the foundation for further reform and in his time he did the best -- good for China and good for further reform. So with that regard, I think I would give him an A+.

MR. BADER: Thank you, Justin. He went from A to A+ in the course of that answer. (Laughter)

Ken, I wonder if you might give us some thoughts on -- you talked about Zhu's sort of special and unique qualities, in some ways -- well, let's say it, an uncharacteristic Chinese leader, in many ways. What kind of obstacles did he face as premier in trying to move China in the direction that he wanted to go? What were the objective factors and the kinds of resistance that he had to overcome and how did he do it? In 30 seconds or in 5 minutes.

MR. LIEBERTHAL: Well, first of all, he had the advantage of being an A+ person. (Laughter) And having very good people in his brain trust.

Seriously, I think, first of all, he had a keen appreciation of China's realities and so he didn't fool himself as to how big the problems were in particular areas and how much had to be changed. Secondly, he understood -- it seems almost silly for an outsider to say, he understood, but it was obvious to me, at least, that he would run very far with the kinds of policies that he thought needed to be implemented, but he always went to Jiang Zemin for the political backing to make that work. And we saw this even in the WTO negotiation, day-by-day, when we were in Beijing for the final set of negotiations, he would push hard and then overnight he would talk with Jiang Zemin and the tone would shift a bit.

And in the book, again, he refers in several instances to how he developed something and it was always, you know, I had this idea and then Jiang Zemin approved it and basically decided on the parameters and now I can run with it. And so there was this interaction between the kind of political cover and then the person who

knew the details and really went down and developed the very specific policies and I think that that was very effective.

And we saw in the WTO negotiations something else that was really very striking, which is that much of that negotiation -- I'd be happy to be corrected, Justin, if you had a different view from the inside of this -- a very strong sense from the outside was that a great deal of that negotiation and really crucial decisions in reaching the final bilateral accession agreement, those negotiations did not involve in a detailed way the affected interest in China. Some major decisions were made either on the spot in talking with the premier, or he would come back a couple of hours later with an answer. And then when we got a final accession agreement, Jiang Zemin came out, met with the group to make clear that he blessed this 100 percent, right? And then, afterwards, you got this being relayed in more detail down the pike to the ministries, et cetera, that were interested.

My understanding is that it had not been translated into Chinese. And let me say, even trying to read the English, for those who are not trade negotiators -- I was there as the guy from the NSC, not as a professional trade person -- even in English most of the time I couldn't understand what he was saying. (Laughter)

So negotiating this in English and doing it without a Chinese text that the Chinese were negotiating internally, really quite startling. So I was really impressed with his ability to move forward, to be bold, but always to cover his political -- or to assure that he had the political backing necessary at the very top of the party, and then focus on implementation once he got to where he needed to be in terms of top-level policy. He never left it there. He then really rammed it through the system.

MR. BADER: As feared as Zhu was through the bureaucracy, and he was the most feared man in China through that whole period, he was awfully careful with

Jiang Zemin.

MR. LIEBERTHAL: Yeah, absolutely.

MR. BADER: I remember the Bill Clinton visit to Beijing in '98 and we knew the role that Zhu was playing on WTO, so we wanted to give Zhu a lot of face on the visit, I recall. And we'd scheduled some sort of event with Jiang Zemin and there was to be joint press events between Jiang and Clinton at the outset of the other meeting and we scheduled a lunch with Zhu Rongji for Clinton, along with the whole state council. And we told the Chinese we would have a joint press event at that event, as well. Well, Zhu Rongji got back to us pretty quick and said there will not be a joint press event. And it took us a few minutes to figure out -- we argued with them and then took a few minutes to figure out why: because he understood that he was not Jiang Zemin. And the joint press event was going to be with Jiang Zemin and that we in Washington might see Zhu Rongji as a co-equal premier and head of government in both systems. And the man who was doing WTO negotiations, Zhu Rongji understood perfectly well, but while he could kick around party secretaries all over the country, he was not going to try to compete with Jiang Zemin on the world stage at a press conference.

I'd like to open it up for comments, so if people could wait for microphones, identify themselves, identify their institution, and ask a question. And although we know there's a lot of wisdom out here, preferably don't make a speech.

The gentleman in the front, sir? Direct your question at someone, if you wish, unless you want to direct it to the whole panel.

SPEAKER: Hi, (inaudible), *China Daily*. Thank you for sharing your interesting anecdotes about Zhu Rongji. And as a journalist covering Zhu Rongji since day one in Shanghai when Zhu was the party secretary, you know, I'm a great admirer of my mayor and the later premier. Obviously, I agree totally with what you said. But the

thing Cheng Li said, this is going to be academic and in an article, so I just thought it's probably more meaningful -- interesting to just also delve into what lessons we could learn from the Zhu Rongji era.

In my mind -- we discussed earlier issues like social injustice, I mean, Nick talking about SOE reforms. I remember covering a million workers being laid off in Shanghai that were not properly compensated, I mean, compared today, obviously, so that was a bitter story for a lot of them. And also the displacing of households, I mean, very little compensation, as well. Soliving in Xingtandi for example, even driven to Pudong, obviously.

And also the environmental sort of a concern people talking about in the early '90s has not being -- I don't know, Dr. Lin has some insight, was there sort of a healthy debate at the time about this issue, social injustice and compensation for SOE workers and also the environmental implications? Thank you.

MR. BADER: Anyone? Justin or others?

MR. LARDY: Well, if you read the book, the discussion about compensation for laid off SOE workers is very detailed. Zhu knew exactly how much they were getting. They were supposed to be getting an amount that would cover kind of basic subsistence and my memory is that that came down to something like one-quarter of their previous salaries, or maybe it was one-third, or something like that. And there's a detailed discussion about how this was going to be financed, how enterprises had some responsibility, local governments had some responsibility, the central government had some responsibility, but that this was flexible; that if the enterprise couldn't cover it, then they'd have to make special arrangements.

So I don't think there was any illusion that people that got laid off were going to be able to maintain their previous existing levels of income if they didn't find

another job. And there were the re-employment centers and I think the overall experience was actually, as I said earlier, fairly favorable. Most people did get jobs.

And, obviously, a lot of them probably suffered some loss of income in the transition, but there was a very basic -- maybe primitive, but basic -- social safety net for people that lost jobs.

On the broader question of the lessons of Zhu Rongji, I would say that we need to look also at the next 10 years of the Hu Jintao and the Wen Jiabao period when economic reform basically stalled. State-owned enterprises, which had had a huge boost of productivity for a few years, fell back into their old, money-losing ways and their productivity declined. And from around the middle of the 2000s onward, state-owned enterprises have become an increasing drag on economic growth because the kinds of reforms that Zhu launched I don't think were sufficiently sustained in the Hu Jintao/Wen Jiabao period.

So I'd certainly think one of the lessons is -- somebody said once to me a year or two into the Hu Jintao/Wen Jiabao period, Zhu Rongji said to an associate, in 2 years they've undone everything that I accomplished in 10 years. I don't know if that's apocryphal or not, but there was certainly a loss of momentum. And Justin gave it a very nice interpretation, well, the situation's different now. One of the reasons the situation is different is that the reform momentum really significantly slowed in the Hu Jintao/Wen Jiabao period. So I certainly think one of the lessons is that, even if you can launch a successful reform that makes some very substantial progress on dealing with some of the underlying structural problems, if you don't continue to move ahead, you inevitably retrogress.

MR. LIN: Regarding the momentum issues, the internal policy discussions certainly pay attention to that, but the result was not as successful as

expected. I think there are maybe two reasons, one related to the state of development in China because at this stage of China's development, manufacturing is still the key. And we know that manufacturing sectors, they have the characteristic of energy-intensive and emission intensive.

And at this stage of development, any country, the environmental issue would be more serious than when you are in the early agriculture stage or later in the service stage. So I think that the frustration related to the environmental issues in China, to some extent may not be so much related to the policy issue because it's a stage of development issue. Certainly, China can do better. Either implementation of the environmental code and so on will be monitored by the local government, but as you know, that in the competition for local development, local officials sometimes do not pay so much attention to the environmental regulations and so on.

I hear the issue is the state of development and the implementation at the local level, instead of at the top level they don't pay attention to the environmental issue.

MR. LIEBERTHAL: I think those are very important points and are accurate. One of the fundamental problems on the environmental issue is that they never created incentives for local officials that would lead them to prioritize environmental clean-up. And rather the incentives were to expand construction, to do big projects, to build infrastructure, to grow the GDP, which would lay the basis for high evaluations in moving ahead.

Also, the system itself makes local officials really care enormously about what happens within their own jurisdiction.

MR. BADER: Right.

MR. LIEBERTHAL: But not what happens in any other jurisdiction. And



the problem with that is that most environmental issues don't define themselves by jurisdiction. And so whether it's water pollution or air pollution or soil pollution or whatever, you just have huge problems when you have local officials both having an enormous amount of impact on what happens within their locality and are not incentivized to prioritize environment and are not incentivized to care about what happens downstream or downwind from where they are.

MR. BADER: Please identify yourself.

MS. DOBSON: Oh, Wendy Dobson. Come back to the issue of corruption and put it, perhaps, in a forward-looking context because it is so important right now. A knee-jerk Western response to the problem of corruption would be, well, you need the rule of law, you need an independent judiciary, and you need a free press to shine light on corruption. So changing institutions to create incentive that we've just been talking about, that may be lacking.

I'd like to hear everybody's assessment of how Zhu Rongji went about it and whether it creates any precedents for how it's being treated now because one of the concerns is that everybody's changing their behavior, but temporarily, until this blows over. That's basically the question, I guess.

MR. BADER: Volunteers? (Laughter)

MR. LIN: Well, I think about this, this way: I'm a student of Gary Baker's and we know that the way to deal with the corruption issue. On the one hand, you need to increase the discipline and the punishment. And on the other hand, you need to reduce the gain of corruption, and the rent from rent-seeking. I think that, as I mentioned, due to the state of development in China at the time, the protection and subsidies to the state-owned sectors was a necessity. Who will maintain the stabilities?

And there are some side effect of those kind of subsidies and protections

to the state-owned sectors because it creates a distortion and random rent-seeking, and that was one of the rules of corruption. And under that kind of context, the emphasis certainly is on the discipline. So, Premier Zhu was very firm on anti-corruption campaign, but because the range was so large -- as long as you reduce your discipline and it's on the corruption, it will become a big issue.

But I think now the situation is better in the sense that, on the one hand, certainly, we need to strengthen the anti-corruption campaign, discipline and punishment. On the other hand, if you founded a Third Plenum to further reform, to remove all those kind of distortion, then, again, the corruption would be much smaller. So I think there's two ways. Not only the way just mentioned, but also it's very important in a transition economy to reduce the rate and then (inaudible) for the market-oriented reform.

MR. BADER: No one else wants to dive in? It's a great question and highly relevant today.

MR. LIN: No, before anyone asks, I'd like to point to one of the very important legacy of Zhu Rongji in China and also in the world was his views on infrastructure investment as many countercyclical measures under the shock of the economy because, in 1998, due to the East Asian financial crisis, the economic growth rate in China slowed down significantly. And at that time he used infrastructural investment financed by fiscal expansion as a countercyclical measure.

So, if you look at the beginning of 1998, the highway system in China only had 4,700 kilometers. And supported by the fiscal expansion and infrastructural projects, by the time of 2002 -- one year before he stepped down as the prime minister -- the highway system in China increased 5 times to 25,100 kilometers. And I think that this is a very effective intervention measure because during a downturn to use infrastructure investment on a short-run created a demand in jobs, stabilizing the economy.

And in the long run, the productivity in China was enhanced. And the bottleneck of growth in China was released, and I can give one figure to support this argument. Before 1998, whenever China had two-digit growth rate, China also had two-digit inflation rate. But after 2002, with the expansion in the infrastructure removing the bottleneck, China experienced six years of two-digit growth rate, but inflation rate was less than 4 percent. And that's one of the major contributions of his infrastructure as a countercyclical measure that could cope with the challenges.

And in 2008, when China encountered the global financial crisis, China used that in a (inaudible). And I'm very delighted to say now IMF also recommends similar measures to other countries if they encounter their shocks and a slowdown in their economy, and they say infrastructure investment is the best way to cope with this kind of need for expansion of the fiscal policies. I think that's one very important legacy in China, but also to the world.

MR. BADER: Ken?

MR. LIEBERTHAL: I'll add just one or two points. I agree with everything you said, including the lesson for other countries. There is a long history in China of very, very tough campaigns against corruption and they have a limited effectiveness over time. You know, everyone scrambles and cuts back their liabilities, if you will, in their corrupt activities for a while, but then the campaign has to ease off because you have other priorities and you need to get people to take more initiative and so forth, and then corruption begins to grow again. And after a while it becomes important enough that it moves to the center of the stage again.

I think to really get at that, therefore, you need, among other things, to reduce the extent to which the state intervenes in the economy at a micro level, at the enterprise level. And that's not only state-owned enterprises versus private enterprises,

but the control of all kinds of things in make-or-break business opportunities. I think those things remain very pervasive, so I think it's a huge job to reduce those.

You also need a very, very good regulatory system. You need to have good regulations and you need to have regulators who really understand what they're talking about, have the ability to get the information they need, and then have a legal system that they can go to, or a system of sanctions that they can go to, to give what they do teeth. And that, again, is not easy.

So there's no such thing as getting rid of corruption, but corruption in China, in the last decade or so, has become truly predatory and so there's an enormous need to whittle that down. You see some of the approaches that one would want to see to get there, but I think that it is well short of what may be required eventually to really get this problem under substantial control.

MR. BADER: In the back?

SPEAKER: Thank you very much, my name is Deng (inaudible) with *China Review*, a news agency of Hong Kong. I believe Zhu Rongji was leading China's efforts to embrace globalization and integrate into the international system. But in a different context of China's development, do you think the new Chinese leaders still have the inclination to integrate into the international order, which is dominated by the United States? Thank you.

MR. BADER: Ken?

MR. LIEBERTHAL: Let me just comment on the Zhu Rongji part of that and then I'll leave it to Justin and Nick. (Laughter)

The Zhu Rongji part, one of the things that comes across very clearly in these papers, et cetera, was that Zhu was not, to my mind, a globalist. He was not a liberal internationalist. He talked about foreign investment in China, about joining the

WTO, et cetera, very much in terms of these are the specific things we need to get out of this for China. We need technology. We need more modern management. We need to open up foreign markets, so that we can grow our exports. We need, as necessary, to control the exchange rate in order to give us opportunity and if we can't control the exchange rate, then we have to use things like rebates on export taxes, and that kind of thing, in order to remain competitive because we need all of that in order to realize our own economic goals.

So he was not, to my mind, someone who believed in globalization in terms of broad trade theory, you know, reducing barriers to trade. If you play out the comparative advantage analysis, it leaves everyone a winner with greater specialty. This was this is what we need for China. We need to keep this under control and we need to use it effectively because it's one of the keys to enabling China to reach its own aspirations.

MR. LIN: Well, first, the current government certainly is continuing to impress the globalization. And if you read the Third Plenum you can see that China needs to use two resources: domestic resources and foreign resources. China needs to rely on two markets: domestic markets and the global markets. So I think the direction is very clear. They'll continue to push towards that direction, but, deeper still, Ken is also right because China is a transition economy.

In transition economies you have a lot of legacies in the past. It does not mean that you remove all the barriers, then it's going to be a win-win for both sides. So we need to have some kind of program to pace this kind of speed of globalization. And I think that you can say that is for national interest, but I think it is also for the global interest because if there is chaos in China, certainly it is not good for China, but it is also not good for the world.

Yes, but overall I think that the direction of globalization, the direction of the openness will continue. And how far we can go certainly depends on the domestic strengths, as it were, as the global situation.

MR. LARDY: Let me just say briefly, I agree with Justin. I think all of the evidence is that this Xi Jinping/Li Keqiang leadership is very committed to continuing opening up. It's certainly reflected in the Third Plenum document where, over and over again, they talk about the need for increased competition, a level playing field, which also implies that you're going to reduce barriers to trade and investment and so forth.

And then you look at the practical side, the range of things that China's currently negotiating. They've finished a free trade agreement with Australia, which is fairly far-reaching, a few months ago; negotiations on the bilateral investment treaty, a much better offer in China's efforts to become a signatory to the government procurement agreement.

Now, at every step foreigners are saying, well, this is an improvement, but it's not good enough, but the trajectory, the direction, I think is positive. The offers that are coming in many of the negotiating domains are, quote/unquote, what we would consider to be better, more liberalization. So I don't think there's much doubt that they're committed directionally, but, as Justin said, the pace will depend on the domestic economy and the political constraints that the leadership faces.

MR. BADER: I just want to say one thing, just picking up on what Ken said about Zhu approach in 2001. The challenge was very different than now. And where China was then is very different from now. No one was thinking about China as a major foundation of the global economy in 2001. No one was talking about China's responsibility for global prosperity in 2001. People were talking about China's growth and that was going to be its contribution.

I think that began to change with Bob Zoellick's speech about responsible stakeholderhood -- 2005, 2006 -- where the notion was that China had to become a responsible foundation of the international system. And now if you look at what China's doing, clearly the current leadership understands that. They understand that they have a different challenge. It's not just development of China, but their integration into the global economy is not merely a benefit to China, but that they have a responsibility more broadly, and a lot of what they're doing, I think, reflects that. So it's just a very different stage in history, I think.

David, did you --

SPEAKER: I was signaling one more question.

MR. BADER: Oh, you were signaling one, it wasn't you?

SPEAKER: It's not from me.

MR. BADER: I'm disappointed. Okay, the gentleman on the right, out there.

SPEAKER: Thank you for the discussion. I have a question for Mr. Bader. You mentioned that the relationship between Premier Zhu Rongji and Jiang was complicated. I am wondering, what is the relationship between the current premier, Li Keqiang, and Xi Jinping? (Laughter)

It's still complicated. Will Xi tell him, don't go there?

MR. BADER: That's a wonderful question which I hope the next panel will get into. (Laughter) And I am a mere lowly moderator, I've said more than I should have, so I -- it's a great question. I hope it will come up. It will be answered sometime during the day, but not by me, I regret. (Laughter)

Maybe there's time for -- we have about a minute or two. The gentleman in the back? Last question.

MR. PARKER: Thank you very much. David Parker from CSIS.

Obviously from your comments and from China's experience under his leadership, Zhu Rongji was an extraordinary leader, but he was also one man. So what do you think are some of the institutions and processes that he established that were really critical to the success of such a broad-ranging and an ambitious reform drive? (Laughter)

MR. LARDY: Well, I'm not sure I heard or understood the full question, but in terms of legacy, he was one man, but the institutional changes that he instituted had an enduring effect. I mean, he moved, for example, to reorganize the Central Bank so that it had regional offices where, in effect, the Central Bank was given a great deal more independence, vis-à-vis first party secretaries in various provinces and cities, so that was a major institutional change. And it's discussed in very clear terms in the book.

I think we knew about it at the time, but this is the first I've seen the actual statements about that. Justin mentioned the asset management companies which had a key role in the restructuring of the banking system in the early part of the 2000s. Some of them still exist and are still playing a role, so I think he instituted a lot of institutional reforms. That he was one man and we're putting him front and center in this discussion, but there were major, major structural changes that he instituted that have had an enduring effect.

MR. BADER: Thank you all very much. Thank you for some excellent questions and for helping stimulate our terrific panelists into a great discussion. Could you please acknowledge our panelists? And we'll take a break. (Applause)

MR. DOLLAR: This next second panel — there will be a break later so if you want to talk to them individually please wait for the break. I need Qin Xiao, Huang Yiping, and Arthur Kroeber to come up here. I like the way that Bader described this panel as moving from the past to the present. So if we get our three participants up here,



if we get them mic'd up, and clean water glasses, then we can move ahead.

So in the interest of efficiency I'll just make a few introductory remarks from here so we can move into the second panel while our participants are being mic'd up. Qin Xiao, yeah, all right. So I'm David Dollar; I'm a Senior Fellow in the John L. Thornton China Center here. Our second panel is entitled Third Plenum Reforms: Opportunities and Challenges. I found the first panel really fascinating. You know, looking at that history, and I think it was Nick Lardy who suggested that following Zhu Rongji there really was 10 years or so where there was not a lot of reform momentum in China, but then new leadership came to power, put out a very impressive set of reforms at the Third Plenum, a little bit more than year ago. We've got a fantastic panel to discuss these contemporary issues. We've got three analysts based in China. I'm going to start with Qin Xiao who is the Council Chairman of the Boyuan Foundation. You know, long history in the financial sector in China. And then I'm going to turn to Huang Yiping, who is a Professor of Economics at the National School of Development at Peking University. And then Arthur Kroeber; Arthur is a Nonresident Fellow of our Brookings Tsinghua Center at Tsinghua University. He is also the Managing Director of Gavekal Dragonomics in Beijing. So I've asked each of them to start with no more than eight minutes, you know, discussing what they see as some or even just one of the key reforms in the Third Plenum, you know, why is it important and what's the progress, and then I'll ask them a few questions and we'll leave plenty of time to turn to the audience.

So I'm going to start with Qin Xiao.

MR. QIN: Okay, good morning, everyone. Before we talk about the implementation we spend a couple of minutes to talk about the significance and the importance of this package or agenda reform passed in the Third Plenary. Number one, I think the whole package is a total solution, not piece by piece. So it consists of over 200

projects and addresses almost all outstanding issues in China and timetable have a target. So what happens is kind of comprehensive and with clear directions a total package reform as we expected. And plus there are strong organizations being set up to guide, to carry out this program headed by Xi Jinping. And there are some procedures and I already invite some independent evaluators, companies, organizations to evaluate and if you have interest, I explain the procedures how to carry out that. Among them I think there are a few topics for reform are so critical important. It has long been (inaudible) equally distributed resources, we need to focus our resources, some certain more important project or areas. Number one is the fiscal reform, number two is the financial one, number three is the price of (inaudible) market, number four is the SOE, and essentially many could be -- it's also important but could be classified as a second priority for them.

It seems to be the last year no significant actions or plans for reform happened. But if you look carefully, actually it's still going forward. Number one is quite comprehensive, they have timetable, they have target, but neither have roadmap, neither have some detailed plan. Need to coordinate between the State Council and the Central Committee, and need to consult some experts and they understand among these hundreds of hundreds of products, there are some interactions, some of them are reinforced, some are you must pay some costs for reach the others. So they do something, for instance the patent law is almost a year to be delivered after three round or four round discussions which will have more discipline, more transparency, and will cut down a significantly the fee charged. In China the total revenue including the tax and the fees and some others like land, the fees take a big portion, and there's no discipline. Even in the county level they can charge fees. So that's a big progress for patent law? And also you will see the significant reduce or remove the administrative approval for

setting up a business for business activities which reduce significantly the transition costs for big running business, has been well received by the market. And we have some structural reduction of the tax to give more fair commission for SMEs and private sector.

In the financial industry you'll see the progress for the interest rate liberation and the exchange rate liberation, and opening up under the capital account. So it has been done for several years and I will say that this last mile, so it's almost close to the equilibrium point both the interest rate and the exchange rate. It's still try to go, maybe takes two years, less than three years. Personally I believe within a couple of years they can reach the target to finalize the last mile.

And the financial market is also an ongoing product being pushed forward for several years. They have a formula in terms of the energy – I mean the oil and also the land, particularly industrial use land, and the labor costs being liberalized, and some utility products still have a gap; particularly for the treatable products like energy they still have a gap. But I appreciate their approach to gradually try to merge this gap instead of – because if you look at the oil price jump 100 percent and down 100 percent, so.

And there are some reforms I will not imagine from day one. I think next year or this year will be a quite important year to see the implementation. And we would like to know the implementation plan rather than just target and timetable. And we would like to see some significant progress being achieved. So I think this year is quite critical, a very important year.

So let me stop here.

MR. DOLLAR: Okay. Excellent, excellent on time and excellent on substance. Let's turn to Huang Yiping.

MR. HUANG: Thank you. What I'd like to do is probably to supplement

what Chairman Qin Xiao said about the economic reforms, but I want to take one step back to look at why we needed this new big reform program now after 36 years of significant progress at a more macro level.

Economic reform lasted three decades or more now is basically a transition from the central planning system to the market system. And the approach as Justin mentioned early on is typically described as a dual track approach, so essentially you have one part of the economy continues to be supported by government policies or controlled by government policies, but the other part of the economy is being liberalized. That is the essence of the reform approach and overall it's been working well as you probably have seen. But my own sense is there were actually two dual track approaches during the last three or four decades. The first approach which is very popular identified – and Justin mentioned earlier – is the dual track approach between the state sector and the non state sector. When you liberalize you keep all the state owned companies, but hopefully the non state sector will rise much more rapidly and then after a while hopefully the non state sector becomes dominant in the economy and the transition to a market economy will be very smooth. However, there is actually a second dual track approach which is not that widely discussed, but that's actually my academic research interest, is the dual track approach between product market and factor market. You look at the product market today in China, agricultural market, manufacturing market, and the service market, they have all been almost completely liberalized, and the prices are freely determined by demand and supply. But if you look at the other part of the economy, the factor markets, markets for labor, for capital, for land, for energy, for water, you can – I mean I think you understand the distortions and control in this area are still very massive. So you look at the Chinese economy today, we are still being on the way to a market system, but almost everything is halfway slow and that's why I think we need the big

program to complete the transition.

The first dual track approach actually was a success as we know that helped China to maintain very strong growth, but also caused some problems. So for instance we are talking about what Premier Zhu Rongji did in the 1990s, and he had very ambitious reform programs. But if you look at the 1990s, what happened in the economy at that time? I mean apart from the very positive side of economic booming we actually had almost the three major economic crises in the 1990s. The first is a fiscal crisis when the government revenue as the share of GDP dropped from 36 percent at the beginning of the reform to almost 10 percent at the beginning of the 1990s, so it was a big challenge. The second almost crisis we had was the banking crisis. In 1998 the non performing loans were estimated at between 30-40 percent, the ratio. You can imagine any economy with a non performing ratio that high would experience a banking crisis, but we didn't because the government in the end supported it. And the third almost crisis was actually in the state sector alone. The state sector around the mid-1990s had a net loss making record. The rough thing at the moment was one-third made express losses, one-third made impressed losses, and one-third was roughly even. So the sector as a whole was making losses. I think the problems we experienced in the fiscal system and in the banking system actually were closely linked to the loss making in the state sector and that's why in part we needed a Zhu Rongji in Beijing and to oversee all these reforms.

The fiscal reform as you probably already know, the fiscal revenue as a share of GDP now is up to around 22 percent. The banking sector reform as Justin mentioned early on, all sorts of measures that writing off non performing loans, recapitalizing the banks, introducing foreign strategic investors, and public listing. The big change as Nick also mentioned earlier is reform of state sector, the so-called let go

small-medium enterprises and focusing on the larger ones. So we never use the term "privatization", but literally half a million of the SOEs were gone within a very short period. And that actually laid the foundation of very strong growth early on, so I thought that that actually demonstrated what kind of problems we caused with the first dual track approach and that laid the foundation of very strong growth in the following 10 years, obviously helped with the WTO accession. But I think you would agree the SOE problem has not been fixed completely. That's why the Third Plenum a year ago was still talking about SOE reform as a key priority.

The second dual track approach as I mentioned is basically about the factor market distortion. And I think Justin mentioned earlier some of the distortions were really necessary to facilitate support the first dual track approach because you want to support SOEs you need some kind of resource allocation, pricing, and so on to support continuation of the sector. But one way of summarizing the distortions in the factor markets in my view is just pushing down the cost of inputs. So the cost of capital as a good example in the formal sector is much lower. But that actually happened not only for capital but also for energy, for land and many other factors as well. So the one way of generalizing the second dual track approach or distortions in the factor market is the kind of impressive subsidies we've been providing to the corporate sector, but the taxes on households. You can make more elaborate cases, but the essence is it's redistribution of income from household to the corporate sector, that's why growth is very strong, export's strong, investment is strong, production is strong, but consumption as a share of GDP has been declining simply because household income was not growing as rapidly as GDP growth. So we end up with today's growth model, one Wen Jiabao described as uncoordinated, inefficient, unbalanced, and unsustainable. But really you look at it, it has two sides. On the one hand growth is very strong, but on the other hand the structural

problems are growing rapidly which make it unsustainable.

So I think what we really need to face now is not so much about the growth story today, but how to rebalance the economy and make the growth more sustainable. My own subscription and my reading of the Third Plenum decision is to liberalize the factor market and that I think I what we need to do. This is why they all mentioned about the financial liberalization, the resource pricing, maybe also a little bit more about the labor market reform. But for these reforms to be most successful you need again to transform the state sector simply because if the state sector's behavior doesn't change don't even think about market based interest rate or exchange rate. So I think these two actually are closely linked and the simplest way to look at it in my view is just to complete what Deng Xiaoping started and what Zhu Rongji made a significant made progress, but the job is not yet done.

MR. DOLLAR: Thank you very much, Yiping. Arthur?

MR. KROEBER: Thank you. Sorry. Is this all right? I'll just make four points very quickly to supplement what Chairman Qin and Professor Huang have said to present a slightly different angle.

The first comment I would make on the Xi Jinping reform program is I think it's important to understand that it is not simply a technical economic reform program. I think often it's viewed too narrowly. It's actually a much more ambitious effort to restructure the entire governance system of China. And I think this is an important thing to understand both to understand how all of the bits of the program link together and also some of the sequencing. And I think the observation was made that when you talk about all of these different economic problems that you see in China ultimately they go back to problems of governance. And sometimes this is discussed in terms of incentives of local officials or whatever, but the governance structure is like the root of

many of the economic problems. And so I think quite appropriately the emphasis of the Third Plenum reform program is really on tackling the governance issues. And you can see this for example in the fact one of the major programs that has actually gotten started is the fiscal reform program, and this has actually I think taken priority over some of the more financial oriented reform programs, and again I think that's appropriate because fiscal relationships lie at the root of many of the problems. So that's the first part; I think that you have to think of this as a governance reform project not simply as a technical economic reform project.

The second point which flows from that is that I think that when we assess how well the reform program is going I think there's a tendency to overlook two elements which don't seem like reforms in a sense, but actually I think lay the groundwork for other reforms. Most important is the anti-corruption campaign which has been much stronger, broader, and more long lasting than anyone anticipated. And I think my interpretation of this is that the anti corruption campaign has several goals, but one of them which I think is not focused on sufficiently is the idea that there needs to be a complete reset of the expectations of what is the tolerable level of corruption throughout the government, because I think the previous panel sort of brought forth a point that corruption is kind of endemic in China. It's to some extent a natural concomitant of a very rapid capital intensive growth process. You can't eliminate it, but there has been not enough systemic efforts to restrain the incentives for corrupt behavior and I think one of the efforts now is to essentially do a reset and lower the bar for what is an acceptable level of corruption or corruption that will trigger some kind of action.

Related to that is I think one of the great achievements of the current government, is to ratchet down the expectations for GDP growth and take some of the emphasis off of GDP growth as the sole indicator of success. And Xi Jinping has been



very vocal through most of the last several months in getting forward this idea of a new normal of economic growth by which he means a much lower number. I think most analysts are anticipating that the final GDP number for 2014 will come in lower than the target rate. The target was 7.5 for the year and probably will come in at around 7.2 or 7.3. This would be the first miss in quite a long time, and I think resetting the expectation about growth at a lower level and also tolerating growth that comes in below a government target is an important step in moving away from GDP targeting which is in fact one of the sources of corruption, rent-seeking behavior, and bad governance at the local level because local authorities had an incentive to focus only on headline GDP growth almost to the exclusion of everything else. So the anti corruption campaign and resetting the growth expectations I think are two important components of the overall program and they kind of set or clear the field for some of the more specific reform measures.

And so the third observation I'd like to make is just if we go down the list I think there's been a tendency among many outside observers in the course of the last year, particularly in the financial community which is what I interact with most of the time, to say well, yes, they had this great plan at the Third Plenum but that was over a year ago and what have they done since? Really nothing has been delivered. And actually this is just not true. If you look at what we've had in the course of the last year, we've had the fund, we've had a Politburo approved fiscal reform program which will redesign the tax system and the local government finance system within two years, and it's really critical. We've had a first step toward a liberalization of the hukou policy, which is a very important move for freeing up labor mobility in dealing with some of the factor price distortions that Yiping talked about. We've had an abolition of registered capital and administrative registration requirements for new businesses which is very important

because again it removes the gatekeeper role of many local agencies, it removes an avenue of corruption, and it makes it much easier to set up a new private business. So if you're trying to reallocate resources into the private sector lowering the barriers of entry to private companies is hugely important. It's already had a huge impact. We had an over 40 percent increase in new company registrations this year despite the fact that economic growth is slowing. So it shows that there was a response to a real pent up demand for new business activities. We've had a further liberalization of deposit interest rates in terms of allowing a wider band in which banks can exceed the benchmark rates given by the PBOC. We've also had the publication of draft rules for deposit insurance which once the deposit insurance scheme takes effect that sets the stage for full liberalization of interest rates. And finally, I think I've left out a couple of things, but the final thing is that we've had a material change in the opening of the capital accounts through the linkage of the Hong Kong and China stock markets.

And I think the important thing is first of all this is a very impressive list, and if you go around the list of other major economies in the world I don't think you can find a single one that in one year has been able to accomplish so much in terms of really basic economic reforms. But many of these things have been talked about and discussed for years and years and years, and sort of were never able to get off the ground. And the fact that they've all moved forward this year I think is a strong endorsement of the government's ability to get things done.

So the final point just very briefly though, is as you can tell I think my overall view on the trajectory now is relatively optimistic, but I think that the scale of the challenge is enormous and I'd just like to finish by sharing a little bit of puzzlement actually that I have on state sector reform, which I agree with Nick and Yiping and several of the other panelists is a really critical part of the agenda. And one of the things that I

find mystifying when you compare the current situation with the situation that Zhu Rongji dealt with 15 years ago is there is a big problem in state owned enterprises; they were a major drag on the economy. And the response to this was a massive program which resulted in the closure or privatization of more than half of these enterprises and the loss of somewhere between 30 and 40 million jobs in the state sector between 1995 and 2005 which -- just to put that in perspective, most of these workers were in industry, the maximum employment that has ever existed in the entire U.S. manufacturing sector was 19 million in 1979. So in the course of 10 years China laid off from its industrial sector about 2 times as many people as have ever worked in one time in manufacturing in the United States. This was a gigantic and massive social dislocation and it was done with surprisingly little unrest. It was an extraordinarily ambitious but also very relatively smoothly carried out program. When you look at the problems of the state sector today they are relative to the size of the economy much smaller. The state sector has shrunk, its employment is a much smaller share of the total, and probably to fix many of the problems in the state sector you would need to create job losses I think somewhere in the neighborhood of 5 to 10 million, which is a big number but it's a lot smaller than we had before. And I'm a little bit perplexed as to why the government has been so reluctant to be more aggressive on state sector reform when the benefits are very clear in terms of improved resource allocation. And the costs compared to the state sector reform that was done 15 years ago would be far, far less because you would have to close a much smaller number of enterprises, lay off a much smaller number of workers, and you're doing it at a time when the labor force as a whole is beginning to shrink. So the prospects for laid off workers on the job market are much better than they would have been 10 or 15 years ago.

So I have to conclude a generally positive view of the trajectory of the

reform process now, but I have a little bit of concern about the apparent reluctance to tackle the state owned enterprise sector component of it. And I do feel that represents one the major locuses of vested interests in obstructions of market oriented reforms. I think we're going to need to see something much, much more aggressive in terms of state owned enterprise reform if the total reform package is to achieve its goals.

MR. DOLLAR: Okay. Thank you very much. So what I'd like to do is start the discussion with a question for each of you, you know, which others can feel free to weigh in on if they are interested. What I'd like to do is start with Qin Xiao. Within a few days we'll get the GDP data, the final data for 2014. The market expects that the 2014 growth rate is a little bit below the target, probably about 7.3. There's a lot of speculation about 2015, will the government set a lower target of around 7 percent or is the government not really able to accept that. And I think that the deeper part of my question is looking at 2015 to what extent are we likely to see stimulus versus reform. There have been some reports in the press about NDRC approving I believe it was 10 trillion yuan, a little bit more than a trillion U.S. dollars worth of investment projects. I can tell a story about why that's not a major stimulus, but certainly there's some speculation in the press about that there might be a major stimulus program. So does the government really accept that the growth is slowing down towards seven, what's your view?

MR. QIN: I think the government is targeted in the short term to deal with the cyclical issues, most of the cyclical issues, when the structural one they want to stabilize their growth rate because the growth was consecutively declining since the second or third quarter of 2013. That's too quick and they will change the expectations of the market. So they want to stabilize, but they do not want to bail out big bail out. (Inaudible) might want, but do not want to bail out. But it seemed to be it gradually stabilized and there are still some implementations of resources could be used fiscally

and currently could be used. So number one I think the next two years will gradually reduce and arriving something like seven were stabilized for some time. That does not mean they are for long run, for the short run, or medium-term run. Number two I don't think the government will have some big ambitious bail out. Number three, I think that's good condition for the reform.

MR. DOLLAR: Okay. Thank you very much. Yiping or Arthur, do you want to weigh in on that first question?

MR. HUANG: I just want to add that you said 7.3 percent is likely below the target. It actually is on the mark because when the Premier Li *Keqiang* said the growth target should be around 7.5 percent according to some officials the definition of "around 7.5 percent" is literally between 7.3-7.7. (Laughter)

MR. DOLLAR: Okay, good; so China hits its target. I always bet on China to hit its target.

MR. QIN: The one thing Li *Keqiang* said is a reasonable range.

MR. DOLLAR: Yeah, yeah, which is sensible. Yiping, my question for you is you said that the SOE issue was not completely fixed which I think there is broad agreement about. So can you say a little bit? And then you talked about the importance of freeing up the factor markets which I agree with, which could indirectly affect SOE performance. But is there a direct SOE reform plan in the Third Plenum or in follow up? What's the plan for SOEs? How is this issue going to be fixed?

MR. HUANG: Okay. I think that the direction of SOE reform is very clear. I thought it was very clear when I read the document from the Third Plenum. The key direction is the management of the SOEs will shift from previously managing personnel managing assets and managing businesses. I forgot. But the key is in the future the priority or the focus will be exclusively management of the state owned assets,

which means the return to the state owned assets will be the most important of concern for the government. I thought if that happens then it will be very good revolutionary change. And one way of putting it is think about traditional SOEs everything is managed by the government, and the new model it might not be very accurate, but think about the Temasek model in Singapore. You have a company which manages really – the purpose is maximize returns of state owned assets without necessarily always getting into the details of the management itself. So I thought it was very encouraging, very revolutionary; however I share Arthur's confusion a little bit. I think since the Plenum there are lots of discussions and different experiments are going on in different areas. It's not entirely clear what really the reforms mean. Now there are a couple of things happening. One is the government is trying to identify different types of SOEs. Maybe they will use a different reform approach which I think is understandable. If a company is in a competitive industry then we should leave it to market, but there are companies in utilities and in strategic industries we'll be using a different approach which I think I understandable.

The second approach is the so-called mixed ownership. That's something I don't quite understand because I thought we already have mixed ownership for all these SOEs which list the companies at the same time, but the idea obviously is to expand the stake of the private sector in these companies. The question to me is does this have a significant impact on the governance, corporate governance. If not then it's not going to be very significant.

So the last thing I think is a little bit disturbing, but which we don't know yet what will be the outcome, is it sounds like SASAC still want to exercise some control, so at least the influences on major corporate decisions. And if that get its way then I'm a bit concerned how much further we can get. So I don't know to be honest.

MR. DOLLAR: Okay. Arthur, Qin Xiao, you want to weigh in on state enterprise?

MR. QIN: Yiping said a lot but I fully agree. I think it has become a political issue or ideological issue rather than simply economic reform. Because in talking about the public ownership and private ownership the first one is social dilemma, second one is capital. Talking about the communist party should rely on its own (inaudible), to build up their governance, the society. But talking about the national security and national interest a lot of – now those words, those descriptions, those definitions sound really clear, it's not logical. So I think it may be the last one to reform because less consensus there, more complicated here. And one thing I strongly believe because as Yiping said, instead of state owned enterprises it is public resources, I mean the capital. The capital is liquidable, movable. If you put in the company that's SOE, we put the social net into the public goods so it does not – if that's the way we shifting from SOE to public resources then we are rationally to calculate where is more needed, where is more efficient. If we look at the fiscal conditions now, it's sound, in terms of debt, in terms of revenue, it's okay, it's good. But in the long run, say 20 years or 30 years if number one there is a big shortage, big deficit for social net, for med care, for environmental issues. And number two, now is a window time. If we too late more costly. So if when they found that we're already had report of this national balance sheet. Let them know if they realize that they have to do that, I mean to take the capital from the SOE to social net and those.

MR. DOLLAR: Okay. Arthur, my question for you -- you're welcome to weigh in on SOEs of course --

MR. KROEBER: That's fine.

MR. DOLLAR: -- but I'll tell you my --

MR. KROEBER: I've had my say on that.

MR. DOLLAR: You mentioned hukou; I think you were the only one who mentioned hukou or you certainly said more about it, and you cited it as one of the areas, you know, where there's actually some progress and important institutional reform. So I'd like you to say a little bit more about your sense of what's happening with hukou reform, but my worry, which I think you know, is that it is very hard to pursue hukou reform in the flagship cities where productivity is actually very high, and in fact the labor force is probably going to start declining in these flagship cities because of China's demographics. So the reform as I understand it seems to be welcoming people to move into third and fourth tier cities where I wonder if they're actually going to get jobs and are they actually going to get the social services that they allegedly are in principle entitled to. So just a little bit more; since you're there on the ground a little bit more sense of what's actually happening with hukou reform.

MR. KROEBER: No, I think that's exactly right. I mean I think just to simplify it, basically what was done in the hukou reform proposal was to loosen the restrictions on people getting urban hukou in smaller cities, but at the same time it was very, very clear that the relatively tight hukou restrictions on the first and second tier cities would remain in place. So basically now you're much more free to move to any city that you would want to move to, but any city that you would want to move to you can't go to. So I kind of share your concern that what we have so far is maybe not quite enough and maybe perhaps even indicative of a potentially misguided urbanization strategy that is unwilling to contemplate the creation of really large scale hub cities and instead is trying to forcibly create much less efficient smaller cities across the country. So I think that's a legitimate concern. For me the very fact though that there has been a specific move to relax the hukou requirements at all is a huge step because this has been talked about for



literally decades and nothing had been done. And I place my hope frequently when I'm in China and frustrated with the progress of developments, at the moment I place my hope on sort of the forcing mechanisms that occur over time. So if you're right that cities like Shanghai and so forth are going to start seeing a shrinking work force soon and literally will not have enough workers to meet their needs, I think this reform even though it doesn't address that problem now it opens the door and it makes it possible for these bigger cities, politically possible for them to relax their hukou requirements in a way that would have been I think inconceivable three or four years ago when there was just this iron restriction on touching hukou at all.

So in short I agree that what we've got now doesn't really get us that much, but in terms of expanding the boundaries of what's politically possible for further reform down the road I think it's quite significant.

MR. DOLLAR: I think that's a good point. It may be that these initial experiments will reveal that it's not too expensive fiscally to provide social services and you can combine it with the central level fiscal reform, and then within a few years you may have powerful demographic needs for more population, for more especially working-age population and you could have a kind of a happy coming together of successful experience in small cities with needs in big cities.

Okay. At this point let's turn to the audience and take questions about the current situation with reform. We've mostly focused on Third Plenum issues, but of course there has also been Fourth Plenum more recently taking up issues of rule of law, ruled by law, so any of the contemporary reform issues are open, except, though, let me just point out the next panel is really about international trade and investment, that's why no one has really said anything about the more explicit trade and investment issues. Let's leave those for the next panel.

And so can we get a microphone right here please. And as usual introduce yourself please.

SPEAKER: My name is (inaudible). I used to be a World Bank IFC person and I'm now a visiting scholar with Peking University, the National School of Development, and also Johns Hopkins SAIS. I one quick comment on the SOE and the institutional implications in SOE reform regarding the employment issues particularly. And I also have a question on the reform, particularly the land market and the rural property reform for farmers.

Okay, the comment on SOE reform, I think it was extremely important to think about unemployment impact as Arthur pointed out. I really appreciate that. I myself didn't really understand the importance until 2003 when I worked in Sichuan with IFC projects. We look at some very large SOEs. These are the largest among the largest SOEs, military, high tech industries. And we realized that a very dynamic company looked like Changhong had one third of their employees that were absolutely redundant, shouldn't exist. And they existed only because of the institutional issues because they belonged to central government ministry management and they couldn't be touched by the local government, but if you let those people go the local government would jump because the burden will be on them. Okay. So at that time it wasn't a thought out issue who's taking the responsibility and the how. Changhong management was very worried about this drag on their efficiency, their international competitiveness; but there was no solution at the time. We saw that similar situation in a lot of the Northeast China cities as well.

So now on the coming reforms I was just still wondering if the panelists could say a little bit more about the rural land property reforms because it was talked for a long time in China, I think all the rationale, the importance was fully discussed and

recognized in China, but it hasn't been done very much. And during and around – before and after the 18<sup>th</sup> Plenary session the advocacy was very strong in both mediums and government documents even, but it seems like kind of faded a little bit again and I was wondering how strong the central government is determined to address this issue because this relates to the local government fiscal problems, it relates to the hukou issue, and it relates to the urbanization issue. And basically half of China's 1.3 billion population still in rural and they don't have clear property rights as the other half who live in the city today, so.

MR. DOLLAR: Good question. And you didn't mention that the issue is very closely related to corruption in China because a lot of the big scale corruption deals with alienating land out of agriculture and developing it and somehow money finds its way into someone's pocket. So who wants to take up the rural land?

MR. KROEBER: Just a very quick comment that it's politically incredibly sensitive. And I think the underlying concern remains that if you move too quickly to fully marketize rural land that you'll wind up having a lot of abuses and a lot of farmers will essentially wind up giving up their land at below market costs. And I think there's some debate about how serious that concern really ought to be, but it is a serious concern. So my perception is that the high level of concern about the socially disruptive impact of an aggressive land marketization scheme has been a real obstacle.

MR. QIN: Before I answer this question about the land property rights we should get clear what we mean by land, okay. There are three kinds of land in agriculture. First it was agricultural land for the rights and we as – it's called right lines. Nobody can change its use. Secondly is the housing of the farmers. The third one is the construction land for the countryside. In the very beginning was for the countryside, the smaller enterprises, but it no longer exists, become part of the urbanization land.

Agricultural land is no touch. It's policy. But still some argue. Some believe we do not need that such big of agricultural land; we can import. That's another story. So we're not talking about that they have a contract to each farmer, they have transferred their contracts with others. That doesn't mean you really own that. You have the use for 50 years or a long time and during that time you can transfer your deeds contract.

For the housing, they're doing this sadly for your own to stay or to leave. You want to go to market, you want to change the zoning. You have some following issues. Number two, it be appreciated the better off should be distributed between the owners and the government. That's the rule because you change zoning. Secondly, there are big differences between those who live in very close vicinity and those who live quite remote from the city. So it creates big differences. So that's the majority of the scholars and the (inaudible) do not want to change this zoning quickly. They still see it as a problem. The third way is construction. Now it's been acquired by government without – on the commercial price it's some compensation, so that's the issue need to be reformed. Number one you can identify this property of the -- the collective property of the farmers. Number two you can encourage them to participate the development rather than just being sold by low prices. That's --

MR. HUANG: Can I just add on the point of the SOE reform and unemployment concern. Obviously that's a concern for any government, but the point I want I want to make is compared to the time in the 1990s that challenge is much less today. And you look at three indicators. Number one we look at the total size of the state sector employment in the total labor force, it's much, much lower now. If you want a number you could look at Nick's recent book. The second point is the labor market condition is very different. At the time when Zhu Rongji laid off so many redundant workers our total labor force was rising by eight million a year, there was massive surplus

labor in the countryside. Today we already turn into a labor shortage problem and labor force has been declining by three million a year. So it will be much easier to deal with the layoff worker issue. And finally if you look at the social safety net, the social security system and so on, obviously it's not satisfactory, it's not good enough compared to what you see in other countries, but in 1998 there was nothing, there was almost zero for social protection. So I would say if Zhu Rongji could do it in the 1990s we are in much, much better condition pushing ahead, but we need a Zhu Rongji.

MR. DOLLAR: Where did the microphone go? Okay. Up here and then I'll go to the back, okay?

SPEAKER: Thank you for that last sentence because my question is for all of you, what influence do you think that Zhu's record, his focus, and his style has had on President Xi if any? (Laughter)

MR. DOLLAR: Qin Xiao, let's start with you. It's a great question.

MR. QIN: He is so capable and so you can compare with Li Peng and Wen Jiabao. He is so capable. Whenever he made decision he'll do that. The implementation ability is first class. And secondly before making a decision he's open and willing to listen. Sometimes even consult some expert abroad. That's second one. The third one, sometimes he knows he has to make political decisions, it's not bureaucratic, it's not technical. For instance WTO. If you rely on the expert they will see thousands and thousands of problems. It's a political decision. So if you want to have the TPP with U.S. and other countries you need American leaders have political decision. What we mean, "political decision?" He know the direction, he know it's a window of time. Miss this opportunity or miss forever. And he will know there are risks and he will take the risks.

MR. DOLLAR: Okay. Let's go to the back. I don't like to discriminate

against the back. There's a woman holding her hand up there; yeah, her left hand, yeah.

SPEAKER: I'm (inaudible) with Xinhua News Agency and I want to ask a question about hukou reform. And the hukou reform is still restricted, labor -- or to enter the big city, but it turned out that the job opportunity created in the big city are much larger than the small city, so how can the government tackle this kind of dilemma? Thank you.

MR. DOLLAR: Arthur, you already made some intelligent comments so can I ask --

MR. KROEBER: Okay, sure.

MR. DOLLAR: -- Yiping or Qin Xiao?

MR. KROEBER: Yes.

MR. DOLLAR: And then you can come back in.

MR. KROEBER: I'm fine.

MR. HUANG: I'm actually not an expert but I think for any government if you want to open up this reform you have to have a starting point. The starting point is in the larger cities, we're already suffering from major pollution problems and traffic jams and also some problems. So, yes, I agree. I think the larger cities should expand because of the greater opportunities there, but you need to fix many of the problems and ease the constraints so that you can actually do much better job. This is why at the moment I think the reform probably will start from relatively smaller cities, but I share your concern. I think we shouldn't go to too small size cities in the country because that will be detrimental actually to the skill efficiency. And even if you talk to people, migrant workers where they want to settle they actually normally don't want to go cities too small because these areas with very limited not only job opportunities but also education opportunities for their kids. So I think we should -- but what the government is facing is to

strike a balance between already overburdened infrastructure in the larger cities and the lack of interest in some of the smaller cities. And I think gradually the two have to converge over time.

MR. DOLLAR: Anyone else want to weigh in on this?

MR. KROEBER: No.

MR. DOLLAR: Okay. This woman here.

MS. JONES: Hi, I'm Lynn Jones from U.S. International Trade Commission. I have a question regarding to the SOE reforms. In the past SOE reform has seen a large decrease of the SOE numbers as well as the emergence of large SOEs through the consolidation. So my question is what characterizes the approach and the objective of the current or future SOE reform? So it's going to be for the improved productivity and the profitability of the SOEs or reduce the size of the state sector, allow more competition from private companies in those industries that SOE dominant or monopolize or both. Can you elaborate a little bit? Thank you.

MR. QIN: First of all we should distinguish the SOE from between the macro labor and micro labor. When we see (inaudible) labor, capital labor, our (inaudible) governance, productivity, innovation, but for the micro labor, the (inaudible) labor, they should reform the institution. For instance the mixed ownership or they ask them to put their profit and losses in budget and to distribute their dividends, and allocate certain of their assets of stock in social net. So that's two levels. I just said they already had produced some (inaudible) and ideas, it's still in – now it's on the way, but ultimately it takes some time to have real reform. So I don't have high expectations for SOE reform, but I do believe they will reduce the number. They will have more mixed ownership.

MR. KROEBER: Just a quick comment on mixed ownership plan. I frankly find it very difficult to understand. So basically the idea is that provinces are being

encouraged and most of them I think have already published plans to introduce mixed ownership system to the majority of the state enterprises under their supervision. And at least at the outset what this means is that outside non state shareholders will be invited to take minority stakes in these province or county or municipal level SOEs. And the problem that presents itself is that a lot of these enterprises are in not very good financial condition. It's hard to understand why any outside investor would take a minority non controlling stake in these not very good enterprises unless they get some promise of management control which does not seem to be on offer. So like why would you do this? So this is one of the things I'm – so it seems like either this is like some kind of compromised solution that no one really knows how it's going to work or it is devised as kind of like the first stage to privatization and it's politically necessary to use this term mixed ownership because politically you don't want to use the term privatization. But I think this is one of the very big question marks that everyone has that on the face of it this program does not – it's not clear how it could possibly succeed at doing anything. So we'll just have to see how it works out.

MR. DOLLAR: Okay. How about one more question; this gentleman here.

MR. BUTLER: Hi, my name is Steve Butler. Could you sketch out the sort of practical implications of going down to 7.3 or possibly 7 percent? Which sectors of the economy are hurt, how much do they have to worry about it and to what extent is it really a constraint on further reform?

MR. DOLLAR: I hope everybody wants to weigh in on that because – I'm going to try to wrap up a couple of moments before the – the program says 10 minute break, I don't think a 10 minute break is realistic so I'm trying to buy a few minutes so we can have a slightly longer break and resume at 11:45.



MR. QIN: It is Yiping.

MR. DOLLAR: Okay.

MR. HUANG: Well, I think this actually is an interesting question.

Looking at my own papers, you look at the Chinese economy, it's actually been slowing gradually, but if you talk to people on the ground you find the feeling is actually much more painful than the headline numbers indicating. So from 8 percent to 7.5 percent, from 7.5 percent to 7.3 percent, these are like very limited changes, but the pain sounds like immense. I think there are at least two reasons why this is happening. You look at the Chinese economy last 30 years – 36 years, economists like to say there are 3 engines of economy: exports, investment, and consumption. And the economy is being mainly driven by or led by growth of investment and exports in the past and most of them concentrate in the manufacturing industry. So we've been at the global manufacturing center for quite a while. But you look at these economies today we are facing major difficulties in these areas. Number one, after the big stimulus package introduced in 2008 we are seeing rising over capacity in the heavy industry which used to support investment activities and now the economy is slowing, investment is slowing. A good example is to look at what happened in Australia, but the heavy industry, the steel, INO aluminum, and the copper, cement, building materials, these are the areas where we suffer from major over capacity problem. Obviously it will be difficult because they are being a backbone or a main driver of economic growth. That's one part of the economy. The other part of the economy also is suffering from economic difficulties. The labor intensive manufacturing industry which has been the main driver of exports, again a growth engine of the Chinese economy. The reason why the export sector is facing difficulties on one part because the global economy is recovering very slowly, but mostly importantly because we are entering into the high middle income range in the world, the

so-called middle income trap. So at the beginning of the reform our GDP per capita was 200 U.S. dollars and whatever you can produce it will be competitive in the market. But now it's 7,000 U.S. dollars. Whatever we've been doing successfully in the past no longer competitive. And I think that this is the big challenge we are facing in the economy. So what I'm telling you is the economy has been very successful in the past and mainly driven by manufacturing expansion, but the two key successful stories in the manufacturing industry now is facing huge difficulties and this is why I think we probably going to see further adjustment. Whether or not the economy can be successful according to this so-called middle income trap is whether or not we can rise.

My overall assessment is I'm not that pessimistic actually. I think we already start to see positive changes in the economy. So for instance you look at the consumption share of GDP is already adjusting. The services sector is already bigger than manufacturing sector. That's why when the economy is slowing employment is not a challenge so far. Most importantly, innovation is happening. You look at the online shopping, look at internet finance, you look at faster delivery, you look at these cheap mobile phones, and manufacturing and so on. Actually we've seen lots of positive stories, but when we are pessimistic we tend to ignore all these stories, but I'm sure you heard about Alibaba. We just don't put them into the same picture as the macro story we're looking at.

So a short – just a quick summary of my answer to your question is I think of many of the traditional areas we will continue to see difficulties. We needed to deal with the overcapacity in the other areas already exist, we needed to upgrade the low end of manufacturing in order to survive, but I do think we actually are seeing industrial upgrading and innovation already. But obviously we still needed the big reform program to be implemented to sustain this process.

MR. DOLLAR: Arthur?

MR. KROEBER: A couple of just quick additional observations. One is if you look at the composition of the slowdown it's clear where it's occurred. Between 2000 and 2012 the average annual real growth in capital spending was about 15 percent a year; that's now down to about 7 or 7.5 percent. So the growth rate in the investment side has already fallen in half. If you look at consumption, the average prior growth rate was around 8-8.5 percent in real terms and that's down to about 7.5, so it's also slowed, but substantially less and that reflects the rebalancing that Yiping has indicated has already occurred away from the heavy industry toward more consumer services. And I think that trend will continue.

Just one quick note from the standpoint of analysts of this, it's a real problem because the data on the parts of the economy that are in trouble is very, very good. We have an excellent industrial survey; we have very comprehensive investment data that enable us to state with exact precision just how terrible things are in the traditional part of the economy. In the new parts of the economy such as the internet and all of these consumer services that Yiping referred to, the data is much worse and in the service sector generally we have very, very poor data. So we have only a very fuzzy picture of how things are changing for hopefully the better in these other sectors. And that's just to reinforce Yiping's point that I think right now we're at a point where there's a little bit of intrinsic bias in the analysis to focus on the negative because that what we conceive very clearly. And the positives we think are there, but it's a little bit harder to put our fingers on.

MR. DOLLAR: Okay. I think we're going to bring this to an end. As I said I wanted to buy a few minutes so we could have a nice tea break. The last session is going to be on U.S.-China trade and investment opportunities which is a great topic

and my colleague Jeff Bader described that as the future. So hopefully the future will be a much closer trade and investment integration between China and the U.S. So let's take a short break and then we're going to start promptly at 11:45. Thank you. And let's give this group a nice round of applause. (Applause)

MS. DOBSON: Hello.

SPEAKER: Just start speaking in the mike.

MS. DOBSON: I was going to go over the mike, but I'm tethered here, so I'll do it from here. I'm Wendy Dobson. I'm from the University of Toronto, and I'm delighted to introduce our last panel, which very much turns -- well, it's going to talk a little BIT about the past, but we're going to look forward to a future that is unfolding as we speak.

We're all aware of the regional and the mega-regional trade in investment initiatives. We're going to talk about those within the context of China's reforms; the economic reforms, and what we've also talked about today.

Now, it's difficult to see an economic future which does not have at least the possibility of the U.S. and China hopefully deepening their economic relationship, as the ties that bond and perhaps raise the costs of outright conflict.

The way we're going to proceed is with our three panelists who are in your program, Jeff Schott, Lu Feng and Peter Petri. So, Lu Feng, I'm going to ask you to begin with, and each of you has eight minutes, and then I will then lead off with some questions and some conversation, and as in the previous panels, open it to the floor.

And we're aiming, boss, to have us out of here by one o'clock. Is that right? So, Lu Feng, would you like to lead off?

MR. LU: Okay. Thank you. This session is mainly about the trade and the investment relationships between China and the U.S., and largely with the rest of the

world. I think that is one of the very important issues for China in the coming years. I would like to talk about this issue at three points.

So first, of course, we're looking forward, but sometimes, you know, and remembering the historical lessons gave us some inspiration and helps to look forward. So, if you look at the past at China's economic reform history, initially, actually, economic reform, many agricultural sectors and opening up many in the special economic zone, they're motivated by different motivations, and they started relatively independently.

After that, you know, you can see a clear pattern emerged by which reform, on one hand, and opening up, on the other hand, interact really subtly a mutual strengthening. Sometimes, process -- progress in the reform agenda makes China possible to open further. Okay? Deepening opening up.

On the other hand, sometimes opening up has been used as a major dragging force to push forward a reform agenda domestically. So, in the preview sessions, we discussed a lot about Zhu Rongji's legacy. One of the legacies is, you know, to use in the opening up for the reform domestically. After he assumed the premiership, he went to push forward a reform. But there's a lot of resistance from various vested interests as well as the ministries are very strong, indeed. Especially, he wanted to break up the monopoly in certain sectors, including the telecommunications sector. That's a strong you know, resistance, against his efforts.

So, I think one of the major factors, not all, behind the opening up especially, you know, make a bid, a fresh bid to succeed. The accession of WTO is to push forward domestic reform. This is why he made the visit to this country in 1999.

He offered very attractive, very comprehensive terms and conditions and try to have a deal with the U.S. as bilateral talks. But unfortunately, he did not get what he wanted, because maybe technical considerations on this country. You know? And it

failed.

But he did reach a very important agreement on a culture sector which laid the foundation to conclude Sino-U.S. bilateral accessions. I think if you're looking back, WTO accession, which has been helped greatly by Zhu Rongji's visit to this country in 1999, helped a lot to advance the domestic reform agenda, you know -- between the centuries, which also helped tremendously, the successful development you know, performance in the Wen Jiabao's period.

That is the -- first of all, I just want to emphasize the opening up, and also, especially, to improve the healthy economic and trading relationships with the biggest country like the U.S., is crucially important for China, not only for opening up of China's economic existence, but also, deepening the domestic reform agenda.

Secondly, now, we face another round of the reform and opening up. Actually, it is well discussed and also commenting on the previous panelists, you know, and over the last decade it was -- in the first beginning or in the first decade of the new century, Chinese economic development has achieved great success in a lot of aspects of economic development, for a lot of reasons, domestically as well as politically, the economic reform agenda has not proceeded as quickly or as comprehensively as we expected or wished.

So, it's the legacy, you know, from the premier's history. So, it imposes a very urgent task for the new leaders as well as the society at large to proceed reform urgently, to break the bottlenecks of the institutional transformation as quickly as possible, to establish or complete the reform process. This is why we can see what we see.

The new leaders, they put a very high priority in the reform agenda. But in order to do that, we need the further reform. So, I think that presents a broad context in

which China and the U.S., the two biggest countries, wish to improve their relationships on an institutional basis. Okay?

A lot of the bilateral and the regional FTR agreements or negotiations are in process, but unfortunately either TPP or (Inaudible) have not included China and the U.S. on the same platform. So, that explains why I think the two country leaders pay a very high price or priority to the -- currently going on these bilateral investment treaty negotiations.

I think, of course, that may be challenging for China, okay, to fulfill the requirements to make which where -- make successful conclusions of the BIT, which has been mentioned in President Xi Jinping and Obama's summit in Beijing at the end of the last year.

But not also presence -- called an opportunity to push forward the reform agenda in China. Actually, we all know that there's a comprehensive reform agenda laid out by the third plenum reform, as well as you know, that the ruling at the reform -- the reform on ruling a rule to achieve the rule of law and to force a plenum reform.

So, in order to do that, I think further opening up, especially in negotiation with this country in terms of the BRT, and it would be very helpful and provide a very positive impact on that.

Thirdly, I would like to add another major area which may also produce a positive impact in the bilateral relationships between this country and China, which also helps, which also right -- relevant to the current subject of this session. That is the agricultural liberalization in China which has been not focused, but I think there was a lot of potential.

If you're looking back over the last decade or so, China's agricultural inputs have been growing tremendously. The total inputs increased from \$1.1 billion U.S.

dollars in 2000 to something like \$140 billion U.S. dollars, okay, in the year before last year, 2013. Okay? Especially, the soybeans. We all know that.

In recent years, China's annual soybean implementation has been increased to the figure, something like 65 million tons, five times of the domestic output in recent years. It's unbelievable, if you go back 20 years ago. In this country -- this country is a major trading partner in terms of agricultural trade.

The inputs from the U.S. by China increased from something like one billion U.S. dollars, okay, in 2000, to something like 7.5 billion U.S. dollars -- to something like 11 billion U.S. dollars a year before last year. I think it's tremendous progress, because China is undergoing reorganization and industrialization, and because the structural affective changes in terms of the labor cost, in terms of the relative scarcity of the land resources, as well as because of the persistent appreciation of the IMB as a matter of the chain.

So, I think that is a structural change, also beneficial to the two countries, because in this country, it's obvious if you -- because in recent years, the net inputs by China from this country is something like 7.5 billion U.S. dollars, if you calculate on the basis of assumption that a quarter million U.S. dollars proceeding of exportation will support one farm job.

Then, you can say these kinds of exports to China can create another 30,000 farming jobs. On the other hand, it is also very good for China in economic terms. It helps China in a raw interest of economic development, because for example, we input the soybeans something like 65 million tons of the soybean. Not this equivalent -- if you use the output yields in China for the soybeans, you can see that saves something like 700 million more, which is one third of the soy area of China, okay, in the land.

So that means, you know, we saved the way -- imported a huge amount



of the land and water are the resources, okay, for China. That is good. But on the other hand, because the current agricultural regime is very protective in nature, so China also increased the subsidies in the agricultural sector, also priced in the regions -- how can I say, produced huge gaps in the agricultural presence domestically and internationally, I just want to say, China and the U.S. can make huge progress if they can have the FTR to negotiate the agricultural -- make a mutual okay, reform in agricultural sectors to further advance the agricultural regime in this country.

So, generally speaking, looking past, and I will say looking ahead, I think the collaboration between China and the U.S. in trade and investment will be very important and have a lot of potential. Okay?

MS. DOBSON: Thank you for those three points. Jeff?

MR. SCHOTT: Yes. Thank you very much. A very difficult act to follow after Professor Lu, and I will try to be as succinct and substantive as his comments.

I also want to send the regrets of my colleagues, Fred Bergsten, who had hoped to join you today on this panel. He faced urgent family matters that prevented him from being in town today, and hopefully, I can be as substantive, if not as provocative, as he would have been in this presentation.

He was going to speak off of a new book that he co-authored, "Bridging the Pacific," which is really about the topic of this panel; about how the United States and China can work more closely together for our mutual benefit going forward.

The topic is a very important one, and even more so, if you think back just 20 years ago, U.S.-China trade and investment relations could only be characterized as primitive, but spurred by the political commitments to economic reform by Chinese leaders that we have been talking about this morning. China began a rapid and dynamic process of integration into regional and global markets.

Of course, there was a big push in that direction with China's accession to the WTO. The United States really played a principle role in negotiating that accession in the 1990s, and as Professor Lu said, this was really about complementing what China leaders wanted to do at home to propel domestic economic growth. Domestic policies drove the interest and desire to complement those policies with international economic arrangements. It wasn't the international agreements driving or pressuring.

And I think we see a very similar process unfolding today with regard to the international economic arrangements that have been negotiated by China, or are in the process of being negotiated by China. This process has been evolving over more than a decade.

China has negotiated numerous trade agreements, mostly with its Asian neighbors; mostly very low quality, but there has been an incremental improvement in the scope and depth of liberalization in the agreements that have been negotiated, starting from a very low base of the China-ASEAN agreement, and building up to more recent agreements with New Zealand, with Australia and the recently announced agreement with Korea, which actually hasn't been concluded yet. They're still negotiating the final parts. So, the negotiations have been announced as completed, the negotiators will soon complete the negotiation.

That said, what's included in those agreements do not drive or complement the new reforms in China very much. They are not of sufficient scope and ambition to really make a difference in the calculus of how you pace the reform, how you deal with adjustment in a Chinese economy. But the interest in working with the United States, in deepening economic integration in the Asia-Pacific region could have that type of impact.

And right now, if you look at all of the arrangements, as Professor Lu

said, really, the one outstanding characteristic is, none of the existing economic integration arrangements in the Asia-Pacific region include both China and the United States. There is a reason for that. We've had very rapid growth in our bilateral trade over the past 20 years. It's grown almost tenfold from about \$65 billion total to aid merchandise trade to over -- around 600 billion.

But the bilateral trade deficit that the -- the U.S. bilateral trade deficit with China has also grown substantially and now is well over \$300 billion. Of course, economists at the Peterson Institute and Brookings will tell you that doesn't matter. It's the broader current account situation.

But the enduring large deficits with China do contribute to a harsh debate and scrutiny by the Congress and affect the political possibilities for deepening our economic relations.

So, you can say almost that there is somewhat of a mistrust in Washington about the ability of China to pursue, implement and enforce economic reforms, and there is a mistrust in Beijing about the intentions of the United States and the willingness of the United States to open up to Chinese enterprises, particularly in the area of Chinese investment in the United States. And that is a topic of current discussion in our ongoing negotiations on the bilateral investment treaty.

There are some challenges moving forward, and indeed, the purpose of the study that Fred Bergsten, Gary Hoffbauer and Sean Minor produced was to try to get a better -- more information and greater clarity on the nature of the problems confronting U.S. and Chinese officials and enterprises, but also, the great opportunities for what can be done to remove restrictions, lower transaction costs and hopefully, pave the way for more beneficial trade and investment between our two countries.

The most direct way of doing so would be through a bilateral free trade

agreement. And yet, while this would make sense for an economist, when you factor in the political participants in both Washington and Beijing, it will require more preparation. But just thinking about it and beginning to understand that the scope of the problem in substantive terms, is not as great as one would have imagined just 5 or 10 years ago, I think is very important and deserves much more attention.

And I think the discussions that we've had, and even the discussion on agriculture and the subsidy problem shows that there are ways of resolving this that are not as insurmountable as one would have thought just a few years ago. Now, there are various channels for doing this. There are ongoing negotiations in the Asia-Pacific.

Again, the U.S. is participating in the most comprehensive one, the Trans-Pacific Partnership, which talks include 11 other countries and are nearing completion. I suspect that there could be some announcement by the spring of substantial completion of the negotiations.

China has been examining -- Chinese officials have been examining these negotiations very carefully over the past two years, and U.S. and Chinese officials have been discussing them very intensively during this period, so that there is a greater understanding of what is going on.

I think this is an important component of our bilateral economic relationship, which sometimes is underestimated, that we now have a much deeper flow of information and consultation that avoid the misunderstandings that used to dominate our bilateral trade relationship. And this goes on in the JCCT. It goes on in the strategic and economic dialogue. It goes on in the various bilateral meetings -- numerous bilateral meetings that our leaders have in various forums all over the world.

There are ways of dealing with this, and in a regional context, as well, and indeed, China led a very important discussion of bridging the Pacific in terms of new

international economic arrangements in APEC that could be supported by APEC during the year that China was the chair of APEC in 2014, and produced a number of important studies, one of which Peter Petri was a key coauthor and coeditor on trying to understand what are the options going forward for U.S.-China engagement both at the bilateral, regional or even multilateral level.

I think there are lots of opportunities, and perhaps, since I've used up my time, I'll turn it over to Peter, because he's got the answers (Laughter).

MR. PETRI: Thanks, Jeff.

MS. DOBSON: Thank you, Jeff. So Peter, what are the answers?

MR. PETRI: Well, this has been a fascinating morning, and I really enjoyed hearing some of the anecdotes about the Zhu Rongji Era, and it occurred to me as I was listening to this, that in the international arena, in the international trade arena, we are, in a sense, at the end of the Zhu Rongji Era; that is, the institutions that he helped to put in place; the China accession to the WTO and the enormous increase in China's presence in the world economy that followed were, in a sense, the product of the Zhu Rongji innovations that we have discussed in many different ways earlier.

But today, we need a new framework. We have sort of run to the end of China's accession to the WTO, sticking with the WTO rules as they were defined, really, in 1994. We have run the end of that era.

There are a lot of new frictions that we are dealing with and that we have to address, and we need a new framework, a new paradigm.

And I think that in that context, the notion of a free trade agreement that ultimately includes China and the United States and perhaps, many other countries, is a very, very strong paradigm. It's not going to happen soon. It's going to take an enormous amount of work, but I think one can begin to see elements of that picture

emerge all right, today.

The first point that I want to make is that the context in which we discuss these issues, the actual facts on the ground are changing quite rapidly, and I'm not sure that our politics has quite caught up with them. During, from 2001 or just before China's accession to the WTO to 2007, Chinese exports to the United States grew at an annual rate of 21 percent a year.

Since then, they have been growing at 5 percent a year. So, it's really quite different. The U.S. exports have been growing very fast, as Jeff says. The bilateral trade deficit is still large. My guess is that it will be always large, due to the triangular trade that involves China, the United States and other countries. But the speed of change has really slowed down, and we are in a maturing relationship.

If you want to look at that period of the 2000s, it was when trade was opened up, as we academic economists like to say, between China and the rest of the world. Now, it's a maturing relationship growing much more slowly, and even if you look at the composition of trade and you look at the rate at which that is changing and becoming more sophisticated, even that is slowing down.

So in a sense, we are reacting to some extent in American politics, but I think also in China, to that era of extraordinarily rapid growth and change, even though in some ways that shock of China entering the world economy and becoming a very powerful part of it; even though that shock is now, to a large extent, behind us.

China's importance is not behind us, by any means, but the shock of its entering the world stage in a very rapid way, causing large adjustments also, in the United States, which is what part of the political concern is about in the U.S., that is behind us.

And in that process, also, the old frictions, which have typically involved

conventional sectors of the economy; steel wire, tires, the most recent of them was solar modules -- these are sort of looking more manageable now. We have a whole new set of frictions, however, that are not so manageable.

Currency belongs on that list, although for the time being, the currency problems are retreating. But cyber security is very much on the top of that list. I would add to that, industrial policy and the various forms in which that manifests itself, including the anti-monopoly rules in China, and most of all, investment.

These are what trade negotiators -- some of these are what trade negotiators call the 21<sup>st</sup> century issues. These were not covered by WTO version 1994. They will have to be covered by a new set of rules of world trade as we move forward.

And these are the issues that I think are on the minds of Chinese and U.S. negotiators. I'm sure they come up at every JCCT or SNED, all of the bilateral consultation mechanisms that we have developed, and all those issues that ultimately will have to have a framework of rules, not so much to prescribe exactly what countries do, but more that they have a mechanism for discussing them, if possible, dispute resolution mechanisms to diffuse disagreements, if they arise, and essentially, we put on a kind of routine basis, much as the WTO put the sectoral issues on a routine basis.

It doesn't mean full agreement. It means continuing friction. But when you look, for example, at anti-dumping rules that the U.S. applies on Chinese products, they account only for about 3 or 4 percent of the trade between the countries. So, they are there. They're not completely put into the past, but they're managed. And so it will have to be with these new issues.

Now, let me then turn finally, to how this might be managed. I think the issue of a large free trade agreement is a very important benchmark, in a sense, a paradigm. But it is obviously not likely to be happening soon. But in the meantime, it

gives rise to a series of topics that hopefully, we can deal with bilaterally and increasingly multi-laterally. And the BIT is perhaps, the most compelling and the earliest one of those.

And we might do that, as Jeff mentioned, bilaterally, but probably not just bilaterally, also regionally, and to some extent through the WTO plurilateral process, as well.

Let me close, just very quickly, on the FTAAP, the Free Trade Area of the Asia-Pacific, which Jeff mentioned, which came up as a very prominent issue in the APEC summit a month or so ago. What was interesting about to me, I think, from the viewpoint of reading about it in the United States, is how curiously misrepresented it was in the press, in that it became a kind of contest between the TPP, which the United States is struggling to complete, and the FTAAP, which China was promoting.

In fact, this is an idea which several generations of APEC leaders have endorsed. Its origins, in a sense, go back to Fred Bergsten's committee --

MR. SCHOTT: Yeah.

MR. PETRI: -- in 1994, which led to the Bogor declaration at the time within APEC, and it's an idea which George Bush, the second, brought to the APEC forum in the mid 2000s. So, it's an idea in which both countries have had a long history of support, and I think it provides -- the outcome of the APEC meeting is actually very good.

It's a two year study which will, presumably by then, much of the TPP work will have been done. It will involve a series of studies both within and outside of the APEC process, and hopefully, it can provide a roadmap for how to bring all of these issues together.

Bilateral progress between the United States and China on these many issues will be very critical to setting the stage for a successful larger agreement. But



such a larger agreement, particularly in the Asia-Pacific context, would have very, very clear benefits and will have shared ownership, which I think at this point, is going to be pretty critical for the rules that we set for the next stage of world trade.

The last thing I wanted to say is, I think Ken Lieberthal earlier hurt my feelings quite a bit as an economist (Laughter) by saying that comparative advantage may not have been the critical issue in China's accession to the WTO and the benefits that followed. At some level, I agree with that, but I want to defend comparative advantage, even the economic gains from a large agreement, that for example, would stretch across the Asia-Pacific, would be quite large.

We have been estimating that, and actually, part of that is in the (Inaudible) at about \$2 trillion, of which maybe half of a more ambitious, more inclusive agreements, of which about half would accrue to the United States and China; more to China than to the United States, because there are more distortions to remove, more expansion to support. But still, very positive benefits to both countries. Thanks.

MS. DOBSON: Thank you very much, all three, for introducing a whole range of issues, and I'm going to ask a few follow up questions, and then open this to the floor.

Maybe I'll start with Lu Feng, and take you back to both Jeff and Peter, sort of skirting around the issues of -- but very positive about the possibility of a bilateral China-U.S. free trade agreement, and as Jeff suggests, this is a way -- working towards this is a way to help resolve differences and build understanding.

How do you see such an idea as relating to the reforms that you have spoken quite positively about? In your remarks, you talked about the BIT. This would be much broader.

MR. LU: Yeah, I quite agree with Peter Petri's suggestion, that these two

largest countries need to have sought after bilateral talks on the institution of arrangements for the new decades and the new environment.

If you look at the current situation, the status quo, we see a lot of the regional and bilateral free trade agreement on the close economic relationships going on there. You know? Of course, that is the result in part of the failure of the successful completion of the Doha round. So, we cannot push forward bilaterally on global trading and liberalization in the process, so we go to regional.

But for a lot of reasons, you know, as we discussed, these two countries don't have opportunities to directly talk to each other, but they have their own agenda, you know, specific talks. In your country, you have the TPP. In Asia-Pacific, you know, our country, we have a lot of bilateral talks, but also ASEAN you know, regional talks through FTA.

So, as Yiping commented in the early piece of paper, he alarmingly commented on this situation, is the risk of another economic Cold War. Okay? Maybe he just wanted to remember; it's not a desire in this situation. So, in order to avoid that, I think we need new talks between us directly to address all of these -- you know, and the emerging issues.

It's quite different from what we talked about more than a decade ago in WTO accession. For example, I think these kind of talks are not only echo Sino-U.S. relationships in a more stable institutional setting, which can be very helpful for us in the coming decades, but also, as I emphasized just now, for domestic reforms inside China.

For example, China now needs to streamline an administrative intervention, including a lot of industrial policies mentioned by Professor Petri. You know? The ministries or administrative agencies, they're (Inaudible) government -- economy using a lot of the international industrial policies.

I think to change the situation, of course, they can have the domestic reform, but also, they can combine with the opening up agenda, you know, because the new generation of the free trade arrangements, they would address broader issues like that, including the investment opportunities.

We know that this country is the largest FTR overseeing development investment in the country, but also, China emerged as a very big ODR country. Last year, ODR, total score of the ODR succeeds -- how can I say, surpassed the FTR becoming one of the major fully directed investment countries.

So, I think talks on these areas for the liberalized environment between these two countries in terms of the direct investment will help China in this area. So, I think there are a lot of areas -- direct talks in these two countries in terms of the bilateral free trade arrangements can help dearly, greatly.

MS. DOBSON: Thank you. So Jeff, you've been involved -- one of the things that you may not know about Jeff is that early in the decade, starting around 2000, Jeff actually fielded a study process with Koreans -- a Korean institution on the possibility of what came many years later, the Korea-U.S. Free Trade Agreement, KORUS.

MR. SCHOTT: Uh-huh.

MS. DOBSON: So, Jeff, why don't you tell us a little bit about the genesis of that process? And before you end, can you also give us an idea of your views on the recent China -- Australia and China, South Korea free trade agreements? As you pointed out, the Korean one is not yet finished.

MR. SCHOTT: Right. Well, there are some interesting parallels, but also important differences in the experience that the United States had with Korea going back 15 years now.

Fifteen years ago, when I was actually asked by a senior official of the

Korean government if I would examine the pros and cons or the challenges of negotiating a bilateral free trade agreement between Korea and the United States, the United States was not interested in considering it, because Koreans were not going to discuss agriculture. And as I did my research in Korea, I found that almost nobody in Korea, except the minister, who was asking me to do the study, actually was supportive of a free trade agreement, because they had strong protectionist interests.

But the objective of the exercise was really to find a way to instill more competition in the Korean market. So, a lot of it was about, how do you encourage foreign firms to invest in Korea.

How do you remove the barriers to that entry as a means of spurring more innovation and productivity growth by domestic firms, but also, bringing in new ideas, new technology into the country.

This was really a way of saying -- the KORUS FTA was really about how do you open up the Korean market to foreign direct investment. Now, in the China context, we're pursuing bilateral investment treaty negotiation, and that has been going on since 2008, and not much happened for the first five years, in part because of different concepts about the scope and coverage of the prospective pack, but also, because the United States was revising its model bilateral investment treaty; sort of a template for what U.S. negotiators expect their trading partners to undertake in an agreement.

And this is a very high standard agreement and goes beyond the normal investment provisions of a traditional investment treaty, but it includes provisions on environment and labor and the like.

So, it's a very high bar. This is something that is posing a big challenge for the negotiators, and indeed, it's not just a problem that China has. The United States has only concluded and ratified two bilateral investment treaties over the past 10 years, with

Uruguay and Rwanda (Laughter).

And part of the problem is the high level of expectations of the agreement, but the other problem is the complications of the U.S. ratification process, because as a treaty, a BIT requires two thirds vote by the Senate, so it doesn't go through Congress like a free trade agreement. And many countries, including Korea thought that a better way of proceeding was to put the investment provisions in a more comprehensive economic arrangement, a free trade agreement that covered trade and investment, and then, go through the still difficult but perhaps, less daunting process of implementing legislation of a free trade agreement.

And so, that's one of the options that we have as we move forward with our investment talks with China, seeing whether this can proceed as a standalone investment treaty, or whether the experience gained and the convergence of positions can be included in other types of agreements, like Peter was talking about.

MS. DOBSON: And my other question, Australia and Korea with China -  
- how comprehensive are these deals?

MR. SCHOTT: Well, the texts are -- the Korea text with China is not out yet, but without giving you a long-winded and not useful answer, suffice it to say that these negotiations had a political imperative to conclude quickly by both sides. And when faced with that political imperative, the negotiators had to cut corners and push some things off the table that otherwise would have been included.

So, there are extensive exceptions, and in some areas where the nature of the commitment is not as comprehensive or as forceful as had originally been hoped. So, they moved the process politically forward quite a bit. They moved the process economically forward a little bit.

MS. DOBSON: Thank you. So, Peter, what would you prefer to see?

You're the one that has done a fair amount of work on the various options, ranging from a China-U.S. free trade agreement to something more phased and more comprehensive in the sense of involving others.

What do you think makes most sense as the default, I guess?

MR. PETRI: Well, what I can give you is kind of brief thoughts on preferences that I would have.

MS. DOBSON: Yeah, yeah.

MR. PETRI: And some of the reasons for that. I think predicting these things is very difficult, and I don't --

MS. DOBSON: I didn't ask you to predict.

MR. PETRI: I don't think I can do that. To me, the idea of an Asia-Pacific regional agreement which includes China and the United States and provides a kind of umbrella that weaves all of these disparate, important economies together is very attractive.

It's attractive first of all, politically, because it's in some ways, a fragile part of the political landscape -- a fragile part of the geopolitical landscape. And I think giving that group a very solid, positive sum game which a free trade area would represent, is not going to solve political problems, but at least it's going to tilt the balance towards solutions that I think are politically desirable.

Second, this is what economists would call a natural trading block. We have in the economics a profession, a kind of debate between those people who say that trading zones or free trade areas are potentially bad, because they exclude important countries, versus those who argue that yes, they may exclude some countries, but within them, they generate sufficient trade to make the benefits to the world as a whole very positive.

And this group of economists, which is generally in the Asia-Pacific regions very clearly falls into the category blocks where internal trade creation is likely to dominate almost any other negative consequences, and we will have then, the resources to compensate countries or to include countries that might be hurt by that. So, it's economically a very desirable one.

And finally, this is just a very important part of the world trading system. Its demonstration effects, its ability to dynamically bring other countries on board across the world, to help to spread the rules that our development is reaching to the world is very high, because everybody wants to trade with them. They're a very important part of the global system.

So, it's I think difficult, but there is a lot to be said for it. One important early issue that will come up is membership. The APEC FTAAP group, the 21 member group, for example, includes Russia. It's going to be a difficult country to negotiate with.

It doesn't include other important Asian economies like India, but there is nothing about the APEC process that would tie such a regional free trade agreement directly to APEC in terms of membership.

So, it could have fewer members, it could have more members, and I think that it's a vision. It's going to take time, but I think the effort over these next two years to take stock of what might be possible, I think is attractive.

MS. DOBSON: My final question, so I'm coming to you, the audience, next. It's a tough one for Jeff, but short. Can you comment on how those of us outside the beltway should understand TPP and TPA and the sequence? Because we read -- I think today's *Financial Times* quotes -- seems to quote USTR as saying, let's negotiate it and then submit it.

And coming from Canada, we don't see that as a very promising option,

speaking for myself, and I think the Japanese don't, either.

MR. SCHOTT: Okay. Historically, there has been a tension between the Congress and the executive with regard to the negotiation of trade agreements. Congress has the constitutional responsibility, but the executive branch actually executes the negotiation. And what we have now is a process where we've had negotiations underway for almost five years. They're nearing completion.

Essentially, the ministers are meeting privately on a number of occasions whenever they get together to try to resolve the remaining open issues, which have narrowed substantially over the last six months. And meanwhile, the Congress is now beginning a process of reauthorizing Trade Promotion Authority which expired in the end of June, 2007.

There is a substantial draft of a bill that was pulled together last year, and one of the coauthors of that bill is now the chairman of the Senate Finance Committee, so it will move fairly quickly forward. The members of Congress used this bill to provide guidance in terms of the objectives of negotiations, and the priorities and some of the redlines to put in for the U.S. in the negotiations.

So, it's odd to do that legislation at the end of a negotiation. I think what Congress will insist on in terms of congressional prerogative and its constitutional authority is that the Trade Promotion Authority legislation will be advanced before the TPP is signed.

Now, what that means is that the TPP and TPA will proceed in an incremental fashion. You will move forward to almost the finish line of the TPP negotiations. That will provide the content for why members of Congress should and will vote for Trade Promotion Authority.

That vote will then allow, after a 90 day notification period for Congress



to review the draft, for the U.S. executive to sign the bill. And that, then, can begin the process of developing implementing legislation. So, it's convoluted, but one where the process could unfold relatively quickly in the second quarter of this year, and lead to a congressional vote before the end of this year.

MS. DOBSON: So, that's the positive.

MR. SCHOTT: That's the optimistic scenario.

MS. DOBSON: Inside the beltway.

MR. SCHOTT: Yeah.

MS. DOBSON: Interpretation.

MR. SCHOTT: Yeah.

MS. DOBSON: All right. Thank you. That's very helpful. So, yes, a question at the back. Blue shirt? Identify yourself.

MR. WOO: (Laughter) It's a test. Hi, David Wu,, former member of Congress, and I have a question primarily aimed at Dr. Schott, but interested in other comments.

And that is, I'm a former international trade and technology lawyer, and I was acutely aware that I was a beneficiary of international trade.

But in Oregon, a high school graduate who has been working in industry for a long time, was unlikely to benefit, and at age 50, unlikely to be retrained as a computer programmer. And I'd be interested in your comments, partially as an economist, but partially as a citizen, about what we do about issues like that.

And secondly, you also recognize that trade agreements are frequently investment agreements underneath the surface. And I'm curious about why don't we characterize them as investment agreements, and then have an honest public discussion about whether we want that or not.

MR. SCHOTT: Those are wonderful questions, and I can't do justice to answering them completely. The first thing to say, though, is that trade agreements create opportunities, they don't guarantee sales.

And so, we need to pursue, in conjunction with trade agreements, domestic economic policies that improve the efficiency and productivity of American agriculture and manufacturing, and we don't do a very good job of that.

It also means that there will be more competition in our marketplace, though our borders are pretty open. And so, whether we have a trade agreement or not, we're getting a lot of competition in that marketplace. We're not doing enough in terms of complementary economic policies to deal with that.

One of the simplest problems to look at is the inadequacies in our investment and infrastructure, which imposes a tax on a wide range of enterprise in the United States. We're taxing our own ability to -- our own firms, and inhibiting their ability to compete because of that.

The adjustment assistance question is a much more difficult one, because you're right. There are some areas where workers will have a hard time finding alternative employment.

At some ages, you can do training or education. We're not good at programs of that, but we've had trade adjustment assistance for over 50 years. The program is well meaning, but not well designed.

The problem for older workers is even more difficult, and I'm of that age that I'm wondering how could I compete with the brilliant young students that I see when I travel overseas. That's a bigger problem, but it's also a general challenge to Congress on how we share the gains from globalization, from trade; how we distribute the benefits across our society, and that's what Congress is supposed to do, and Congress hasn't

done a very good job of doing that with a view towards equity and efficiency and growth in the U.S. economy. And that's been going on for a long time.

MS. DOBSON: Okay. Peter, you'd like to add?

MR. PETRI: Yeah, if I could just add to that. I think we tend to frame this picture of trade in the context of the 2000s, of that decade between 2001 and just the beginning of the financial crisis, and that was a very unusual decade. It was very unusual, first of all, because China became a very powerful exporting country.

It was also very unusual in the United States, because we borrowed a lot and we spent a lot. We built a lot. And manufacturing was a sector that suffered from all of those combinations of things.

If you look at what has been happening in the last five or six years, that's not so obvious anymore. That's not happening. And the effects of that on manufacturing are certainly not as negative. And I would argue that if one looks at the next decade, that participating in a very active, aggressive, competitive international economy will be important for the United States.

So, we shouldn't look at it from the perspective of that pretty bad decade when imports, among other things, were the kind of dominant feature of that era.

MS. DOBSON: Good point.

MR. SCHOTT: Very good.

MS. DOBSON: Next question. Yes? Yes, third back from the front?

(No response heard)

MS. DOBSON: Who else has their hands up? And then, you with the glasses over there.

SPEAKER: Hi, Chung Wey from China Daily.

I want to ask -- the professor, Joseph Stiglitz wrote in the recent Atlantic

Monthly, basically describing TPP as a U.S. attempt to cut China out of the Asia supply chain. I want panelists to take on that.

I mean, obviously, the Chinese has changed the somewhat official attitude. I mean, some still believe there is a conspiracy on the U.S. side. I mean, I can't find evidence. I mean, a lot of criticism, both in China and inside, in the U.S. about the U.S.' sort of lack of enthusiasm, or maybe even opposition to sort of the China proposed Asia infrastructure investment bank. You know?

And the second, related, I want to describe how difficult it would be for China to join TPP, I mean, versus what Zhu Rongji led China into the WTO. I mean, I would think, I mean, things in Vietnam, which is behind China in this sort of flying geese pattern is going to qualify, so how China is not going to qualify.

Thank you.

MR. PETRI: Jeff, this is yours (Laughter).

MS. DOBSON: Well, you want to take it?

MR. LU: Okay. I think whether there's a conspiracy motivation, some American colleagues can answer much better than me. You know? (Laughter)

So, there's a lot of discussion in China's media and academic circles, you know, about the possibility of whether -- how can we approach or access the TPP initiatives in recent years. In my observation, I think there's two elements.

On the one hand, I try to assume, you know, and the U.S. as the leader and the rule setter in this work, they want to -- how can I say, to make efforts to create a new generation of the new rules for the bilateral or regional, even global, you know, trading regime, or new institutional settings. I think that that is one element there.

But on the other hand, I think as a part of the -- major part of the rebalancing strategy, it also covers elements to you know, deal with China and to

manage -- Sino-U.S. relationships. I think that may be also there.

I read the report entitled "Big Bets and the Black Swans," okay, produced in this institution, which also mentioned this issue -- you know, the TPP as a major policy instrument as a rebalancing strategy in the new environment. But the problem is how China takes their own position towards this kind of initiative.

I think even you know, given there's two elements in there, then I think China should take a more positive approach in terms of this negotiation, because we discussed extensively, there's several issues -- for example, environmental protection. Maybe the standard is higher that China should take, given the developmental stage at the moment, which emphasizes the adjustment.

But if we can try to stretch, we can touch it and we can manage. On the other hand, because domestically, we feel -- we also feel the pressures of the environmental -- the pollution as major domestic policy issues. So, a lot of issues, a lot of the policy objectives, we cannot do 10 years ago, 5 years ago. Maybe we can do now or in the near future, especially the climate change issue. You know?

In the past, there's also controversy or speculation about the transparencies. But recently, I think there's bigger progress in the APEC summit. We two countries made that deal in this area. Also, in the SOE reform.

Actually, we want to push forward the SOE reform, per se in the first place. I think we cannot negotiate on that (sic). Okay? Also, these kind of competition usability issues -- I think all of these areas, if we can talk to each other, then, we can find some way on the balance which can mutually satisfy both sides, including agricultural area.

Actually, there's a lot of difficulties in dealing with these issues with Japan, with Korea. China, of course, also difficulty. But I think maybe there's more

potential, in my personal judgment, for China to make a deal in this area. Actually, that Zhu Rongji achieved in his visit in 1999 to this country, which did a great job. You know, supported tremendously of China's eventual secession of the WTO deal.

MS. DOBSON: Jeff, with your permission, I'm going to go to the next --

MR. SCHOTT: Okay.

MS. DOBSON: So?

MR. SCHOTT: You're the boss.

MS. DOBSON: Okay. Yes, ma'am.

SPEAKER: Hi. I'm Nancy (Inaudible) from the Carnegie Endowment for International Peace. I have a question about the bilateral investment treaty.

Do you guys see the possibility of an upcoming conclusion? What are the challenges you think that China and the U.S. face? You mentioned Chinese investment in the U.S. How about the negative --

SPEAKER: Sure.

SPEAKER: -- like what are the other challenges you foresee? And given the political pressure to conclude the process, do you think it might fall short in terms of the like standards in the investment treaty? Thank you.

MR. SCHOTT: Well, the BIT negotiations accelerated about two years ago, a year and a half ago, when China made a dramatic advance in its position to negotiate off of a negative list; basically, to say that the rules would apply to activities, except those specifically listed in the agreement.

That argues that China is now trying to have a more comprehensive agreement that would fit more into the template that the United States has been insisting on. And that really led to a rapid progress in the negotiations. Now, the hard work is under way.

How do you sort through what will be accepted, exempted from the rules? Because if you don't list them, they're going to be covered. And that leads to many sensitive issues with regard to state owned enterprises, with regard to types of investments, with regard to the process of investment, including whether you include pre-establishment rights in the agreement, which is crucial for the United States, and which China has only recently begun to include in its investment agreements.

So, I think there is an interest in moving -- continuing to the progress and moving quickly in the negotiations this year. I think these issues are difficult ones, and I doubt there will be a substantial watering down of the agreement as a bilateral investment treaty, because that would complicate the ratification process in the United States. So, why conclude an agreement that will sit in the U.S. Senate for 10 years and not enter into force? So, neither side wants to have that type of result.

MS. DOBSON: Okay? Yes, Peter.

MR. PETRI: To add quickly to that.

Bilateral investment is very interesting, and in fact, David Dollar has done some very interesting work on this. It's slow.

It's far less than what one would expect between two countries the size of China and the United States. So, this would be my guess. One of the very early, very positive effects of reaching an agreement.

MS. DOBSON: So, yes, sir? And then one at the back, and one here, and I think that will probably finish the session.

MR. SCHOTT: Maybe we can group some.

MS. DOBSON: Yeah. So, I'm going to take all three questions together, and we'll remember them. Right (Laughter)? Yes?

MR. BRODSKY: I'm Mark Brodsky, retired CEO and physicist.

I have a global question. We heard a lot today about how international pressure or excuses enabled domestic change within China; a very significant change in reform. I have the reverse question.

As China makes huge domestic reforms, how will that affect the international stage and the other countries?

MS. DOBSON: Good question. Next one? So, this gentleman on the aisle with the blue shirt, is it? And then, a young man just before the camera at the back.

MR. MORRISON: I'm Wayne Morrison --

MS. DOBSON: Yes, sir?

MR. MORRISON: -- with the Congressional Research Service. And so, my question is on contradiction.

If you look at some of the surveys that the various U.S. business groups have been putting out the last couple of years, you see sort of the growing negativism about the investment climate in China. In fact, I think U.S. investment trends down a lot this year.

And at the same time, you have China talking about a high standard bilateral investment agreement based on a negative list. So, it's kind of unclear to me. Why is the investment climate in China getting worse, while at the same time, they're negotiating this high standard agreement? I'm not quite sure why there's such a contradiction in terms of the policy they're implementing now versus what they're negotiating for.

MS. DOBSON: Thank you. And then, the gentleman in the bank.

SPEAKER: Thank you very much. My name is Shing Isolvay with CSIS.

My question is about how will the U.S. political cycle affect the bilateral economic relationship? Because usually, when the U.S. presidential election gets closer,



the U.S. takes a hard line against China.

So, some experts are expecting that the BIT negotiation will not be concluded until 2017, and Congress gets much tougher against the Chinese FDI to the United States. So, can they manage these political difficulties and move forward in many negotiations, practically?

Thank you very much.

MS. DOBSON: So, I'm going to move to all three of you. Lu, are you ready?

MR. LU: Okay.

MS. DOBSON: Professor Lu?

MR. LU: So, the first question is, if China reforms successfully, what's the impact on global economy?

I think obviously, that will be positive. I think if China's economic reform goes smoothly and successfully, then productivity of China's and catch up will continue. Then, China will be able to organize and provide more and more goods for the rest of the world at a relatively cheap price.

But on the other hand, I think can import a lot of the goods from the rest of the world. That way, we'll boost the economy you know, in the world.

On the other hand, I think as China becomes a more mature match on the economy, I think China can play an even bigger role and a positive role in a lot of other areas that you can see. Of course, maybe there are different opinions, but in my regard, in my observation, I think recent efforts by China to set up this kind of Asian independent infrastructure developmental banks, as well as other initiatives, they can't help a lot.

You know? And for other countries' development, including ASEAN or other

Asian countries, including even African countries, because Yala can't do a lot of the infrastructure built in there. And that is the issue, just in past dialogue in recent years.

So, generally speaking, then, China can play a more -- have the more -- a bigger confidence to play a bigger role in the international, you know, framework setting, and a lot of creatively participate in the rural setting in the world, I think. I left the other two questions.

MS. DOBSON: The investment climate is getting worse, was the question. Is there a contradiction between that and the --

(Simultaneous discussion)

MR. LU: Yes. I think that is a very -- how can I say -- a shocking question. I appreciate that there's a lot of discussion as well as controversy about industrial policies in China. So, a lot of -- some people and the interpreted this -- how can I say, backward and the process, in terms of investment -- the environment nature.

I want to say, you know, maybe there's individual cases, but I would hesitate, even after hard reservations about the judgment of the oval room. How can I say? Returning you know, back of the international investment -- the environment in China.

Generally speaking, I think as the Chinese government implemented further opening of policy, pilot projects in Shanghai experimented zones, as well as especially, domestic reforms, including the anti-corruption campaign.

So, I would like to say even though there are still some unsatisfactory cases, the overall environment maybe at the margin where it has been proved and will be improved in the future. So, also, on the other hand, I think that the Chinese negotiations with the U.S. in terms of the bilateral investment treaty, if they make progress as expected, for example, if in February if China can deliver quality sharply -- an active list

and then put the momentum going up, I think that will tremendously improve -- further improve the environmental investment environment.

So, I think maybe there is -- that is the issue subject to further observation and discussion.

MS. DOBSON: Thank you so much. Jeff, you have about a minute.

MR. SCHOTT: Well, on the U.S. political cycle, as you know, Wendy, politicians like to say nasty things about our trading partners. So, lots of nasty things about Canada and Mexico have been said over the years. Japan, and now China.

But the U.S. electorate, the people who vote don't care very much about international events. And they vote basically on domestic issues and domestic concerns. And so, we even saw, when Obama was fighting for the Democratic nomination in 2008 against Hillary Clinton, there were very nasty comments about NAFTA.

But by the time you got closer to the election, people weren't talking about NAFTA or anything in the -- in international trade. They were talking about --

MS. DOBSON: But we didn't forget.

(Laughter)

MR. SCHOTT: So, I think you'll hear more nasty things close to the election, but in terms of affecting the bilateral economic relationship, I think it's being conducted by adults (Laughter), and it will move forward.

MS. DOBSON: Peter? You get the last word.

MR. PETRI: Well, very quickly. This is a huge relationship. This is the world's biggest trading relationship. These are the world's two largest economies.

It's going to be competitive, as well as complementary. So, I think some of these questions about, for example, TPP as kind of laying down the markers for rules that the United States would like to see in the world, yes. I mean, I don't think one needs

a conspiracy theory to understand that. In fact, the U.S. is trying to help define those rules for the future through the actions it takes.\

But these around also the two economies that I think, in the long run, have the most to gain from a system in which rules are fairly predictable, and in which open trade is an investment -- is permitted and is fair -- you know, reasonably fair across the world. So, we have to be pragmatic. We have to take the competition at its face value, and ultimately, try to bring these rules about that help us both do well in the long run.

MS. DOBSON: Very good advice on which to end.

So, on your behalf, I would like to thank Professor Lu, Jeff Schott.

And Jeff Schott, by the way, for leaping into the breach at very short notice. And Peter Petri. This was a very revealing, if rather technical at times, discussion. And on your behalf, I'd like to thank you all.

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