

THE BROOKINGS INSTITUTION

U.S.-CHINA COOPERATION ON GLOBAL ISSUES

Washington, D.C.

Monday, May 10, 2010

PARTICIPANTS:

Introduction and Moderators:

KENNETH LIEBERTHAL
Senior Fellow and Director
John L. Thornton China Center
The Brookings Institution

RICHARD BUSH
Senior Fellow and Director
Center for Northeast Asian Policy Studies
The Brookings Institution

Session 1: The Climate Change Issue in U.S.-China Relations

WILLIAM J. ANTHOLIS
Senior Fellow and Managing Director
The Brookings Institution

TREVOR HOUSER
Visiting Fellow
Peterson Institute for International Economics
Partner
The Rhodium Group

Keynote Address:

JAMES B. STEINBERG
Deputy Secretary of State
U.S. Department of State

Session 2: Dealing With States Going Nuclear: North Korea and Iran

CHARLES "JACK" PRITCHARD
President
Korea Economic Institute

KENNETH POLLACK
Senior Fellow and Director
Saban Center for Middle East Policy
The Brookings Institution

JONATHAN POLLACK
Professor of Asian & Pacific Studies
Chairman of the Strategic Research Department
U.S. Naval War College

JOHN GARVER
Sam Nunn School of International Affairs
The Georgia Institute of Technology

Session 3: Global Economic Issues in U.S.-China Relations

ANNE KRUEGER
Professor of International Economics
Johns Hopkins School of Advanced International
Studies

BARRY P. BOSWORTH
Senior Fellow
Economic Studies
Global Economy and Development
The Brookings Institution

* * * * *

P R O C E E D I N G S

MR. BUSH: Good morning. Why don't we go ahead and get started.

My name is Richard Bush. I'm the director of the Center for Northeast Asian Policy Studies here at Brookings. My co-convenor today is Dr. Kenneth Lieberthal, the director of our John L. Thornton China Center. And it's our joint privilege to welcome you here today.

The subject is U.S.-China cooperation on big issues. Washington and Beijing will soon convene the second strategic and economic dialogue. The first was last summer, and at that first dialogue President Obama gave a speech that captured his vision of our bilateral relationship.

Among other things, he said:

The relationship between the United States and China will shape the 21st century, which makes it as important as any bilateral relationship in the world. That really must underpin our partnership. That is a responsibility that together we bear. . . . I believe that we are poised to make steady progress on some of the most important issues of our times.

My confidence is rooted in the fact that the United States and China share mutual interest. If we advance these interests through cooperation, our people will benefit and the world will be better off -- because our ability to partner with each other is a prerequisite for progress on many of the most pressing global

challenges.

Ken Lieberthal and I happen to agree with the President, that challenges like the global economy, nonproliferation, and climate change have moved to the center of the U.S.-China relationship. And you can see that point in the joint statement that the two presidents released last November.

Ken and I also believe that cooperation between the United States and China and other major powers is the only way to address those challenges. Cooperation is also the optimal mode of interaction among major powers in an increasingly multi-polar order.

But President Obama's vision does raise some questions. Number one, do the United States and China each understand the challenges like climate change, the global economy, and nonproliferation in the same way? After all, each of these issues has its inherent logic, which our two countries may or may not accept.

Question 2: Do we indeed share mutual interests on these problems? To put it differently, what's the actual degree of overlap between how the United States sees its stakes and how China does?

Question 3: Even if the answer to those questions conforms to President Obama's views, how effective has our cooperation really been? Does cooperation truly address the challenge at its core, or is it just

superficial? Does the gap, if any, between our respective interests actually significantly limit what we can achieve together? What is the likelihood that the current mode of cooperation will effectively address or at least contain each of these challenges?

That is the purpose of today's session, to assess the extent and quality of U.S.-China cooperation concerning climate change, Iran and North Korea, and the global economy. For each of these issues, we'll have one presenter who will address the challenge per se -- what I call the logic of the problem -- and then a second presenter will, considering that context, discuss U.S.-China cooperation specifically.

We will start this morning with climate change. After a break for lunch we will hear Deputy Secretary of State Jim Steinberg, who will offer the Obama Administration's perspective. And then after that we will do nonproliferation and the global economy.

So, thank you again for coming. I now yield the floor to my colleague Ken Lieberthal, who will chair the first session.

MR. LIEBERTHAL: Thank you very much, Richard. It's a genuine pleasure to welcome you here for this conference, and I want to express my appreciation in advance to our speakers, a number of whom have come from out of town to participate in this event today.

Our first panel is on the major issue of global climate change.

This is clearly an issue where the United States and China are the two biggest players on the issue, in a sense unfortunately, since each of us now accounts for more than 20 percent of global greenhouse gas emissions every year.

And it's an issue whose kind of focus is changing. The U.S., historically, has clearly been the largest single contributor -- it's a peculiar term to use, but anyway -- the largest single responsible country for, in terms of greenhouse gas emissions. And since these gases remain in the atmosphere for a long time, that history matters. But as we look to the future, the U.S. has now basically peaked in its greenhouse gas emissions, and the issue is, how much will we reduce those emissions and over what schedule?

China, unfortunately, is nowhere near its peak. It is on a very steep upward curve. So while the focus has been on the U.S. historically, increasingly it's going to shift to China as accounting for a very large percentage of the increase in greenhouse gas emissions as we move forward.

The whole world, moreover, is looking at the U.S.-China relationship to be a major factor in global responses to climate change, both in terms of mitigation and in terms of adaptation.

Fourth and final facet of this, I just want to mention before

turning to our speakers, is that as you think about the U.S.-China relationship itself, both sides, I believe, now see the climate change issue as possibly an area in which we will develop new levels of mutual cooperation. And in the process, perhaps increase mutual strategic trust. But it's also an area that's so early on and still so much needs to be done that it's possible it will end up being the opposite, which is to say an area of an inability to really get our priorities lined up reasonably well together and, therefore, an area that may produce an increase in the strategic distrust and, therefore, increasing obstacles to dealing with this issue overall.

So, that's why we're leading with this issue. The issue itself is of enormous global importance. The U.S. and China are enormously important players. But we are early on in engaging this issue, both bilaterally and as the key players in the multilateral arena.

We have two terrific panelists to introduce this topic and discuss it with you. You have their bios, so I'm not going to simply read what you have in front of you. Let me just note that Bill Antholis is managing director of the Brookings Institution. Hello, boss. He has long had a keen interest in the climate change issue, and in fact he and Strobe Talbott, the president of Brookings, this week on Friday are publishing a book called *Fast Forward*, which is on the climate change issue in its global context. So, if this panel whets your appetite, on Friday you can really enjoy the full

banquet.

Trevor Houser is both a partner at the Rhodium Group and a visiting fellow at the Peterson Institute of International Economics, right across the street. He's done enormously useful and insightful work on China's relevant policies and on U.S.-China interaction on the climate change issue. And he just left, what I recall was a six-month stint -- is that correct? -- working with Todd Stern, our special envoy on climate change; working the negotiations leading up to and through Copenhagen. So, he brings a tremendous practical experience and very fresh experience to the discussion this morning.

We're going to have both presentations and then open it up for Q&A. Each presentation will be roughly 20 minutes long and we'll begin with Trevor, and then with Bill. So, welcome.

MR. HOUSER: Thanks very much, Ken. Thanks to Richard and Ken and to Brookings to ask me to join this panel.

For those of us who toil in the fields of China's energy and environmental markets and policy, we all stand on Ken's shoulders. About three years ago, when I provided my kind of humble initial offering into this issue space, I had the honor of Ken come and serve as a respondent, which was both one of the most terrifying and rewarding experiences of my career. So, it's a pleasure to be here today.

Ken asked me to join a similar event last fall, which I was ultimately unable to do because, as Ken said, I was doing a stint in the State Department. So I'm grateful that I was able to respond positively to this request now that my schedule is a little bit more my own. So, of course, everything that I say is my opinion, which I am now free to offer since I'm not in the cone of silence of government.

And I think what -- Bill and I talked a little bit about this before -- and I think what I'll do is, I'll lay out some of the context of where we stand in the climate change negotiations -- U.S. and China's role -- and map out some issues going forward, both to help kind of lay the table for the conversation, but also because I've been, you know, this close to the issue with no room for actual creative thought or strategic thinking. So I will leave that all to Bill. And since I left government at the end of the year to have a newborn child, I am slow in getting back up to that level of strategic thinking.

The current round of climate negotiations were launched about two and a half years ago in Bali, Indonesia. And the U.S. and China were in many ways at the center of why the international community felt it necessary to kick off a new round of negotiations. The existing international architecture for addressing climate change in the form of the Kyoto Protocol had two absences. The first was the United States, the largest emitter in the developed world -- which, over time, it's become increasingly politically

untenable for other developed countries who are in the Kyoto Protocol, like Europe, Australia, Japan, and Russia, to continue to be in the Kyoto Protocol if the U.S. is not.

And the Kyoto Protocol only had emission reduction commitments for developed countries, not for developing countries. And in the decade between when the Kyoto Protocol was signed and the Bali conference in Indonesia, rapid economic growth and emerging economies made it clear that any long-term solution to this problem could not be a developed country solution alone.

So, in Indonesia the international community, buoyed by a rise in both scientific convictions surrounding climate change and awareness of the challenge -- a week before the Bali conference started, as you remember, Al Gore and the Intergovernmental Panel on Climate Change split a Nobel Peace Prize -- kicked off the current round of negotiations, which were supposed to conclude in Copenhagen.

And in the two years between Bali and Copenhagen, the international community saw encouraging movement both in the policy and the politics in developed and developing countries alike. Right before Bali the government in Australia switched hands. The Labor Party won, and that brought about more ambitious Australian climate change action and policy. And that, of course, was followed by a change in government here in the

U.S. And the Obama Administration both raised the profile of climate policy in its domestic agenda, and reengaged in the international negotiations. And then, in the fall of last year, the government changed hands in Japan from the LDP to the DPJ, and that brought about much more ambitious Japanese climate change targets.

And the developed countries weren't alone. We saw in September of last year, for the first time China announce economy-wide climate change-oriented targets. Hu Jintao speaking at the UN General Assembly in September, announced that China would do three things by 2020: China would increase the amount of primary energy coming from non-fossil sources to 15 percent; would increase forest coverage by 1.3 billion acres, and would -- or million acres, billion acres, not sure which is the right unit for forest acreage; and would reduce the carbon intensity of the Chinese economy by a significant amount by 2020. In late November, they announced what that amount would be, and it was 40 to 45 percent improvement. That's the first time that China has ever made an economy-wide emission reduction target. That carbon intensity target came a few days after the Obama Administration announced a goal of a 17 percent reduction by 2020, followed by continuous reductions thereafter to ultimately an 83 percent reduction in emissions by 2050.

After China made their announcement, India announced an

economy-wide target. And by the time the Copenhagen conference started in December, we had economy-wide emission reduction policies or targets from all major economies. That was pretty significant.

Also over the past two years, bilateral, multilateral cooperation on this topic expanded. The Obama Administration reinvigorated a process started under the Bush Administration called the Major Economies Forum, and that group of leaders in July of last year produced a communiqué that foresaw to a degree a pathway with both developed and developing countries pulling their weight.

In bilateral relations, last summer we and our counterparts in Beijing negotiated a U.S.-China memorandum of understanding on clean energy and climate change cooperation that mapped out a pathway, a set of principles, for what the two countries could do together. And, you know, as Ken said in his introduction, this is an area that can either be a pillar in the bilateral relationship -- it is one of the earliest areas of bilateral U.S.-China cooperation. Pretty much the first thing that Deng Xiaoping and Jimmy Carter did after normalizing relations was sign an S&T agreement in 1979 that has served as the foundation for, you know, 30 plus years of clean energy cooperation. Or it can be a point of kind of strategic mistrust and tension.

The goal with the MOU that was announced last July was to

kind of map out a set of principles going forward. And then in November during the President's trip to Beijing, there was a suite of clean energy and climate change initiatives announced for everything from renewable energy to shale gas energy efficiency, to start implementing that memorandum of understanding. And a similar set of initiatives between the U.S. and India.

So, we have all this kind of positive momentum and bilateral, multilateral relations in domestic policy. None of that was translating into the international negotiations actually tasked with coming up with an international climate agreement, which for two years were completely mired in debates over both content and form.

There are a lot of views as to why the international negotiations have struggled. I think at the core, the most important issue in the difficulty of translating that political will into an actual treaty has to do with the legacy of climate institutions and agreements that we're left with and uncertainty about the future.

You have three positions in the negotiations that are difficult to reconcile. You have the developed countries that are part of the Kyoto Protocol who can't continue to be in that framework without the United States. They need symmetry with us. You have the United States, who under the Obama Administration is willing to not sign the Kyoto Protocol but be part of a new international agreement -- a binding international

agreement -- and is willing to allow for differentiation between what developed countries do and developing countries do. But insists that if we're to sign the new treaty that all countries need to stand behind their actions. So, all countries need to be bound legally. They can commit to do different things, but there's no justification for some countries to be legally bound and other countries to be taking voluntary action.

And for emerging economies like China and India, the Kyoto Protocol works pretty well. And while those countries have put forward significant domestic policy, they're reluctant to translate that into international binding commitments. And, you know, my view of why in the case of China, one of the primary reasons is that while China is fairly confident that they will be able to meet the targets that they've laid out for 2020, they're uncertain of what the pathway looks like after that. And if China were to agree to a legally binding treaty in which they were taking legally binding commitments and that treaty had some global goals, like long term reductions in line with two degrees, that that might imply a future Chinese commitment that's greater than leadership currently thinks they can deliver.

Because keep in mind, there is a significant difference between energy and climate policy and other areas of international law like trade or finance. When trade negotiators come up with an agreement to reduce tariffs, it's pretty straightforward how that actually gets implemented,

provided you can get your legislature to vote for it. You pick up the phone, you call customs, and you drop the tariff.

If you commit to a climate change target, to an emission reduction target, you have very little certainly about your ability to actually achieve it. It requires a broad array of policy tools -- everything from mandates to pricing -- that we don't have much experience with how effective that is in actually meeting those objectives. All you have to do is look at the U.S. experience with our wind and solar incentives in recent years to get a good example of that. So, people are risk-averse, they're cautious.

Now, thanks to some significant engagement directly by heads of state in Copenhagen, we were able to sidestep these ultimate questions of legal form of who's bound and who's not when we're dealing with climate change, and produce a political accord with broad agreement on the key areas of substance and a kind of pathway for action going forward.

More importantly, I think the Copenhagen accord signified a fundamental shift in our approach to this problem internationally from the top down approach that was embodied in the Kyoto Protocol, where we all get together and we allocate the pain and we negotiate our domestic policy with each other and see who needs to do what, to a bottom-up approach where countries come with their own policies negotiated domestically, and offer

those up and compare and take stock of how each other are doing going forward.

That bottom-up approach also means we'll likely see movement going forward in multiple forums. There will be movement in the UN framework convention this year, hopefully -- a series of decisions that can help move forward progress on finance, on transparency, on adaptation, on technology. It will be challenging to make that progress because there's still uncertainty about what happens to the Kyoto Protocol, which contrary to popular belief doesn't actually expire in 2012. It continues, and the developed countries who are party to that are expected to take on another commitment period. So, that's a particularly tricky issue.

But we'll also likely see more work on climate change at other forums -- the major economies forum, potentially the G-20 -- and work on some of the issues that help address climate change, though not directly, like the deployment of clean energy, through forums like the new clean energy ministerial that Secretary Chu announced and will meet for the first time this summer here in Washington.

I think the other significant change following Copenhagen, in addition to going from top down to bottom up, is we're going from a climate-oriented focus to a multi-issue focus. In a lot of countries that matter, political support for policies to reduce emissions for the sake of addressing

climate change, has taken a bit of a hit in the past six months, not least here in the U.S. Fortunately, the means to the end of addressing climate change, the deployment of clean energy technology, addresses a number of other ends as well. Whether it's local environmental protection, energy security, economic growth, or employment creation, those narratives continue to be important and powerful politically in a number of large emitting countries and drive policy. And I expect that we will see that be more and more important in driving policy in the years ahead.

Now, there's a good news story to that, which is that if we move from a narrative of how do we allocate the pain to how do we all take advantage of the gain, some of the international negotiations get a little bit easier. Instead of, in D.C., thinking we need to wait until China moves for us to move, if you're telling an economic employment story, then, theoretically, there's some advantage in being the first mover in this space.

But it comes with a lot of other policy challenges, which I think are going to increase in their profile in U.S.-China relations in the years ahead. The deployment of clean energy in all countries right now requires subsidies, either directly from the government or indirectly in the form of higher energy prices. And so there's strong political support in all countries for ensuring that the economic activity created by those subsidies accrues to firms and workers in the country that's actually paying the subsidies. So in

the U.S. stimulus package, we saw Buy America provisions. There are local content requirements in China. This is a trend that if it continues to escalate, creates significant challenges globally.

If we all make everything soup to nuts in the clean energy system in our own country, energy prices will be higher, deployment will be lower, and our ability to tackle this problem will be less. But if we're going to trust that if I buy things that China does better than the U.S. does, that I also need to trust that China's going to buy things that the U.S. does better than China does. And that requires being smart here in the U.S. about where we have comparative advantage, investing in that, and prioritizing our foreign trade and investment policies accordingly.

I read on the flight down from New York this morning, there was a quote from Grant Aldonas in a newspaper article saying that you need -- when you go to the negotiating table with China, you need to know what you want. And that presupposes a strategic view about the U.S.'s role in the global economy. I think we're still searching for that strategic view. And in the clean energy space we need it critically, as that becomes the kind of narrative driving things forward.

I'll just make a couple more comments and then I'll wrap up. This driving policy through the co-benefits, as I call it -- whether that's trying to address energy security, trying to address employment creation, local

environmental protection -- in a way that also reduces emissions at the same time and helps us tackle climate change, I think will deliver meaningful results over the next 5 to 10 years. But it's not a long term solution.

Ultimately, to meet the types of goals that the scientific community has laid out globally will require things that actually cost money and are hard to do. And our freedom of air -- we have a little bit of room right now, for the next decade, to experiment with what policy works, what works best. We don't have to have a top down approach where every country is allocated a certain right to emit. We have a flexibility for the next decade.

As we go forward, that flexibility is reduced. And our margin of error in terms of meeting long term stabilization goals will be lowered. And so we will need, ultimately, a top down, legally binding approach to this challenge. And that will, once again, bring us back to core issues that are difficult, that were left unresolved in Copenhagen. And so we need to begin laying the groundwork for that conversation now.

And I think that means a few things for the U.S. The first is that it means passing U.S. legislation. We will be in a different place in 2020 than we are today. Chinese per capita emissions will be higher than Europe's in 2020. China's economy will be significantly higher. The impacts on vulnerable countries will be much greater than they are today. The

political conversation we had in Copenhagen will have a distinctly different tone in 2020. But if the U.S. can't act -- if we can't pass comprehensive energy and climate legislation -- if we can't demonstrate that we believe what we say and that it's possible to de-carbonize your economy while maintaining prosperity, then it will be very difficult for climate diplomats to put pressure on other countries to do the same because we won't have any credibility.

Second, that legislation needs to deliver financing -- financial support to vulnerable countries. One of the reasons why it's difficult for us to make progress today in the negotiations is because the U.S. in particular, and developed countries more generally, have yet to seriously follow through with the commitments they've made for the past two decades. And so we are, you know, in some ways rightly criticized for moving the goal post as we go along.

We made some important commitments on finance in Copenhagen: thirty billion collective finance from developed countries between 2010 and 2012, and then a commitment to mobilize up to 100 billion in finance, both public and private, annually by 2020. That's from all developed countries. I think it's critical that we come through with that pledge, both to help the countries that desperately need it but also to build the credibility that will be required for other countries to follow suit.

So, that's my introductory comments. And look forward to hearing what Bill has to say. Thanks. (Applause)

MR. ANTHOLIS: Well, thanks, Trevor. And thanks to Ken and Richard for inviting me and putting this on.

As I joked with Ken beforehand, being asked to talk on a panel on U.S.-China climate cooperation by Ken is like bringing coals to Newcastle, although I think there's got to be a clean energy, politically correct way of saying that.

And in this case, it's bringing coals to Charleston, West Virginia, or to China. Because that's really at some level the heart of the story or where it starts in both countries.

Just going back to Ken for one second, I just do want to say that Ken's work on this issue has really been path breaking. In preparing for this I read Lieberthal and Sandalow. David Sandalow, now assistant secretary for energy for international and policy affairs. And then Ken Lieberthal's own congressional testimony last year -- last fall on this area. And it really has sort of laid out a groundwork at an intellectual level. But it's also based on a lot of Ken's own practical experience in building a dialogue for U.S.-China clean energy cooperation.

I start my own assessment of this both looking at material interests and ideological or political interests more broadly, and I'm going to

be a little more down in the weeds of the -- how the countries themselves feel these issues. Trevor, I think, did a terrific job of giving the broad negotiation overview, which I'll touch on a bit. Both of which are in Fast Forward, which Ken mentioned, which will be out this Friday -- available on Amazon and on the Brookings website.

You know, in the United States we start with 80 percent of our energy coming from fossil fuels. We have about 20 percent from nuclear and renewables, a little bit from renewables. But somewhere between 75 and 80 percent of all our energy needs coming from fossil fuels. And from that we produce just under 6 billion tons of carbon dioxide a year, or gigatons.

China produces 90 percent of their energy from fossil fuels, and that creates about 6 gigatons. So right there between those 2 countries, you have 12 out of the world's 30 gigatons. And by 2050, in order to keep that temperature growth underneath 2 degrees Celsius, we need to get global gigatons down to 15. So right now, China and the U.S. together produce 12 and we have to get globally to 15 in the next 40 or so years.

That's a huge challenge. It's a huge challenge of technology, it's a huge challenge of finance and of changing both the regulatory nature of our economies, but even how the economies themselves operate. And each country has a different set of material requirements -- material and

economic requirements to get there that end up getting teamed up with a set of political requirements to get there. So it's not surprising that somebody who knows a lot about politics, Richard Gephardt, described this as the most difficult political transaction in the history of mankind. I think that's actually fair to say.

If you think about what it took to get healthcare passed in the United States, which is roughly one-sixth of the U.S. economy, that's about the same size as our energy economy. And we have to do that in 190 countries around the world, starting with 2 of the most politically complicated, the United States and China.

So from a material standpoint, that's how the interests themselves are. They're actually fairly similar but we have completely different economic systems. So, doing it in both places is actually rather different. And through Ken's forum and through a number of different efforts, both systems -- political systems, economic systems -- are starting to understand what it takes in one another's countries to make that transformation.

So, from an ideological, from a political perspective, both countries are adjusting to that challenge internally. And that's, in both places, a real conversation between political policymakers, political leaders, and the public. In the United States, the challenge that we face as our -- as

my colleagues in governance studies here in the United States have recently described, we essentially have parliamentary parties. That is, our parties have become more polarized and more hardened around ideological positions. But we don't have a parliamentary system that gives one party or the other a mandate to do whatever it wants. We have this bicameral system that is -- or divided government system between three branches of government and then bicameral in the Congress. Which as we saw in healthcare, makes things so difficult. On the energy side, it's done the same.

What you've seen in public awareness on climate is a growing acceptance of climate change in the center part of the country, which is where the bedrock of public opinion is. The political extremes in the United States -- the left has, for several decades, believed climate change to be real. The right, for several decades, has been quite suspicious. But among the center you've seen a growing awareness and acceptance that climate change is a real problem.

In the last year or so, there's been a small setback in that regard, I think for a number of different reasons the issue has become politicized. Again, the science has become politicized. But still, among moderate centrists, independent voters in the United States, there is still a pervasive belief that climate change is real. They don't know how much of

it's manmade, they don't know how much public policy can address it. But still, if you benchmark it against 15 or 20 years, an advance in the belief.

But that hasn't impacted the political debate that much. Last year, almost a year ago, when the U.S. House of Representatives passed comprehensive climate and energy legislation, it was done on a pure party line vote with -- actually, one could look at it as a high water mark of bipartisanship in that seven or eight Republican members of Congress voted in favor of the bill, which was extraordinarily high. The reason that seven of those eight voted in favor of it was that Barack Obama four months before had won their congressional districts and they had happened to win. And then each of them had specific reasons for voting for it. So, two were from the New Jersey shore, where environmental issues always poll quite high. One was from a swing district in Illinois. That member of Congress, Representative Kirk, has now -- he was for the climate legislation before. He's against it now that he's running to replace Barack Obama in the Senate, he's decided to oppose the legislation. Another member from upstate New York is now -- though, was a Republican -- is now Barack Obama's Secretary of the Army. He was already from a moderate district, was already somewhat left-leaning among Republicans.

So you see on this issue almost all Republicans voting against, with a few coming over. And almost all Democrats -- except for in

heavy coal states, a number of Democrats opposing. That's what we see as the tee-up to the debate that's going to start happening later this week when Senators Lieberman and Kerry introduce comprehensive energy and climate. There are, again, about seven or eight senators on the Republican side who are thought to be considering voting in favor of this, for a number of odd circumstances. But I think what you will continue to see on the Republican side is what we saw in the state of Utah. The hard right in the Republican party is forcing members in their primaries to vote in favor -- or vote against -- these kinds of legislation.

And the same may happen on the Democratic side. Right now, a number of Democrats oppose climate legislation. They come from more conservative states or states more heavily dependent on coal and fossil fuels. We'll see whether or not Blanche Lincoln in a Democratic primary is forced to be more in favor of climate legislation than she might otherwise be. That's the U.S. side.

On the China side, climate change is not a huge area of public opinion concern, such that it exists in China, though it is growing. But what you have is very, very high understanding of the issue among policymakers, though they themselves are divided on the issue. And that division broke most openly in the run up to Copenhagen and actually at Copenhagen itself, when Premier Wen Jiabao when negotiating with Barack Obama actually

had his top negotiator disagreeing with him in a room with President Obama, and Wen then telling the translator to stop translating. It was a fascinating moment where Chinese private debate among policymakers suddenly became public. And again, if you're interested in that exchange, go to Ken Lieberthal on our website, he has a terrific exchange of what happened there.

It was critical as a moment for U.S.-China cooperation on climate change because we saw literally the two heads of state negotiating with one another and, at the same time, turning and having to negotiate with the political forces that they have to deal with. And that is the sort of wrestling match that defines the issue moving forward.

What that means, I think -- in this, there's violent agreement between Trevor and I on what that means for the next set of years. Both the U.S. and China are not particularly wild about binding treaties right now. The reason in the United States is passing a binding treaty means going to the Senate and getting 67 votes. And that's a very difficult thing when it's hard enough to get 60 to break cloture and to pass legislation. But getting the additional seven votes is nearly impossible.

On the Chinese side, again, China can sort of understand what its energy profile looks like until 2030, but beyond that to 2050, it's very difficult to understand and particularly as those emission levels have to come

down to get the world under 15 gigatons. China doesn't want to be constrained in that environment.

So, during this initial period both countries are sort of trying to see what they can do by themselves without having done so in terms of a legally binding agreement that they're negotiating internationally. So, there's actually quite a lot of cooperation between the U.S. and China on something like a Copenhagen accord, which is politically binding but not legally binding. And so, in many ways, the untold story of Copenhagen was how the U.S. and China worked together over the course of a year, starting with Hillary Clinton and Todd Stern's trip right after Barack Obama's inauguration, where they went to China; a number of different bilateral contact points between the two countries, both at the Cabinet level and then ultimately at the leaders level, both on the margins of G-7 and G-20 summits, and then also in their own bilateral in November before Copenhagen; and then actually on the ground in Copenhagen, where these two leaders together really did get together and make the deal happen.

In fact, in Europe what you see right now are newspaper articles in *Der Spiegel* and others talking about how the U.S. and China conspired to break up a legally binding treaty. At some level, that's true. But that may actually be a good thing for the climate, because it allows the whole world system to try to move forward on this.

So, at the national level what you -- and at the international level you see this kind of cooperation. Perhaps the most important cooperation is happening at the corporate level, where you see a number of different engagements of foreign companies trying to go against what Trevor was pointing to that's happening at the governmental level in terms of domestic legislation of subsidies and tax breaks and even -- I'll get to protectionism in a second. But what you see are companies cooperating.

So, last week -- or two weeks ago, I was in Nevada for the launch of a wind turbine plant that's being built by a Chinese company in Nevada to build a wind turbine farm in Texas. That kind of cooperation is happening in China as well, a U.S.-based company, CODA, is building an all-electric vehicle in China using Chinese battery technology to be sold back into the United States¹. First Solar, the largest solar panel producer based in Phoenix, is working to do the same in China as well as in the United States. So, instead of taking coals to Newcastle, someday we'll be taking photovoltaics to Phoenix, I guess, is the new metaphor.

Those kinds of things are critical, but they also face their own set of roadblocks, as Trevor was saying. These subsidies pose problems in the WTO. Perhaps the biggest one that's out on the horizon is, in the

¹ Bill Antholis's comments about CODA Automotive may have left some viewers with the perception that the CODA car is entirely assembled in China and that the battery is entirely Chinese. In fact, CODA plans to have final assembly in the United States. And while CODA has a joint venture in battery development with a Chinese company, nearly all the technology belongs to CODA and is made in the US.

context of getting domestic legislation passed in the United States, it seems likely, actually, that there will be something called border tariff permits, which many people consider to be taxes or tariffs against companies that have not adopted comprehensive climate and energy legislation. So, in order for the United States to pass such legislation, they might say if a country like China doesn't do the same, imports from those countries would be forced to purchase emissions permits at the border in the United States.

Some people consider these to be WTO illegal, some consider them to be legal. For me, the biggest question is when these kinds of things get phased in. If they get phased in in a post-2020 or a 2030 framework, that appears to be enough time for China to establish enough domestic rules and, more importantly than the rules, the ability to implement the rules so that one can say whether or not they've acted on climate change. It also builds in a time for the U.S. to act and to demonstrate that it has acted.

If, however, these things go into law and into operation as soon as American domestic legislation goes into operation, then that poses real challenges, I think. Because it's essentially setting a standard that we ourselves haven't proven that we can live up to, and the Chinese haven't had an opportunity to demonstrate that they have the domestic capacity to move forward on.

Finally, I just want to sketch out a few potential areas for

cooperation that the two countries can continue to work on. And again, some of these I draw from Ken, although some I think we've just seen in the last set of months.

Perhaps the biggest is this issue that came up at Copenhagen that almost derailed the talks, which is the verification and accounting of emissions in developing countries. This is an enormous issue and of enormous complexity.

The Chinese reasons, I think, for opposing this -- although they did end up acknowledging this as part of the Copenhagen accords -- but is, again, the lack of governmental capacity within China to assess and monitor the levels of emissions in others. In other words, there are two ways to monitor emission levels. You can simply look at the fossil fuel inputs that a country takes; how much oil they import, how much coal they import or mine domestically. But the key thing for carbon emissions is not just how much you use, but how effectively and efficiently you use it. And that means going in and looking at the actual technology that you have in place. And the Chinese have cause for concern about that, because it really opens up almost their entire economy to external monitoring and verification.

In addition to that, you're doing it in the context of -- though it's a politically binding agreement -- something that could be legally binding. And there is a great concern, I think, among Chinese, that they would be

opening themselves up and essentially giving away their sovereignty. That is an enormous issue to work on, both diplomatically but also at the technical level. Are there ways to monitor emissions that are not as invasive as the Chinese fear them to be? This is a critical, critical set of questions moving forward.

Two, as I mentioned, the trade issue. I think there needs to be a greater understanding of exactly what this border permit system would look like, both in the United States and in China.

This comes to an issue that Ken and David Sandalow pointed out a while ago, and I think really is a critical area for cooperation. And that's, we've talked about national and international cooperation between China that is at the global level. We've talked about corporate. But there is this important middle ground of state level cooperation. We have to understand that the four big players -- this is something that Strobe and I talk about quite a lot in our book -- the four big players on climate change are big, complicated, federal or confederal systems: the United States, India, China, and the European Union.

Among those 4 players, you have 60 percent of the world's population, about 60 percent of global emissions, you've got almost 70 percent of the nuclear power reactors in the world. This is a really critical -- and a lot of the regulation in the United States on energy and environmental

issues is done at the state level. That's where the experiences are. In the last 10 years, from the failed Kyoto negotiations where the U.S. ended up not ratifying and then walking away from the table, the greatest learning that's happened in the United States on climate change has been at the state level. Where, in the Northeast collection of states -- also California -- in looking at and adopting climate change legislation, they have gone to Europe and learned from what's happening in Germany, what's happening in the UK, what's happening in France, how they regulate on this set of issues. They're about the same size and same complexity as those state governments, and so that kind of learning between the United States and China -- between the United States and India, between India and China -- is really critical, I think, over the next 10 or so years.

It is a big place, as well, if you think about it from the standpoint of a governor where they can learn about international diplomacy and economic diplomacy in a very hands-on way. People forget that when Bill Clinton was governor he did a number of trade missions to China, and he really learned to talk about the global economy. This is where the next set of governors is really going to talk about not just the global economy but the global environment.

And then finally, this issue of nuclear is very critical. China is ramping up its nuclear technology quite quickly. It obviously has an

important nonproliferation side, it has important financing dimensions to it. It is a huge regulatory challenge for China. They have announced that they want to double the number of nuclear regulators in the country.

We have enormous experience for that in the United States. There has been some concern, I think, that we haven't replenished our own next generation of nuclear scientists because domestic nuclear -- civilian nuclear reactors have gone out of style in the last 30 years in the United States. They are coming back on style, people expect as many as 30 permit applications for new nuclear reactors in the United States in the next 10 years.

This is a huge area for cooperation between the United States and China, and one that I would encourage very much.

So, with that, I've probably used my 20 minutes. (Applause)

MR. LIEBERTHAL: Thank you very much. Between the two of you, you've really covered the landscape here.

I want to open this up for Q&A. When people have a question, if you'd raise your hand. When you're identified, we have a couple of roving mics and we'll bring them to you. Please first briefly indicate who you are and then if you want to direct your question to one panelist or the other, feel free to do so.

Before I open it up, I want to ask one question of both

panelists just to get the discussion going. And it is as follows. The next 10 years is going to be extremely important, in terms of both how the world begins to come to grips with climate change, and in terms of the U.S.-China dynamic on this issue. My question is, for respectively the U.S. and China, as we look at the other side on this issue over the coming decade, what are the biggest -- what are the big ticket items that we're really concerned about? Whereas are there a couple of things that we should be really focused on from an American perspective as we worry about China and vice versa? What are the Chinese really worried about concerning America on this issue over a 10-year perspective?

Trevor, do you want to begin? Thank you.

MR. HOUSER: So, I think on the Chinese side first. I can divide Chinese mitigation opportunities, you know, ways to reduce emission into largely two camps. In the near term, I think that the most bang for the buck in China comes from reducing the amount of emissions through lower energy demand. That's both in terms of technical efficiency, but even more importantly through the structure of the economy.

The rapid growth in emissions that we've seen in China in the past decade was not the result of less efficient Chinese production, and it wasn't the result of faster Chinese economic growth in the decade preceding. It was a change in the structure of the Chinese economy that

changed the carbon intensity of China's growth from 0.4 to every 1 of economic growth to 1.2 to every 1 of economic growth.

The good news story there is that a lot of the macroeconomic adjustments that Beijing is trying to engineer in terms of rebalancing away from exports and investment towards service sector and domestic consumption will have a massive carbon dividend, much greater than any technological initiative or pricing policy. So, that, I think, is the most important in the near term.

In the long term, of course it's about changing the sources of energy supply from more carbon-intensive to less carbon intensive. And, you know, there will be significant deployment of renewable energy, of electric vehicles. The core question is what you do with base load power. And there it's a horserace between nuclear power and CCS in China. And there are significant challenges to both that need to be addressed in the next five years if they're actually going to be viable alternatives in 20 years.

On the U.S. side, I think the most important thing that happens over the next 10 years is going to be getting the regulatory framework in place. If we don't -- we have an opportunity right now where our business as usual emissions are lower. The EIA reported that U.S. CO2 emissions are down 9 percent on the year prior. That makes meeting the Obama Administration 17 percent targets a lot easier. We have explosive

development of shale gas on the supply side, but there's not a lot of structural demand for that gas. So we're at this juncture where it's cheap for us to act, and where doing so can kind of solidify these energy supply systems domestically that will make the long-term cost of action much, much less. But all of that is going to require policy.

MR. ANTHOLIS: Yeah, so I'm going to now flip and complement Trevor where Trevor was very focused on the internals of our economies and I'm going to look globally.

I think the U.S.'s biggest worry about China is which part of the Chinese government engages in the international negotiations. Is it the cooperative part that President Obama found in Wen? Or is it the part of the Chinese negotiating team that really saw the Copenhagen process as something that they could use to delay domestic action on the part of China?

And the way -- the place the rubber meets the road on this is what happens with the Copenhagen accord in future UN negotiations? Remember at the end of Copenhagen, the UN failed to -- the UN body, the UNFCCC, the framework convention on climate changes, the big meeting that everybody attended -- failed to endorse the Copenhagen accord. It was noted, but it was not adopted.

What that means for the negotiations moving forward is that every one of the pieces of that short agreement -- it was about a three-page

agreement -- has no standing right now within the UN. So they have to take each of those pieces and run it back through the functional equivalent of a committee system that we have in Congress. And taking one piece apart from the other pieces -- say four or five go through, but three or four get stuck in committee -- that makes the agreement fall apart a bit. And China has, perhaps, the biggest say over what happens in that because they are the pivotal vote with respect to the developing countries, which are the great majority of countries in the UN.

So, the U.S.'s biggest fear is the progress that was made at Copenhagen between their two heads of state ends up getting bogged down in the UN system. In fact, this is what happened after Kyoto. For three years after Kyoto -- remember, it was negotiated, it was still three years left on the Clinton Administration clock -- the U.S. and EU got into a big dogfight about what emissions trading meant. And after three years of negotiation, the negotiations actually broke down while everybody was counting the votes in Florida in December of 2000. There was a UN climate meeting at the Hague in Amsterdam, and the U.S. and EU couldn't agree on the rules of emissions trading and Kyoto essentially fell apart right there.

And at the end of the day, the Europeans end up adopting a year later what the U.S. wanted when the U.S. fell away from the system. And it was just -- we've had a lost decade of international negotiations as a

result of those three years where the U.S. and the EU couldn't agree to the details. We can't let that happen with what happened in Copenhagen. So, the U.S. will look to China to see that it becomes a constructive force in the UN process.

On what China's looking for from the U.S. in the international setting is to not walk away from the UN. The U.S. started this major economies forum, the U.S. tries to bring climate change into the non-formal UN sessions because the UN process can be so cumbersome. And to the extent that it does that, it makes China's relationship with a number of other developing countries much more difficult. Essentially, poorer and more vulnerable countries don't trust China negotiating with the U.S. because they think that the U.S. and China will walk away from their interests.

So, what the U.S. can do is continue to reassure China that it takes the UN process seriously. Again, it will only take the UN process seriously if China is not obstructing that process.

MR. LIEBERTHAL: Thank you. The floor is open. Yes, sir.
Back here.

Again, a reminder, please briefly identify yourself. And if you want to direct your question to one or the other panelist, please feel free to do so.

MR. CHEN: Yeah, Chow Chen, freelance correspondent

(inaudible).

I have a couple of comments. And first is to talk about international issue. China and the U.S. both are big countries, and the climate change is a national security. So, I think this issue either Wen Jiabao or Obama cannot make decision.

Obama have a younger ingenuity. He wave all the Chinese advisors to Wen Jiabao in the airport, then he come to Wen Jiabao saying let's talk, so I can (inaudible). And also, this conduct by the United Nations and all the United Nations agreement is not binding, and the particular, this involved sovereignty. And this also a very basic problem in the Congress consider this.

I have heard all kind of discussion in U.S. U.S. discussion forgot what the problem in the U.S., and first speaker talk about going -- being in -- climate policy in U.S., particularly you mentioned in Congress. And those are very -- too whole picture.

U.S. state now is in a state (inaudible) non-government. And I don't know when we're going to have a climate change policy.

MR. LIEBERTHAL: Excuse me, sir. We have a lot of people who want to ask questions. Do you have a question?

MR. CHEN: No, I don't have question. I only have critical comment. Thank you.

MR. LIEBERTHAL: Thank you. Yes, over here.

MR. DALMAN: Thank you very much. Carl Dalman,
Georgetown University.

Thank you very much for the presentation. I have a question for both of you.

One issue that I want to see if you can clarify for us, there was some confusion at the Copenhagen as to whether China had said it was not going to be asking for part of the transfer of this financial assistance or not. I think the *Financial Times* reported, and then it was sort of -- so, where does that stand? Perhaps you can tell us a little bit.

Because, if China were to agree to that, that would give a tremendous leverage with respect to the developing world and will put a lot of pressure on the U.S.

MR. HOUSER: So, I think that -- you know, China understands that there will be finite funds made available for both mitigation and adaptation. And what Chinese negotiators have said publicly is that they will not compete for those funds with more vulnerable countries.

He Yafei, who spoke to the *Financial Times*, is -- can be a very expressive speaker. And whether he was misquoted or was kind of going beyond his mandate, not sure. But it's -- you know, it's one thing to kind of acknowledge that you won't compete. To state publicly that you're not going

to take any of the money is a more difficult position to defend domestically.

But I think there's a fairly wide acknowledgement within the Chinese delegation that the financing that's made available, that more vulnerable countries will be first in line.

MR. ANTHOLIS: I just only had one thing to add there, which is that -- everything that Trevor said is exactly right about -- particularly about official government financing. But, you know, the key thing that happened at Copenhagen was a commitment for the United States to help mobilize \$100 billion of financing, public and private. And a big part of the private financing goes to offsets through the clean development mechanism and other things.

And it's undoubtedly -- that is also controversial with respect to China, because China and India already have benefited from those, are likely to continue to benefit. And the real question moving forward, I think, once we get past whether or not the Copenhagen accord has any standing internationally is how those systems operate and how much of the share goes to China and India.

And that is a huge question moving forward, I think.

MR. LIEBERTHAL: Yeah.

MR. McVADON: Eric McVadon, the Institute for Foreign Policy Analysis.

How much of the Chinese stimulus package went towards

green projects? And has it all been expended, or are there still opportunities for U.S. investment that they might find in that area?

And how has the balance with the -- sort of the technological lead, you mentioned the Chinese batteries that were one -- are there other examples of that?

And then overall, is China enthusiastic about building trust and confidence now in this area? Or is it more interested in showing that it's already confident in itself and sort of being aggressive?

MR. LIEBERTHAL: (inaudible)

MR. ANTHOLIS: I also want to bring Ken in because he may know more on the stimulus package question.

I actually don't know the answer to that. I know a lot of it was directed towards infrastructure of various kinds. It's hard to say, and hard to count. And how -- the one thing that I do know about the Chinese stimulus is, a lot of this stuff was already in line and got packaged as stimulus and sort of expedited. It wasn't that different from ours, in some sense.

And on the new technologies, I think we should start pulling Ken into the conversation as well because he's been as much on the ground as anyone. The one thing that I do know is that, you know, the Chinese investment in this is both considerable and likely to continue and expand over the time horizon. And how much of it is going to be used internally, and

how much it's going to be used for export is a real question moving forward. I mean -- and it doesn't necessarily translate into emission reductions domestically. This may simply be another export opportunity for China, and that's one of the reasons people are very concerned if China is not talking about an actual target at some point in the future. At what point that kicks in is a real question about their domestic capacity to enforce it.

But I think this technology point is a really critical one, but it's not yet clear from a climate standpoint how it plays out.

The last question is the one that I find most interesting, which is sort of capturing Chinese intent. I think what we've seen is that this is a country that is no longer a black box. That you can't really tell domestically what's going on because there are a number of different forces. For me, the most interesting thing that came out of post-Copenhagen and China was the debate that erupted, not just at the negotiating table that Ken has chronicled, but in the weeks thereafter where you had Chinese scientists saying, essentially, China had not committed to enough at Copenhagen, they should be more aggressive. But a number of Chinese industrialists and people who have always seen the mission for the government as spurring economic growth, saying China gave away the store at Copenhagen. And so a debate is breaking out within China on this issue that is just underneath the surface. People are probably not quoted as much in the press, but some people are

actually increasingly willing to get quoted as criticizing government policy.

Within a month after Copenhagen, essentially the central planning authorities said, okay, the debate is over, we're going to implement Copenhagen. And that was a message to both sides saying, stop fighting over this and let's get serious about what it takes to implement domestically. And then just in the last few days, we've seen -- there was a Wall Street Journal story today -- the Chinese emissions intensity backslided. Whereas they had been making progress on emission intensity, suddenly it seemed that there was a 3 percent decrease in intensity as opposed to the 14 percent increase that had been over the previous years.

So I think internally it's hard to say what China's intent is. There are different forces out there. The government seems committed to the plan at Copenhagen, which as Trevor aptly described is a ground up -- bottom up approach. What can -- what does a country's leadership think it can do? And let's use the next set of years to benchmark how well it does against what it thinks it can do.

MR. LIEBERTHAL: Boy, on the basis of that answer I want to get Bill to join the John L. Thornton China Center staff. You really know your stuff. Did you want to add?

MR. HOUSER: I can add a point on the stimulus. You know, most of China stimulus, whether it was -- and I'm sure Anne is going to talk

about this more probably this afternoon -- but whether it's directly in the form of kind of fiscal allocation, or whether it was increased bank lending, ended up going to state-owned firms and kind of state-directed infrastructure projects.

What that means -- you know, a lot of those were projects that ultimately could reduce the carbon footprint for China. So, high-speed rail will reduce, you know, vehicle miles traveled and will reduce bottlenecks for coal transport where you have diesel trucks idling on highways for, you know, days at a time.

The near-term consequence, though, is an increase in Chinese emissions because all those projects take a lot of cement and steel. And so the balance of the Chinese economy between the service sector that doesn't use a lot of energy, uses a lot of people, which is why Beijing wants to grow that sector because it creates a lot of jobs, and the heavy industrial sector, which uses a lot of energy, but doesn't use a lot of people, has swung with the stimulus in a more energy-intensive direction. Which makes exiting from the stimulus and transitioning to long-term economic rebalancing, that Beijing's been trying to engineer, that much more difficult.

Now, whether these projects have a dividend in terms of their lower energy footprint over the long term that kind of compensates for the near term blip that shows up in the statistics that Bill mentioned -- the

increase in carbon intensity -- kind of remains to be seen. Depends on how efficiently that investment happened. But that's been the short term effect.

MR. ANTHOLIS: And just one quick thing on that. I mean, in the U.S. we had a similar -- the challenge of the metrics on this can be seen in our own Cash for Clunkers program. And China did a bigger one, right? Some people argue it takes fuel inefficient cars off the road and puts fuel efficient ones there, but it kept the auto industry moving. And one of the reasons that we had lower emissions last year in the United States -- 9 percent lower -- was because our economy crashed. Cash for Clunkers got the economy going again in the auto sector, it's likely that emissions will increase as a result of that.

So, the same thing played out in China where, if I understand correctly, the Cash for Clunkers program was even more expansive than that in the United States.

MR. McVADON: Ken you smiled when I said seeking trust in confidence are already overconfident in China's attitude.

MR. LIEBERTHAL: Oh, I was smiling because one of them was going to answer the question. (Laughter)

Yes, back here. If we could get a mic back there. The far side.

MS. RIEFEL: I'm Helen Riefel, Resources of the Future. And

I taught environmental science at Sichuan University in Western China for two years. And I'm very aware of how alert the universities all around China and the students are to the need for fighting climate change.

However, I'm always appalled in the discussions here in the United States at how seldom it's mentioned -- and you have not mentioned -- that per capita, the emissions in China are one-quarter the emissions in the United States. And it seems to me that the effort here should be much stronger than in China, where there's so much more poverty, especially in the West. And the need for development is so much greater. It seems to me the need for efficiency here -- and, again, the need for technical cooperation on our part with Chinese -- is very strong.

It's the one-quarter per capita that keeps popping into my head.

MR. LIEBERTHAL: Thank you. Of course. The problem with per capita is the number of capitas also makes a difference. And so you end up with, you know -- all of us have responsibilities here. I don't know what you want to add to that.

MR. HOUSER: So, that's true, of course. And that's part of the equity debate that makes this so challenging.

India would, you know, would offer a target -- has offered a target that our per capita emissions will never exceed the West's. China will

not take that deal, because China knows its per capita emissions will exceed Europe's shortly, like 2020 timeframe. And that would impose a constraint that would be more ambitious than they'd like to see.

The -- from a U.S. negotiating perspective, the view is not that China should do the same thing as the U.S. Clearly, China is in a different place in terms of economic development. Clearly, the kind of level of ambition that should be expected from China is less. The view was that whatever is appropriate for China, that China should be bound. That this binary distinction between developed and developing countries that was drawn up in 1992 and enshrined in the UN framework convention is out of date. Because there are a number of countries that are treated as developed who have per capita income and per capita emissions far lower than a vast swath of developing countries.

If you look at the 20 poorest developed countries that were classified as developed in 1992, today the top 40 percent of developing countries are richer than that. Including Singapore, that's the third richest country in the world on a per capita basis, all of the Middle East, and a large swath of emerging economies as well.

And so I think that it's appropriate to have a conversation about equity, about per capita emissions, about income levels, and about what an appropriate allocation of responsibility is. But that has to be a

conversation that's based on more than everybody who's stuck in that Annex 1 Treaty that we signed in 1992 gets to take action, and everybody who's not has no obligations. You have to -- there has to be a gradient beyond that.

MR. ANTHOLIS: Yeah, I think that's exactly right.

Again, the basic point is not only well taken, it's incorporated into everything that people are talking about right now. The United States has gone on record at the Copenhagen accord of saying that it's going to cut its emissions by 80 percent. What the Chinese have said is that it's going to cut the growth of its emissions, but everybody accepts that Chinese emissions will continue to grow because their per capita emissions are going to continue to rise as they rise.

But per capita emissions as the only standard is a troubled standard for a couple different reasons. Right now, for instance, per unit of economic output China actually produces more emissions than the United States does. And India is slightly more than the United States. So as their economic output continues to rise, they're still much more inefficient than we are.

And then as Ken said, the number of capitas really does matter. And this is where sort of population growth is an important issue. I wrote an op-ed on this in the Wall Street Journal last summer, and a number

of my friends in India teased me that I'm now known in India as the man who thinks there are too many Indians. So, that's not the case at all. But it does make a difference if China or India grow to 2 billion people by 2050 as opposed to staying in a 1.4 or 1.5 range, because those extra half-billion people, if they each produce, say, 5 tons of carbon a year, that's a lot of carbon that they're putting up in the atmosphere. So, these formulas are really quite tricky. And simply using per capita as a standard as opposed to per capita emissions per unit of GDP, which is really where the conversation is more going to, is probably an important distinction.

MR. LIEBERTHAL: If I could just add a footnote to Trevor's comment. Bill and I were at a conference at Aspen last summer, and -- which brought in people from around the world. At the end of that conference in the summary session, one of the key representatives from Africa got up and really was angry. And he said, you know, every time I hear China grouped with Africa on climate change I get very upset. We have nothing in common with China on climate change. Nothing.

They have technology that we don't have, they have manufacturing that we don't have, they have wealth that we don't have, they create damage that we don't create, we're the ones who suffer. As soon as you put us in the same category, we're dead. So, don't do it. All right?

All it does is highlight the reality that on this issue, the world is not

developed or developing. The world is enormously more complicated than that, based on how many people you have, on the structure of your economy, on your growth rates, on all kinds of things.

So you construct your equity arguments almost to seek yourself on this, you know. There's an angle that anyone can take to make themselves look better. But the reality is, if we fall considerably short of having the top 15 carbon emitters in the world get really serious about this issue, we're all in deep, deep trouble.

Yes, sir.

MR. MITCHELL: Thanks. Gary Mitchell from The Mitchell Report, and this is a question for any or all members of the panel. I want to probe a little bit more on the domestic politics of this issue in both countries. And I won't use the term drill down on that subject, but I'd like to probe it a little bit.

MR. ANTHOLIS: Drill, baby, drill.

MR. MITCHELL: Yeah. Interested to get your assessment of where each of these two countries stand respectively on the two components of this politically. One is the awareness and acceptance that the problem exists, which is arguably to say on the science, but more than that.

Second, it is then the policy components of then what do we

do about it. So, in China and in the United States, you're reading today -- you know, if we had a scale of 1 to 10, 1 being it's all hocus pocus, 10 is sort of the Bill McKibben it's too late anyway -- where are the Chinese, where are we on that component?

And second, then, depending upon your answers to that, where are we on the second piece of that, which is the capacity to put together policies that will actually get something done?

MR. HOUSER: So I'll take the first crack at those numbers.

I would say in the U.S. in terms of kind of faith in climate science and believe of urgency of action, we're probably right now at a 4 out of 10, I would say. Down from maybe a 6 last year.

And I'd say China's higher than that, probably 6 or 7. I think there's an intermediate step, though, that you have to look at between that question and the policy action which is, where does it fit on the priority list. And so for China, I think there's a much greater belief in the science and in the long-term effects. But when you stack it up in priorities, I think they actually come down somewhere slightly below where we do, even though we're at a 4 on the belief scale.

But the good news is that, as I said in my remarks, when you start to translate that into policy there are a number of other issues that have the same means as addressing climate change, where both countries score

much higher. So, energy security, trying to find what the industries that are going to create economic activity and employment coming out of a recession, local environmental protection -- all of those score very high in China and continue to score very high in the U.S.

And so I think in either country, a policy package will be motivated by that collection of policy goals, with climate probably being, if not last, next to last in what ultimately gets a bill moved. I would not be surprised if when Senators Kerry and Lieberman release their bill on Wednesday, climate change is mentioned pretty far down in the press release. Energy security and economic growth and job creation will be the headline pieces.

MR. ANTHOLIS: Yeah, not much of a disagreement with Trevor. I'd probably rate it a little bit higher in the U.S. I think the polls always ask the question differently, but generally the numbers had been about 75 percent of Americans thought it was either a serious or somewhat serious question 2 years ago and now the number is around 58 percent. But when you actually drill down, are you willing to actually pay something for that, the numbers get sort of scary where Trevor is.

That said, what is -- I tend to be a bit of an optimist on these things. There's two things driving action in the United States. One is that there are a number -- quite a large number of moderately inclined legislators

on the Republican side that actually understand the scientific challenge, despite all the Climate-Gate stuff about the East Anglia e-mail files from last year. You know, people like Dick Luger and Lindsey Graham and others, who identify with the issue and in particular see the next generation of Americans, college-age students, who have very high resonance for the issue.

Remember, we're an increasingly college-educated society. College graduates increasingly believe that climate change is real, and the younger they are the more so. And that extends all the way down to grade school level. I mean, the story that I always tell is getting into our Prius on Sunday and going to church one time and my six-year-old yelling at me for turning on the air-conditioning. And when I explained to her that not only is this an energy efficient car and I do this for a living, she just couldn't tolerate that. We were polluting the environment.

And I do think that there's -- and we, you know, send our kids to a public school in the middle of Virginia which is not, you know, sort of bedrock liberal America. You know, this is -- Lindsey Graham himself said this as articulately as anyone could in an interview with Tom Friedman. For him, it's a values issue, and it's a next generation values issue.

And in that sense while I think the oil spill in the Gulf of Mexico, on the one hand, makes this a much more difficult deal to pull together

because an important part of the coalition for passing a bill in the Senate is one that includes provisions for “drill, baby, drill” for more offshore drilling, there is sort of a moral charge and a next generation charge to this that I think the oil spill just helps draw attention to.

The Chinese side is just very hard to really get arms around, because you know, it's just very hard to make generalizations about a country with 1.2 billion people -- 600 or 500 million, Ken will tell me the right number -- that live in rural poverty, you know, who are literally dying to move into the cities and work in factories. Yet, there is certainly a government commitment to the issue. And the thing that drives that is the extraordinary impact that natural resources and the natural environment play on Chinese society. Having that many people living in rural poverty -- particularly in Western China, which is a pretty arid place -- the impacts are felt in a very direct way. You know, I remember Ken in his office showing me the relief map of China, and when you look at how much the country depends on those Himalayan resources -- even if the IPCC got the date wrong about when they could expect the Himalayan glaciers to disappear, the fact that runoff from those mountains would be affected in a warmer world is a big issue that really worries the Chinese, that water tables are dropping in the North of China. You know, it's just an enormous set of challenges that it appears, from everything that I've heard, Chinese authorities really believe

that this is a coming crisis and they want to get ahead of it.

They face the challenge of an expectation of 7 to 10 percent economic growth a year to just keep up with that flow of people from the rural countryside. And that's the biggest constraint. To the extent that they can steer that economic growth in a green way? I think that's terrific for them, but they also know that they have to keep the economy growing and they don't want to impose any constraints on it.

MR. LIEBERTHAL: In back, right in front of the camera back there.

MR. KONG: Hi, my name is Bo Kong from Johns Hopkins SAIS. Trevor, it's good to see you. Thank you for the presentations.

I want to ask this question to the panel and possibly Dr. Lieberthal. No one undermines the -- or doubts the efforts that the Chinese government has been making toward a low carbon economy, but if you go through the landscape, natural gas accounts for 3 percent -- less than 4 percent of the country's total energy consumption. Even if you boost shale gas, it's going to account for a small percentage. Nuclear accounts for less than 1 percent. By 2020, even if the country builds 100 nuclear reactors -- 80 to 100 nuclear reactors -- nuclear will account for, you know, about 5 percent of the country's total energy consumption.

So the bulk of the country's energy will come from coal.

Renewable will account for a small percentage, right now providing less than 1 percent of the country's total energy consumption. Plus the process to install renewable -- solar and wind -- can be very energy intensive and very polluting.

And so, if you look at the landscape, then you tend to conclude that the two serious -- two areas where impacts can be very, very significant are energy efficiency and the other area is coal, because coal is providing over 70 percent of the country's total energy consumption. And by 2030, the country will still draw at least 60 percent of energy consumption from coal -- or 50, over 50 percent.

But then you wonder how the United States can make an impact or have an influence on the country's clean coal consumption or energy efficiency. If you look at energy efficiency implementation in China, the success is lacking because of lack of financing for energy efficiency. China accomplished the good efficiency record in the '80s and '90s with annual decline of 5 percent of intensity, but then the record was reversed in the new millennium. And now the record seems to be pointing to the other direction again.

So my question is, then --

MR. LIEBERTHAL: I've got to ask that you get to a question.

MR. KONG: Yeah, my question is then, you tend to be pretty

pessimistic. Can the United States really have impact on the efforts in China? Because all the efforts seem to have internal problems or internal challenges. And so my question to the panel is, where are the areas you think the United States can have impact on China's efforts to reduce CO2 emissions going forward?

Thank you.

MR. HOUSER: Let me take a stab at the first bit -- the assumption, Bo Kong, that you're prefacing the question on and where the U.S. can have impact. Because they're kind of two separate questions.

So you're right, and that's why I broke down freedom of movement for the Chinese energy system into near term, which is all about moving down the demand curve, because you just can't substitute out at the kind of 100 gigawatt a year level that China's installing power capacity alternatives to coal.

And it's not -- because I think it's critical not to assume because a country has a coal endowment that they are pinned to coal as the resource. I mean, it's all about economics. You can have a lot of coal in the ground that it's not economic for you to use. The reason that coal fire power is hard to compete with is because you have a delivery system in China for coal fire power equipment that can now install at \$500 per installed kilowatt, right? Because you've gotten to scale doing 100 gigawatts a year, and it's

really easy for a Chinese design shop to come up with a kind of a turnkey, super critical, coal fire power plant and set them on the grid at a gigawatt at a time, right?

Getting to scale on an alternative technology to coal, at that level, will take time. It took China a while to get to that scale for carbon electric and Dongfeng to get to that scale of coal fire power equipment. And so in the near term, it's about structural change to the economy, energy efficiency, et cetera, while starting -- because that has a long lead time -- nuclear power, CCS, whatever your kind of base load solution is going to be. There's a long lead time in getting those supply chains in place.

So I think you have to look past 2020. I don't think that 2020 is the window as the kind of decisive factor. You can see a pathway for China -- hard pathway, but a pathway -- consistent with the 2-degree world that has significant structural adjustment in the economy, plus improvements in technical efficiency in the next decade, followed by more aggressive deployment of nuclear power and CCS after that.

In terms of where can the U.S. make the best interventions, you know, after kind of experiencing the past year -- I mean, we announced seven U.S.-China clean energy initiatives in Beijing in November, ranging from an initiative on shale gas, to renewable energy, to energy efficiency, to coal, to electric vehicles. And all of those are important areas of

cooperation. I think we have to be realistic in our view of how much our work together is actually going to change the needle in either country, right? I mean, we're -- as Bill mentioned, you know -- in the U.S. we're a \$2 trillion energy economy, right? China is a \$2 trillion energy economy also. There are areas where we can -- where our work together can have a catalytic effect. But ultimately it's going to be domestic policy that drives change in either of these markets.

So, where is our work together most promising? I think that in places where there are either institutional knowledge or infrastructure bottlenecks to wide-scale deployment -- bottlenecks to the kind of effectiveness of a policy incentive that's already been put in place, actually working and catalyzing change, right? So, in renewable energy both China and the U.S. are bumping up against this hard wall of grid constraints for broader wind power deployment. Because you've installed pretty much all the wind turbines you can, either in West Texas or in inner Mongolia and where the wind is and kind of getting beyond that is going to require some significant institutional changes in terms of electricity system governance and technological innovation.

There's a whole there that's greater than the sum of its parts, in terms of the two countries sharing expertise. I think there's areas in energy efficiency finance where our shared knowledge can really be

transformative. But ultimately, we're not going to change China's energy system and China's not going to change ours. It's domestic policy that'll do it.

MR. LIEBERTHAL: I'm afraid our time for this panel is up. I want to mention a couple of logistical items before thanking our panelists. One, the presentation by Deputy Secretary Steinberg will be at 12:45 in this room. Please be here and be seated by then if you want to listen to that, and I hope you will be here.

Secondly, for those who don't have other plans, there are sandwiches, coffee, cookies, et cetera, out in the hallway. Feel free to go out and enjoy. Those of us who work at Brookings especially appreciate your removing all fattening cookies from the premises before you leave the building today. (Laughter)

Third, and finally, I simply want to thank our panelists, Trevor Houser and Bill Antholis, for getting this day off to a terrific start. And we look forward to seeing all of you when Mr. Steinberg shows up.

Please join me in -- (Applause)

MR. LIEBERTHAL: Good afternoon. I'm Ken Lieberthal, director of the John L. Thornton China Center. On behalf of Richard Bush, who heads the CNAPS Program at Brookings, I want to welcome you all

here for those of you who were not here for the first panel late this morning.

I want to introduce Deputy Secretary Steinberg's keynote address to this conference first by reiterating the key issues that Richard Bush raised as themes for the conference as a whole earlier this morning because there's a major change that's characterized the U.S.-China relationship since President Obama took office. I think Richard and I both agree that that change is the movement of truly global issues increasingly to the center of the U.S.-China bilateral relationship. And among those global issues, the most important, we feel, are the issues dealing with the global economic and financial crises, the issue of climate change, and the issue of nuclear proliferation. This conference is, therefore, asking throughout the day about six key questions:

Do the United States and China understand the challenges like climate change, global economy, and nonproliferation in relatively the same way?

To what extent do we share mutual interests in these problems? Or to put it differently, what's the actual degree of overlap between American and Chinese interests on these big issues?

Third, how effective has our cooperation been to this point?

And fourth, does cooperation to date actually address the challenges at their core or is this cooperation so far around relatively

superficial dimensions of these various issues?

Fifth, do gaps between our respective interests actually significantly limit what we're able to do together?

And finally, what is the likelihood that the current mode of cooperation will effectively address or at least contain each of challenges?

It is a genuine pleasure to have Jim Steinberg here to deal with these issues. With Jim we are welcoming him back home to Brookings. In one of his many -- one of the many distinguished phases of an utterly extraordinary career, he served as a vice president of Brookings and as director of our Foreign Policy Program. Jim has also held a number of positions on Capitol Hill, including I think your first was with Senator Kennedy, if I recall. Yeah.

He has held a variety of major positions in the State Department in addition to being deputy secretary now; therefore, principal advisor to the Secretary. He was also the deputy head of -- I guess -- head of policy planning, deputy head of INR at various times.

He served as deputy national security advisor during the second Clinton Administration to Sandy Berger. And I had the great pleasure of working under Jim's guidance, and sometimes very strong guidance, during those years.

He also, before rejoining State, served as dean of the Lyndon

Baines Johnson School of Public Policy at University of Texas at Austin, and is on leave from that position while he serves as Deputy Secretary of State under Hillary Rodham Clinton.

It's always been a pleasure to know Jim. He's an extraordinary individual. I think the country is extremely fortunate that someone of his great talent is so committed to public service and has been willing to devote so much of his career to making the United States and the world a better place. So we're delighted to have him back at Brookings today to give his views on U.S.-China cooperation on global issues.

There will be time for Q&A at the end of the remarks. All the remarks and Q&A are on the record.

Jim? (Applause)

MR. STEINBERG: Well, thank you, Ken, for that kind introduction. It is always good to be back at Brookings and there are so many familiar faces and good friends here. It's a pleasure to be back. It always feels like you never quite went away. And you especially feel that, of course, because I have the honor and pleasure of having so many of my former Brookings colleagues being my current colleagues now in government, including the former leader here of the Thornton Center, Jeff Bader, who's doing such an extraordinary job for President Obama over at the White House, and so many other colleagues. And so it's nice to see

both the former administration officials who are populating Brookings and vice versa.

And I'm particularly grateful to have a chance to talk about the issues that you raised, Ken, because I think your observations are quite right. I think the big change in our relationship has been the centrality of these global issues and answering the questions that you put, really, I think, are essential to understanding both where we are and potentially where we can go in this bilateral relationship which has such enormous consequences not only for the people of the United States and China, but for the world given the central role that both of our countries play in both being part of the problem and part of the solution on so many of these issues, like the economy, climate, and the like.

I want to also express appreciation to my good friend and former colleague, Richard Bush at CNAPS. I'm glad to see CNAPS continues to thrive. It's something that I take a great deal of interest in. It's made a great contribution over the years under Richard's extraordinary leadership, so I'm glad to see things remain in very good hands here.

I think it's important to begin this discussion of our collaboration on global issues by reiterating the basic approach and sort of precepts under which President Obama has led our engagement with China. And as he said, "We welcome a China that is strong, prosperous, and a

successful member of the international community. Now is the time for our two great nations to join hands and commit to creating a prosperous future for our children.”

This is a commitment, a very forward-looking and positive commitment, which reflects the fact that we need to understand our bilateral relationship in a broader context. And this really goes to a point that Secretary Clinton made in a speech she gave to the Council on Foreign Relations last year, which is that, “Given the nature of these challenges we face and the changed global agenda, we face a world in which the central problem of our time is how to generate effective collective action to deal with the problems that no country on its own, no matter how powerful, can solve.”

And I think this is an insight that both the United States and China share and is at the core of our effort to deal with these global problems. So for us, the great challenge is to build these structures of cooperation which includes building, on a multilateral basis, institutions and mechanisms of cooperation for the 21st century. But also to undergird that with strong bilateral relationships with key players, beginning with our traditional allies, of course, but then also to the emerging powers, not just China, but also India, Brazil, Turkey, Indonesia, South Africa, and the like -- all of the countries which play an increasingly systemic role in dealing with the big global challenges of our time.

And I think although the press tends to focus on the day-to-day ups and downs of our bilateral relationship with China and, from time to time, proclaims near or imminent or virtual crises in that relationship, I think it's fair to say that if you look back over the last 18 months this has been a very strong and productive period in U.S.-China relations. And it has demonstrated that the two countries, our two countries, are able to work together effectively to deal with these big structural challenges of our time.

This is not to say that everything is always perfectly smooth sailing. I don't think any of us who have dealt with the U.S.-China relations would ever expect this to be without its difficulties or the cooperation would be automatic. But I think we've demonstrated over time that where there are difficulties, we can work through them. And that when there are differences or disagreements either of goals, but more typically among means, that we can work through them through dialogue, by building trust and trying to find common ground, by recognizing that on most of these big issues the core objectives, the core interests, are common between our two countries. And that while we may have differences about the best means to achieve them, that strong conviction about the common goal gives us a framework within which to work through these differences. And I'll talk through a number of those issues in just a moment.

So I think if you look at our strategy going forward, it has been

to build a strong and comprehensive relationship that deals with a full range of issues -- we don't have the luxury of just narrowing it down to a handful -- but also to build a relationship of trust across a broad range of issues, which then gives us a context in which to solve individual sets of issues that we face. And I think it's particularly timely to look at some of these areas of cooperation because we in our administration, and I'm pretty confident our counterparts in China, are right now very focused on working towards the second Strategic and Economic Dialogue, which will take place in Beijing in just a few weeks under the leadership on our side of Secretaries Clinton and Geithner.

When we think about some of the areas of cooperation, some of the areas that Ken identified, on her first trip to China, which is now almost a year and a half ago, Secretary Clinton highlighted three areas which she anticipated at the outset of her time as Secretary of State would be areas for -- where there was great opportunity for increased collaboration. The first was international and regional security issues, especially Iran and North Korea. The second was clean energy and climate. And the third was the response to the -- what was already then a clear, substantial global economic crisis, and building a new foundation for balance and sustainable growth. And I think on all three of those they have proved to be the core issues of our relationship. And I think we can see that we have made

security challenges, like counterterrorism and counter-piracy, the attempt to build a more sustained military-to-military relationship, and most urgently and the one that captures the headlines is dealing with Iran and North Korea.

I think if you look at issues like counter-piracy, for example, the deepening engagement in China in supporting global efforts to deal with this common scourge really demonstrates the degree to which China increasingly sees its part of having to do its share and be part of the global solutions and learning to work effectively with other navies and with other nations to deal with a common challenge and not just to free ride on the efforts of others. And I think this is a very welcome development. And we see that as we understand this is a common threat to commerce and to safe shipping, the fact that we have so many countries working together and countries which have not historically participated in these multilateral ventures is a strong example of how China can play an important and contributory role.

On the military-to-military front, there, too, we see progress, although it's not as sustained as we would like because we believe that it's important that military-to-military cooperation be an all-weather effort. And even when we have difficulties, it's important to sustain the dialogue between our militaries. But we have had some important exchange of high-

level visits on the military side which we think are critical to building trust between the two nations.

On Iran, I think the strategy that President Obama and Secretary Clinton have led since the beginning of our administration, which is to reach out to Iran and demonstrate our willingness to engage and to seek a diplomatic solution to our differences, particularly on the nuclear question, has proven successful, if not inducing Iran to agree to the steps that we think it needs to take, but at least to demonstrating that we are serious about looking for a diplomatic solution, and clearly putting the onus on Iran for the failure to make progress up to date. And I think as a result of that we are seeing unprecedented international cooperation in sending a clear message to Iran that its actions are not supported by the international community and that it needs to work effectively with us or it will subject itself to significant new costs.

We saw that last fall in the very important decisions taken by the IAEA Board of Governors in which we have the strong support of China and Russia. And now as we move forward in the Security Council, following on the P5-plus-1 process in which Iran and -- is dealing with China, Russia, and our European partners.

And while we have not fully adjusted our positions in terms of what precisely the action the Security Council should take, we've seen --

particularly since the President Hu's visit to Washington for the Nuclear Security Summit -- a growing willingness of our partners in the Security Council to recognize that the time has come to take significant action. I think it's clear from both their statements and their engagement in New York that China understands that an Iran which is seeking to develop nuclear weapons is not in its interest; that there is a need for a clear international message to go with that. And we are working very hard to reach common ground in the coming days in the Security Council to send a clear message to Iran.

The path to diplomacy remains open. We clearly believe that's the best way forward. But Iran will come to understand that there is a strong consensus in the international community that what it is doing is dangerous and it needs to change course.

Similarly, with respect to North Korea, I think the -- our willingness to both engage and to offer the prospect of engagement with North Korea -- but also to make clear that we have very clear expectations of what that engagement needs to produce -- has helped to build a strong international consensus both in support of diplomacy, but also in support of effective international measures where North Korea has turned its back on diplomacy. And I think that has paid off very substantially in the common actions we took along with China and the other members of the Security

Council in response to North Korea's missile test last year and its nuclear -- announced nuclear test last year, which led to, I think, both swift and unprecedented degree of consensus among the remaining parties in the six-party talks. And then have the Security Council to move forward with new sanctions on North Korea, which we believe are having a significant impact there.

We obviously face a very challenging situation with the sinking of the Cheonan and it really underscores the precariousness of the situation on the Korean Peninsula. And I think that we all recognize that we need a thorough and complete investigation. No one is trying to hasten unduly the conclusions on this, but we are determined to pursue this thoroughly and to follow the facts where they point. And this will in turn have an impact on how we proceed in dealing with the challenge of North Korea and its actions, not only in the nuclear front, but in other provocative measures that it takes.

And how we proceed is going to depend first on clarity on the cause of the sinking of the Cheonan; second, a clear understanding by North Korea that it must live up to its international obligations on the nuclear weapons program, on abiding with the UN Security Council resolutions; and more broadly, ending its belligerent and threatening behavior towards its neighbors.

Throughout this process, as I say, China has played an

important and constructive role through the six-party talks and in our engagements, both bilaterally and in New York. And now we are engaged in an intensive discussion with all of the key partners in the region, including China, on how to deal with this latest incident. And we very much hope that during this recent visit of Kim Jong-il to China that they had an opportunity to share with him their concerns about North Korea's behavior and to make clear that we are watching very closely to see how events unfold in connection with the Cheonan.

So that's the first basket in security. The second basket that the Secretary identified was on clean energy and climate. I don't think I need to tell this or any audience why it is that the United States and China have such a significant role to play in dealing with the challenge of energy and climate change. We are the two largest energy consumers, the two largest greenhouse gas emitters. And there's simply no imaginable solution to the problems either of long-term energy security or of dealing with the problems of greenhouse gases and climate without significant engagement and contribution by both the United States and China. And so it's now up to us to be the vanguards as it were to accelerate the transition to a low-carbon economy if we have any hope to meet the globally agreed objectives for limiting the concentration of greenhouse gases in the atmosphere and the risk of increased global temperatures.

And I think the evidence here suggests -- and I know a lot of people here at Brookings are spending time looking at this question -- that we are seeing a real sea change in the way that China's approaching this question, from its historical position of really sort of suggesting that either it wasn't a problem or, if it was a problem, it was somebody else's problem to deal with and, therefore, not a responsibility for China or somehow something that could impede China's economic development. We now are beginning to see a recognition that China recognizes in its own self-interest the need to deal with the problem of greenhouse gas emissions.

And so we've seen in China's national plan and its actions in Copenhagen that we are beginning to see China address what I think are the key challenges, which is to see China reduce its emissions below business-as-usual levels as it goes forward with its economic development and put it on a long-term path to meet the global needs for what climate science has told us is a sustainable level of greenhouse gas emissions or concentrations in the atmosphere. And to improve transparency and accountability so that the -- all of us can judge the extent to which the kinds of plans and commitments that China's making in its own nation level are something that can be essentially validated and perceived by the international community as well as to play a constructive role in international negotiations.

And I think we saw in the final outcome in Copenhagen a clear recognition of China taking at least positive steps, if not complete steps, on each of those elements. We've heard a lot about the difficulties of those negotiations. For those of us who were involved in Kyoto, I think this should come as no surprise in that the -- like many fine soufflés or meals, the test is not in how it looked while it was being made, but how it came out of the oven. And I think if you look at how Copenhagen finally ended, we saw some very significant steps forward.

Notably, for the first time, all major economies, including China -- and it's particularly significant that China was part of this -- making national commitments to curb emissions and to transparently report on their mitigation efforts, which is critical to giving credibility to these commitments. And now we need to all work together going forward to make the Copenhagen Accord operational with balanced commitments by all major economies.

And that international engagement has been complemented by our bilateral work on energy and climate. We've signed a Memorandum of Understanding to enhance cooperation on climate change, clean energy, and environment at the last Strategic and Economic Dialogue. When the President visited Beijing last November, we had adopted a packet of measures, including a new clean energy research center, an electric

vehicles initiative, and a renewable energy partnership. We also had agreed on a public-private energy cooperation program and cooperation on clean coal development. All very practical steps which can offer benefits to both countries and to our private sector partners who were part of these efforts.

So I think while we have a substantial way to go forward and we also have some things that we need to do at home, but we're very much committed, the President's committed, to that. I understand that we're going to see some movement forward in the Senate as early as today on new efforts to move legislation forward in the United States. We understand we need to do our part, but it's something that we can do hand-in-hand with China to meet this common and collective good of a clean and predictable environment.

So the third topic that the Secretary identified in her initial remarks was the challenge of the economic crisis and global growth. And I think here, again, we saw the potential of the partnership between the United States and China. This is not a G-2. We recognize that there's -- however important our two countries are to deal with these challenges, that we need the cooperation of all the systemic international players. But without the United States and China playing constructive roles, that the prospects for dealing both with the short-term challenges of the recent economic crisis as well as the long-term challenge of sustainable global

economic growth simply cannot be met.

And on this, I think, both countries did step up and do their part. China was a key player in the international coordination of the financial crisis. As you'll all recall, this was the occasion of the President's first meeting with President Hu. It was in London for the G-20 meeting. Both the United States and China adopted historically large stimulus packages to support both our national economic activity, but also part of the global economic strategy.

And now we need to turn to the elements that will make this recovery sustainable over the long term. And that, of course, requires China to recognize the need to shift to more consumption, a service-based economy, that that's in China's interest as well as the overall interest of the global economy. And I think we see clearly some signs that the Chinese leadership understands that basic insight.

We on our part recognize that we need to do our part for global sustainability, including the need to reduce our long-term debt. And that, of course, connects to the question of domestic consumption in China and other emerging economies as we try to sustain a more balanced economic growth.

Clearly one element of this, we've made clear, we believe is the importance of China moving to a market-based exchange rate. And I

think this is a principle that China has embraced and it's been reiterated by President Hu and Prime Minister Wen. And we look forward to our continued discussions on this topic. It's something that is not done as a favor to any one country, but is actually part of China's own national interest. Its economic leaders recognize it needs to be done in a way that recognizes that these are changes that take place over time, but we need to move in the right direction if we're going to give the global economy and global markets confidence that we're going in the right direction.

And moving towards market-based exchange rates is a win-win because all of the economies will be stronger, including there'll be stronger markets for our exports, but also a more sustained basis for China's own economic industries if we have a balanced growth.

At the same time, we recognize that as countries like China and other emerging economies play a greater role in the global economy, that we need to have their significant participation in the key global economic institutions. And so we've seen, as I said, the role of the emerging economies and the evolution of the G-20. We now have China with the third largest share of voting rights at the World Bank. And we support giving China a greater role in the IMF. And this gives China an opportunity to exercise leadership and responsible leadership in this long-term strategy to keep the engine of global growth going.

So all these issues are very much on our agenda and they all demonstrate that on the key global issues of our time that there has been significant progress and a real convergence, I think, at the highest levels on common and shared visions about where we want to go, as I said, even if we don't entirely agree in every detail on the means. And this really underscores the importance of the Strategic and Economic Dialogue, building on our very successful first meeting here in Washington. And in this upcoming meeting we will have even more senior leadership participation than we had here in Washington, with 15 U.S. Cabinet members and agency heads traveling to Beijing.

And we have -- we use this meeting both to deal with long-term challenges, but also, frankly, as an action-forcing event to help us move forward on some issues and to kind of crystallize the attention of leadership and to get things sort of taken out of the bureaucratic level to the leadership decision level.

It's also a great opportunity to sustain the dialogue between key decision makers and policymakers in both governments; for them to understand our thinking, for we to understand theirs as well. And hopefully, to influence decision making there. And the ability to do this across a cross-cutting set of issues that intersect between the strategic, political, economic, environmental, and energy is a particularly important feature of these

dialogues; to break down the stovepipes that exist in both of our bureaucracies and to think in a more systematic and integrated way.

The S&ED sets out an opportunity both to give long-term priorities for engagement, but also to have concrete tasks. So, again, as with last year, the S&ED will have two core tracks: the economic track where we'll be focusing on economic growth; and clearly from our perspective including the importance of sustaining employment here in the United States, building and strengthening exports and investment opportunities for American firms, as well as to encouraging China to move forward to contribute to economic -- global economic rebalancing.

On the strategic track we have three pillars: One is the pillar of counterterrorism, energy security, and military-to-military ties.

The second is the international regional security issues. In addition to the two that I talked about -- Iran and North Korea -- Afghanistan and Pakistan increasingly figures in our discussions where we also are having a very positive set of dialogues and working together on common objectives there.

And a third track focusing on cooperation through multilateral institutions on issues like climate change, health and pandemic disease, and food security.

Now, needless to say, in every one of these dialogues that

each side is free to raise the issues of their concern. And we will have an opportunity as we always do to make our points about issues that are important to the United States, including human rights and religious freedom, the need to protect intellectual property; our concerns about aspects of the military modernization in China, as well as the issue of the overall global economic balance and the role of exchange rates.

We will undoubtedly discuss core issues, like peace and security in the Taiwan Straits and, from our perspective, the need for China to have a deeper engagement with the Dalai Lama over Tibet within the framework of the One China policy that we have continued to reiterate.

On the economic and trade front, we will discuss our concerns about aspects of Chinese economic policies which we think have protectionist casts, particularly China's effort to link government procurement with innovation policy in ways that could undermine market access to key sectors of the Chinese economy. And as I said, this is an opportunity in both the formal and informal sessions for us to have a sustained dialogue, to exchange views in a friendly but fulsome way about each side's perspectives, which allows us to move forward and deal with these issues and the strategic importance to both.

So I think it's -- on the whole, the balance sheet is a pretty positive one. We don't want to in any way underestimate the fact that

important difficulties remain. But on these great global challenges, I think the answers to most of the questions that Ken raised are that we are heading in a positive direction. For the most part, the nature of these problems are such that our interests are shared in terms of the fact that we sink or swim together on issues ranging from global economic growth to health, to terrorism, to proliferation, to protecting the sea lanes, and other challenges that are in our common interests.

But we need to make sure that as we continue our support for China's growing role in the global economy and the world political structure that China's growth is a positive-sum contribution to the security and economic growth of the world; and that its growth and prosperity do not come at the expense of others; and that it's ready to play a constructive role in addressing these global concerns in security, economic, political, and environmental health issues. I think that's a challenge that can be met. It's one that we're certainly committed to try to work with China to achieve. And we are looking forward to this very sustained engagement we will have in Beijing in just two weeks' time.

So thanks for your attention and I look forward to your questions. (Applause)

MR. ZANG: Thank you. John Zang with CTI-TV of Taiwan.

Mr. Secretary, talking about the Taiwan Strait, how do you see

President Ma's recent remarks to the fact that in an interview with CNN he said that we will never ask the United States to fight for Taiwan? Are you encouraged by his determination to defend Taiwan on Taiwan's own strength or are you relieved that the United States will never be dragged into a potentially bloody war. Or are you concerned that President Ma may be distancing Taiwan from the United States?

Thank you, sir.

MR. STEINBERG: Well, I think we're quite -- generally quite encouraged by the direction of cross-straits relations between Taiwan and the PRC. I think we have long believed that a strategy of engagement by the two sides to look for a peaceful resolution of the issues is critical to their common future. This is something that -- in the end we have always believed that this is something that is best resolved through dialogue and that we've encouraged Beijing to make clear that it can respond to these efforts by the leadership in Taiwan to try to find common ground, to build trust across the straits. The discussions on the economic cooperation framework are particularly important.

And so that provides a foundation for the two sides really to deal with each other because this is a situation where conflict is in nobody's interest. And I think it's not particularly useful to speculate what would happen in the event that conflict comes about. The goal is to try to avoid it,

and that comes about by a commitment by both sides to look for a peaceful resolution of their differences that takes into account the interests and the wishes of parties on both sides of the strait.

MR. McVADON: Eric McVadon, the Institute for Foreign Policy Analysis.

Jim, you mentioned sea lane security a number of times; warmed the cockles of my heart. On the area --

MR. STEINBERG: Always glad to happy to do it, Admiral.

MR. McVADON: With respect to maritime cooperation, it seems to me that there's a window for things like humanitarian assistance and disaster relief exercises with the Chinese, and anti-piracy, of course, expanding that. And that folds right into energy security. But let me ask a question that I pose with respect to the global climate change issue with the first panel this morning. Are we saying that the Chinese have increasing interest in building trust and confidence or rather in demonstrating that they're already pretty confident?

MR. STEINBERG: I think, as I alluded briefly here and in more detail in an earlier speech I gave, I think one of the great challenges that we face is how we understand and how we adapt to China's growing military power. We understand and accept the fact that along with economic growth, that countries tend to develop their defensive capabilities, and that's

something by itself which is not necessarily objectionable.

But at the same time, because China's approach lacks the kind of transparency that we'd like, we do have questions about the long-term intentions. And that's why we want to strengthen the opportunity for military-to-military exchanges and dialogues, so that we have a better understanding of China's goals, plans, and intentions and what's driving its decisions over military modernization, not just in terms of equipment, but also in terms of doctrine and its operations, to give us the assurance that what it is seeking to achieve is consistent with the security and broader security, political, and economic interests of others.

So to the extent that China has a greater naval and maritime capability to contribute, as you say, to counter-piracy and to humanitarian efforts, that's clearly welcome. And the capacity to go further out and yet to contribute to those things is a contributor to global well-being and global security. But because there are other aspects of their modernization program, particularly in the maritime field, that are less clear, we would like to get greater clarity about what their goals or intentions are and to build the kind of trust between our militaries and our leaders that'll let us understand what that is about.

I think we hope to persuade the Chinese that we're -- the world that we live in requires more cooperation, not competition. And that

neither side will benefit from a military competition between the United States and China or between China and any of its other neighbors. This is a situation where we've learned from long experience that the risks associated with those kinds of competition are severe and that nobody wins in the long term. And so I think that's why dialogue is so critical in this sphere and why we've tried to persuade our Chinese counterparts to try to insulate that dialogue from our disagreements on substantive issues so that we don't lose the opportunity to discuss areas where we have concerns as well as where we have obvious common interests.

MR. NELSON: Thanks, Ken. Thanks, Jim. Great talk. On the -- I'm sorry, Chris Nelson, Nelson Report.

On the recently completed North Korea meeting, are you getting a sense that the Chinese are getting a little bit closer to seeing the U.S. argument that North Korea as it is is a strategic threat to China? Or are they still trying to keep it going just somehow?

And in that regard, as the Cheonan incident shows, regardless of who's judged to be at fault ultimately, it does seem to have started a more considered discussion of the level of U.S.-South Korean military intelligence sharing, perhaps enlarged BMD, all that sort of thing. Do you think it's correct to be thinking about an enhanced U.S. relationship with South Korea in the military and strategic sphere, leveraging that on Chinese progress in

seeing our point of view on North Korea? Or is that -- am I mixing apples and oranges, going too far with that?

Thanks.

MR. STEINBERG: Well, let me kind of begin with a few general observations and then -- I think first, you know, I think it -- I'll let the Chinese speak for themselves in terms of their own assessment of the situation in North Korea. And I'm sure they'll have some things to say about that. But I would say, first, that there is a strong understanding that stability in the region is in the interest of all the neighbors -- and that's a common interest -- and that aspects of North Korea's behavior, particularly their nuclear activities, is a threat to that stability and that we have a common interest that binds the other five-party in six-party talks together to address that, as well as other risks of instability coming out of North Korea. And those are the subject of intense consultations, both bilaterally and multilaterally, among all of the various combinations and permutations, in two, threes, fours, and otherwise of the parties in the region.

I think no country can feel entirely at ease with the situation in North Korea right now. And we are looking for ways to work together to try to address that in ways that enhances the common security of all of North Korea's neighbors.

I think in terms of our engagement with South Korea, I mean,

it's hard to imagine a much more enhanced capacity than the unique relationship that we have with South Korea, both on a political and a security level. I mean, the combined command is an almost unique example of two militaries that are deeply, deeply intertwined in dealing with the security challenges of the Korean Peninsula. And we work together, you know, in a remarkably united way together as two militaries to address those challenges.

So whether we need to make specific adjustments in our posture or operations is something I'm sure we'll all take a look at. But in terms of the need to get closer it's just hard to imagine. And that extends not only to the operational day-to-day of the two militaries, but I think on the political level, beginning with our two presidents. I think the level of cooperation and consultation between the United States and the Republic of Korea now is unprecedented in my experience, which now isn't as long as Jack Pritchard's, but it goes back a ways.

And I am really very encouraged and heartened by the degree to which we are working so closely together on a full range of issues, not just on the issues of stability on the Korean Peninsula, but the strong contribution that South Korea's making to our efforts in Afghanistan, its global commitment on piracy, and other issues. It really is a remarkably strong and important bilateral relationship. And so that's why we're working so closely

together on the investigation of the Cheonan. It's why we are consulting closely on all aspects of the challenges on the Peninsula. And I'm confident that that close collaboration will continue as we move forward.

MR. KLUG: Hi. Foster Klug with the Associated Press.

You seem to be willing in your speech to link the Cheonan to the future of nuclear talks. Is there any other guidance you can give on what else the U.S. is prepared to do if, as appears will happen, there's some sort of linkage to North Korea with this attack?

MR. STEINBERG: Well, I'm going to resist all those "ifs" in your question. We have made no conclusions. We are continuing the investigation. We will do this thoroughly, objectively, and in close cooperation not just with the South Koreans, but this is actually a multinational effort with Australia and Norway and others who are involved in this. So this is not -- I think it's been very important that this is a broad-based and very objective assessment. And I don't propose to speculate on how this will turn out because we don't know yet. And we really want the facts to lead us, but we won't -- at the same time, we will follow the facts where they go and we'll draw the conclusions from the facts.

But I do mean to say that we can't be indifferent to this event. This was a very -- a deep tragedy for South Korea and the people of South Korea are entitled to a full -- as full an explanation as possible as to what

caused it, and we will work with them to do that. And until we have clarity about this, I think it's important for us to be careful about how we move forward, leaving open any of the possibilities and without prejudging what the possibilities of this investigation are.

But I think right now is a time to be prudent in terms of our actions going forward. And we've encouraged all sides to be prudent in every respect until we know what the results of those investigations are.

MR. LIEBERTHAL: Let me say it's a very serious issue. I was smiling as Jim was answering this only because I was recalling back when I joined the National Security Council, Jim sitting down with me and explaining it to me that as an academic, I probably like to deal with hypothetical questions, but as a member of the administration never answer -- never, ever answer a hypothetical question from a member of the media. So it's a pleasure to watch you.

MS. BAGCHI: Indrani Bagchi. Deputy Secretary, China just announced last month that it wanted to supply two new nuclear reactors to Pakistan under an agreement which is probably not grandfathered by their NSG entry. How do you look at it and what are the conversations that you have with the Chinese on this subject?

MR. STEINBERG: Well, I think, as you suggested from your question, I think, you know, the question is what is the status of this

assistance and how does it fit into understandings with the IAEA? And I think this is something that is still under discussion among all of us. Obviously it's important, from our perspective, that all countries live up to their commitments. As you say, the Chinese have argued that it's grandfathered. This is something that we haven't, I think, reached the final conclusion on, but it's something we're obviously looking at very carefully. But I think it's important to scrupulously honor these nonproliferation commitments, so we'll want to continue to engage on the question about whether this is permitted under the understandings of the IAEA.

MR. CARDEN: Thanks. Isaac Carden from National Defense University, INSS.

I just hope you can expand a bit on your comments on U.S.-China security dialogue on Afghanistan and Pakistan where you said -- you noted that there was -- that it increasingly figures into the security dialogue and that the dialogue has been constructive. And I didn't quite hear whether you'd said the dialogue was on common objectives or interests. And I wonder if there is, in fact, a meaningful distinction.

And then just expand to dig a little deeper, is Chinese investment or commercial activity consistent with U.S. objectives in Afghanistan and/or Pakistan? And is it -- or is it insufficient without greater coordination on political and security affairs?

MR. STEINBERG: Well, we have, as I said, had an intensified conversation with China on these issues. Ambassador Holbrooke has been to Beijing several times. We've had conversations both in Beijing and elsewhere. The Chinese have participated in a number of the multilateral meetings involving Afghanistan. And I think our objectives are largely coincident in Afghanistan. I think we all seek a stable Afghanistan that has an inclusive government, that's responsive to its people, and a particular concern to both of us that it does not harbor violent extremists that can pose a threat to the United States, to Afghanistan's neighbors, and the international community as a whole. So I think the basic framework in which we approach these things does have a shared set of interests.

We welcome Chinese economic investment in Afghanistan. Clearly, creating jobs and economic opportunity is part of the long-term strategy for creating a stable Pakistan. Creating alternatives to illicit production of narcotics and other sources of income for the Afghan people. So investment is important. And as long as that investment is transparent and meets generally accepted international standards to the extent that it involves assistance, we welcome it. And it's something we've had a dialogue with the Chinese about, but it's largely a positive one.

Similarly, with respect to Pakistan, we think that China can play an important role in helping strengthen the capacity of the Pakistani

government to meet the needs of its people and to provide an alternative to the extremism which threatens the Pakistani state as well as the rest of us.

So I think in the main, our interests and objectives are common. They're never identical in any case, but it's important that all of the neighbors who have a big stake in a stable and non-threatening Afghanistan work together. And we've been encouraged by China's growing willingness to be part of that effort.

MR. MITCHELL: Mr. Secretary, Gary Mitchell from the Mitchell Report.

Earlier today, we heard a very thoughtful panel talking about clean energy, environment, et cetera. And there was an interesting sort of factoid that came out of that about what happened at the tail end of the conversation between President Obama and his Chinese counterpart in Copenhagen that reflected what, I think it's fair to say, is a significant difference within the China policy elite on questions related to clean energy and climate, which leads me to ask a question that has three components parts, but they all should run together.

One is, are you seeing that kind of dissension on the other two components that you identified in Secretary Clinton's speech: security and global financial crisis? Are you seeing that kind of division or dissension or however you might describe it?

Second, is it growing or is it static?

And third, to the extent that it could be done, is there a way to characterize what the nature of political differences of opinion in China are like in the way that it would be easier to do, for example, in this country to talk about right versus left and Tea Party, et cetera?

MR. STEINBERG: I don't know whether there's a Chinese equivalent of the Tea Party, but I'm not going to go there. Good tea.

I think, you know, the climate and energy issues, because they are so deeply caught up in economic issues, obviously have different impacts on different sectors of society. You know, different sectors are impacted to a different degree by climate change and climate disruption, and the cost of adaptation and the cost of mitigation fall in different sectors, and that's true in any society. And so I'm confident that there's as lively a debate in China among the various stakeholders about these issues as there is in the United States. But it's the role of leadership to provide an overarching framework and to figure out where the national interest lies.

And I think one of the positive signs that we've seen is that there seems to be a growing recognition that the most senior leadership in China that when you put it all together, that China's future depends on China taking significant measures to address this challenge. There are lots of reasons why it's in China's interest and there are probably lots of internal

political reasons why the Chinese leadership is moving in that direction. And I'll leave it to Cheng Li and others to explicate their thoughts on this.

But I think it is significant that as they think about this sort of contending voices and perspectives within China, that there is -- seems to be a growing rate among the leadership to recognize that China needs to get out in front of this. It's in China's interest on economic grounds because it needs to adapt for the future and have an economy that will reflect what is the inevitable transition to a low-carbon economy. I'm confident of that and I think the Chinese leadership recognizes that China could benefit from being, you know, part of the solution rather than part of the problem.

I think it's important to remember on so many of these issues that the effort to deal with carbon emissions and greenhouse gases is deeply tied up with more localized forms of environmental damage in China, which also gives the Chinese a strong incentive. You're talking about black carbon you're talking about particulates, lots of other aspects of the cost of the environment. Just as in our country, the leading edge was clean air, clean water, and more localized environmental issues, they come together and gives them a strong natural constituency.

As China's own economic well-being advances, its people increasingly are tired of, you know, polluted air or polluted water, and the like. And so these converge a round of issues and are also a recognition

that there's a cost to China from being seen in the international community as not helping to contribute to the solution. And I do think that was an important part of what took place in Copenhagen, was a recognition that China will be viewed in the court of global public opinion just as we will if we don't meet our responsibilities.

So whatever the contending forces are, I think what we are seeing is that whoever's summing them up at the senior leaderships there, seems to be willing to move forward -- not as much as some would like to see, but at least in the right direction -- on these issues.

MR. OTTEMAN: Hi. Scott Otteman with Inside U.S.-China Trade.

At the end of President Obama's visit to China last year, as part of the communiqué there was a mutual commitment by both sides to accelerate bilateral investment treaty talks. Since that time, the United States has been engaged in a review of its own bilateral investment treaty model. It was supposed to have initially reported to come out at the end of last year. You're still working on it. I wondered if you'd give us a status report, if there's likely to be any further acceleration of the talks with China, which are stuck at a technical level.

MR. STEINBERG: We're still working on it.

MR. OTTEMAN: How about then in terms of your talks on

indigenous innovation with the Chinese that you mentioned? You would speak up about it at the next S&ED.

MR. STEINBERG: Yeah. No, this is obviously of considerable concern to us. We think this is -- it obviously has a huge impact on the United States and our firms and our investment in China. And we think it's -- in the long term it's counterproductive for China's own interest. I think long history shows that this kind of infant industry protectionism or these kinds of tools in the long run tend to distort even the country who's nominally trying to promote its own interests. So we think that China's own long-term interests would benefit from a free and open playing field that allows -- that global firms, including U.S. firms, to come and compete on an even basis. It is the core principles behind the WTO. Clearly we would like to see China extend that into the procurement field.

And I think, you know, I'll leave it to Secretary Geithner to elaborate as he gets into his discussions in Beijing, but I think that the Chinese certainly understand our concerns and we hope that they will be responsive because we think that in the long term this is -- the system that China will want to belong to is one that promotes a true level playing field in China that will bring world-class investment to China by firms from around the world.

MR. HAROLD: Mr. Secretary, Scott Harold of the Rand

Corporation. Thank you for your remarks today and your service to our country.

In interviews in Beijing across the last two weeks, as well as in Shanghai, the subject of the S&ED came up quite frequently. It was always highly praised and almost always immediately followed with: We need this from our side, the Chinese side, as an opening for our top leaders to give the room for policy innovation and relationships to be built at the working level. However, the follow-up would go, we would then like a secondary track, 1.5, or track 2 where our working level officials could talk with your working level officials to build the kind of ideas that can push up into that space that's been opened up.

Without wanting to put you on the spot, sir, I wonder if this is something that the U.S. side would welcome, has thought about, or would be open to if the Chinese side were to propose it or if we were to propose it to them.

MR. STEINBERG: Yeah. I mean, I would say, first, we would welcome it. And I think we kind of think we are doing some of that. I wouldn't call it a track 1.5. It's just -- it's the intercessional work that takes place between, kind of, the big, high-level plenaries. But we've all recognized that for these things to be effective, we have to do the work in between the formal sessions of the S&ED. And I know many of my

colleagues who are working on these individual issues would say that that's exactly what they're engaging on. We probably do need to do more. I think we -- certainly I know that in at least one of the meetings between the Secretary and State Councilor Dai, we explicitly talked about the need to strengthen these ongoing mechanisms so that these aren't just episodic engagements, but really do produce sustained work.

So I think it's something that we feel we're doing some of now. We clearly could do more and would welcome the opportunity to engage on a more systematic basis.

MR. HA: Thank you so much. Yeah, I'm (inaudible) Ha, a correspondent from South Korean newspapers, (inaudible). I'll try not to use the term "if," but it may (inaudible) some hypothetical question.

Once the final investigation report by the South Korean government about Cheonan incident is finalized, can the schedule to transform 2012 (inaudible) can be rearranged? What is your opinion?

MR. STEINBERG: The only thing I want to say on that issue is I don't see any linkage between the two issues. I think that we have -- we've had a long discussion and we will continue to have discussion about the command relationships on the Korean Peninsula. But I would not see that whatever discussions we have or don't have on that topic would be influenced by this particular incident, however it comes out. I think that's

something we want to make sure that whatever command relations we have serve the interests of our two countries and promote stability on the Korean Peninsula

MR. LIEBERTHAL: Jim, thank you very much for coming over here and giving this masterful overview. (Applause)

MR. BUSH: I'm Richard Bush again and our subject this afternoon is Dealing with States Going Nuclear.

One of the issues in U.S. foreign policy that you may not know about is export controls. And the subject of export controls is dual-use items -- items that have a civilian purpose, but also can be used for military purposes. And nuclear power is the ultimate dual-use item because it can be used to provide electricity and do so in a low carbon way. It can also be used to create the most horrific weapons which can turn -- can -- have the potential to turn weak states into dangerous ones.

And we're looking today at two cases where the countries concerned started out appearing to be interested only in nuclear power, but it turns out they're interested in something else. And they may have been interested in that something else -- a nuclear weapons program -- from the very beginning. So this now poses a challenge to the international system, to the security of the Persian Gulf region, and in the case of Iran and Northeast Asia and in the case of North Korea. And as we have already

heard from Deputy Secretary Steinberg, it's a focus of U.S. interaction and U.S. cooperation.

So that's the subject this afternoon. We have two -- four outstanding panelists. From left to right, Charles "Jack" Pritchard, president of the Korea Economic Institute, former colleague here at Brookings and in the Clinton Administration; Jonathan Pollack at the Naval War College, formerly at RAND; John Garver, Georgia Tech University; and Ken Pollack, a colleague here at Brookings. I think as far as Jonathan and Ken know, they're not related. But at some point they probably were.

SPEAKER: You can do a genetic examination.

MR. BUSH: That's right. That's right. So, let's start with North Korea. And Jack will talk first about the issue in (inaudible) and then Jonathan will talk about how well the United States and China are working together on that subject.

Jack.

MR. PRITCHARD: Richard, thank you very much.

I did a program last week at Brookings and I was remarking how it was -- I just really appreciated the opportunity to go last at a two-day conference. And I've now just figured out what is worse than going last at a two-day conference, and that is following Jim Steinberg.

Now, I'm not a mathematician, but by my calculation we lost

almost half the audience, maybe not quite. There are four of us and that ratio means that we're about one-eighth the draw of Jim Steinberg. But we're going to persevere anyway.

You know, one of the things that it's a pleasure to be is on this panel. And it's probably not the right thing to do, but I'm going to start off by stealing Jonathan's thunder and telling you if you haven't read his latest paper. It is "North Korea's Nuclear Weapons Development: Implications for Future Policy." It is a terrific overview and suggestions on what to do forward on that. And I don't know if you're going to speak about that, you may not, but I found it absolutely worthwhile and I commend you all to take a look at it.

Well, the first thing I'd like to do is kind of focus in on what is the U.S. concern about North Korea because that helps us answer that question later. And throughout my dealings with North Korea, you know, the thing that I would tell people even as we dealt with the developments of their nuclear weapons problem -- program is I don't wake up in the middle of the night thinking that North Korea is just on the verge of mating a nuclear weapon to one of their missiles and therefore San Francisco, where I was born, is soon to disappear. But it is, by far, the question of proliferation. And I think a lot of this will follow through as we go through this presentation.

We have to be most concerned about what the North Koreans

are doing, why they are doing it, what they have, and the potential for it becoming less than accountable on their part. Richard has asked a question and I won't reveal it now, but it is a very pertinent question and it has -- the answer has to do a lot with this particular issue.

And so we have dealt with the North Korean problem for a number of years. We have had fleeting glimpses of success in the agreed framework of 1994 that froze the North Korean nuclear issue for some period of time, but not completely. It had its flaws with respect to the Nuclear Non-Proliferation Treaty. It postponed our reckoning of what North Korea was supposed to do to a later date which we never got to because of a number of things that I think that you are well familiar with.

And so I think at this point now, rather than suggesting that the six party talks are the panacea and we need to get right back to them, I'd like to take a different attack. One of the things that we need to do is to stabilize the size of the North Korean problem immediately. We need to minimize the future risks that we have with regard to North Korea. When we have that opportunity that follows then, we should remove as quickly also possible the fissile material that North Korea has. Now, what that suggests to me -- it's kind of the endgame here -- is that once we get back to active negotiations with North Korea, we really ought to be doing something different, something that we have not done in the past, and that is to negotiate the endgame first.

We need to control the material as quickly also possible, dispose of it, and then kind of clean up the game afterwards.

The piecemeal approach that we have seen over the last several years really did not work and it opened the door in periods of time for North Korea to expand a rather limited amount of fissile material. Basically, we started behind with North Korea having possession of some small amount of fissile material in the range of one to two nuclear weapons worth of plutonium. That opened up dramatically in the March timeframe of 2003 as the second nuclear crisis got underway. The North Koreans furthered that in 2005, each time expanding their possession of nuclear materials to the point where their program matured in October of 2006, as you know, to their having detonated the first nuclear device that was followed this past year towards the end of May, almost one year ago today in a couple of weeks, where they detonated a second device.

Now, what's happened between -- I don't know, the last 18 months or so -- is there has been an unfortunate relaxation of concern -- that's probably not accurate, but I would characterize it that way -- in which we have settled into the maintenance, the management of North Korea's Nuclear Weapons Program. We have not actively been seeking to get rid of the stuff. There's a lot of reasons for that. Not all of those are the Obama Administration's problem. They've done a lot of things that are absolutely on

track, but we are not moving in an effort now to get rid of this material, which I suggest is the main problem.

Now, compounding that -- and I don't want to spend too much time on that; we've had a number of programs recently -- is this Cheonan incident. I know Secretary Steinberg indicated that there wasn't a connection between the Cheonan incident and the movement towards the transfer of OPCON, Operational Control, during wartime from the United States to Korea. I would suggest that there probably is a domestic political connection that we can explore offline. But what it has done is to suggest, as Secretary Steinberg said, that we cannot be indifferent to it. And that indifference puts us back into the management -- continuation of the management of this nuclear issue. We are postponing our active resolution of the situation.

So what are we going to do in the meantime? What makes sense? For me, lacking the active resolution, then we've got to make sure that we don't end up with the inadvertent or deliberate movement of fissile material from North Korea elsewhere. And one of the things that probably needs to be done is an emphasis on the consequences to North Korea should that occur.

And I've probably told this story too many times, but I'll spend 30 seconds again. When I was in government, without any particular

direction or authority -- I told the North Koreans directly, probably in 2002, 2003 -- that proliferation was the redline that the United States would not tolerate. Considering during the '93-'94 timeframe, reprocessing was supposed to have been the redline for which the United States, according to Bill Perry, former Secretary of Defense, was prepared to use military force on. They passed that redline a couple of times recently.

But I was convinced in a post 9-11 environment that the United States would not tolerate the transfer of material, or technical assistance if you will, to a third party. Well, we saw very clearly that the North Koreans did just that. We found out in September 2007, as the Israeli Air Force bombed the Syrian nuclear facility, that the North Koreans had been involved in the transfer of assistance to a third party to help them in their own nuclear weapons program.

Now, the problem with that is, if you take a look back, there was no consequence. You know, there was nothing that the United States did that reinforced to the North Koreans that this was unacceptable behavior. So one of the things that we've got to ensure, even in this period of inactivity, is that message has to go back to the North Koreans that proliferation really does matter to this administration. And that once we begin the active resumption of six-party talks, one of the agenda talks has to come back on the plate that is a resolution of what happened with Syria.

And it has to be done in such a way that it sends a signal to North Korea that we really would not and will not tolerate the proliferation of fissile or technical information there.

Now, this is, I think, necessary because we've missed the boat on a couple of occasions. One of those is -- you may recall in January 2003, as the North Koreans were breaking out of the agreed framework, one of the things they did was to withdraw from the NPT. And I find this somewhat, you know, amusing to a degree -- the manner in which they did this. You may recall that in the '93-'94 period, the North Koreans actually announced their withdrawal from the NPT. They were supposed to give 90 days' notification. They gave notification and the clock began ticking. It went on 89 days and some number of hours until they suspended their withdrawal from the NPT based upon progress that was being made and eventually concluded with the agreed framework.

In January of 2003, after a confrontation with the United States over a concern about highly-enriched uranium, the North Koreans said, okay, we're going to withdraw from the NPT. Oh, by the way, that becomes effective in about 10 hours. We are combining the notification that we gave you nine years ago to what we're doing today. That sends, to me -- and just to put an emphasis on this -- the U.S. response to that was not to formally protest. And that was unfortunate.

One of the things that I think that we need to take advantage of is fully understanding North Korean motivations. And this is where I come back to commend the reading of Jonathan Pollack's paper. He does just an absolutely wonderful job of tracing the developments of the North Koreans' nuclear program and gives us a much better understanding of where they are, where they've come from, and where they're likely to go.

For the North Koreans, I think there has been an added factor that we -- that most of you are aware of, but we've got to keep it in mind -- is we look to the potential solutions. And that is the events of the last almost two years now -- in August of 2008, you're well aware of what we believe to have been a stroke by Kim Jong-il. What that did in effect through his recovery period at the end of the Bush Administration and the beginning of the Obama Administration, the things that we saw there, the inability to come to conclusion about a verification regime with the Bush Administration, what was perceived by the Obama Administration to be very provocative actions by preparing for and launching a long-range missile on April 5, 2009, followed some short weeks later by the detonation of their second nuclear device, all suggest to me that the North Koreans then and are now in a position where they cannot show weakness, nationalism is of a priority, and they're in no position to compromise.

And so as we take a look at the ground here and we solicit

assistance from others there are a couple of things to take in mind. The situation is not the same as it was towards the end of the six-party talks -- the last active phase of the six-party talks. The situation in China with regard to their own national security interests I don't think has changed that much except their full understanding of what is going on in North Korea.

Now, the second part of this is the regime itself is under stress, the North Korean regime. And their attempts in a very belated manner to find a route to succession that has always been understood as their understood manner from transitioning from Kim Jong-il to a later leader, has been extraordinarily late in coming. I won't go into those details other than to say that the North Koreans, as they are positioning themselves for the next couple of years with 2012 being an important date for a number of reasons, that they are not now in a position to walk back on a voluntary basis their nuclear weapons program.

So where does that leave us? It suggests to me that we ought to take advantage of the vulnerabilities of the North Korean regime -- the things that they hold dearest in terms of regime survival, regime successful transfer of power, and the pointing towards 2012. Now, you know, what happens if we are to resolve the Cheonan incident to a satisfactory conclusion that allows the six-party talks to be resumed and, you know, what's the probability that the North Koreans are going to in the near term

give up their nuclear weapons? Quite frankly, in my opinion, very little.

A lot of this has to do with, you know, there's a political science theory of ripeness. The situation is not now currently ripe for North Korea to move forward on its own initiative and so it is incumbent upon the United States and its partners to help shape that environment. And people may have heard me say this before. But what I want to do is to spend one sentence talking about what North Korea is doing in its attempt to shape the environment. Kim Jong-il has just returned from a trip to China. We don't certainly have the full reports of what's going on now, what has transpired between Kim Jong-il and Hu Jintao, but one of the things that we have seen come out of that is a suggestion that the North Koreans said that they're going to help with the Chinese to create a more favorable condition in which they then can participate in the six-party talks.

Well, what are those conditions? Well, we know them from the recent past. They'd like to have a peace regime dialogue with the United States. They'd like to have the sanctions withdrawn there. So what they are attempting to do with their relationship with the Chinese, in fact, is to shape the environment to their advantage. Now, what we need to do is to move as rapidly as we can to pick up the momentum that I believe has been lost. And I want to end on this particular point. Shortly after the second nuclear test in May of last year, the following month there was a consensus that

resulted in the development of U.N. Security Council Resolution 1874, for which the Chinese were part of the authorship of that. Now, even knowing what their own national security interests are, and they do not include bringing down the North Korean government, the Chinese, in my opinion, started off a lot on the right foot in the implementation and at least the verbal implementation of 1874.

One of the things that the Obama Administration did to its credit was to create a sanctions coordinator, Ambassador Goldberg, who on two occasions visited Beijing among other countries and kept the focus and attention on the actual implementation and effectiveness of 1874. One of the things that I would remind you on about 1874 that in my opinion is significantly different than other Security Council resolutions and sanctions in general is that while it was directed at North Korea, the responsibility was universal. On each of the members of the United Nation, they were required to do a number of things -- to identify, to board, to search, et cetera, to report, to dispose of. And on a number of occasions that we have seen, this was successfully done. And in my opinion there was a very small window of opportunity last summer when the North Koreans, while they certainly did not believe the sanctions were adversely affecting them on a day-to-day basis, they did not like the path or the direction of where this was headed. And it created for a moment in time a charm offensive by the North Koreans

to improve their relationship with the South Koreans, with the United States, and to try their best to get out from under the future application of the sanctions.

Now, I would suggest that this is an important part of what we need to be doing. It is a vulnerability that -- and I'm not going to go into much, if all, in terms of the Chinese role there, but I do think that there is a positive role to be played based upon their own commitments there. That if we could get back to that moment of time, which hopefully isn't asking too much given our full understanding of what their interests are, we might have a chance of beginning to shape the environment so that the North Koreans understand that that they're headed in the wrong direction. And once we do that we will begin to open up the potential for a resolution of their nuclear weapons program.

So with that I'm going to stop.

MR. BUSH: Thank you very much, Jack, for laying the foundation in that clear and very comprehensive way. We now turn to Jonathan for the U.S.-China piece.

MR. J. POLLACK: Thank you, Richard. And my appreciation to you and to Ken for the invitation to be here today. Obviously, these are my own views. I am an employee of the United States Government, but fortunately I can get to express my own opinions.

Jack has tried to set the larger context of some of the questions related to the North Korean nuclear issue, if we may call it that, and there's no need for me to go over that same ground. My focus will be much more on Chinese policy calculations towards North Korea and how in turn these could advance or inhibit U.S.-China collaboration intended to constrain and ultimately reverse North Korea's continued nuclear weapons development.

Now, I've been asked to place this in a global context. This is part of the new agenda in U.S.-China relations. And that is so. However, I think one of the challenges is that it has a global dimension and it has, dare I say, a local and an historical dimension, especially for the Chinese. We, of course, are meeting in the immediate aftermath of Kim Jong-il's visit to China. This was his -- oh, now I realize I'm picking up the mic. Sorry. This was his fifth visit since 2000. Of course, it was his first visit to China since North Korea conducted its initial nuclear test in October 2006, but his visit now coincides with a number of urgent issues, ones that remind us that it is more than the question of North Korean nuclear issue. It is the very question of North Korea itself -- where it proceeds as a political and military system, what the dangers and risks are of this really quite extraordinary and very, very self-referential polity.

All of this again occurs in the aftermath of the Cheonan --

ongoing Cheonan investigation. We will await word, determinative findings on that. But we have, as well, Kim Jong-il's own very uncertain health, the leadership succession, the acute economic needs of this very, very troubled society and system, and not least, its determined pursuit of a nuclear weapons capability. Ones that have been reinforced, not undermined by its recent statements, most fully in a statement of the 21st of April where, if I could quote North Korea lest you were wondering, the North Korean statement, Ministry of Foreign Affairs says that the nuclear tests going back to October '06 by this, the state of nuclear imbalance in Northeast Asia where nuclear weapons and nuclear umbrellas were packed and where only the DPRK remained as a nuclear vacuum zone was brought to an end. But the deterrence effect provided by the Republic's possession of nuclear weapons, the danger of the outbreak of war, has noticeably been reduced. This is precisely the effort made on the current stage to remove the nuclear threat, not through pleas only in words, but by deterring the United States' nuclear weapons with our nuclear weapons.

There are other cheery messages in this statement which I commend to your attention because this is where we find ourselves at the present time.

China, I suspect, looks at this question in a much longer, historical context. Its history with the regime over the decades; the fact that

it, of course, was -- that China helped quite frankly save, rescue the North Koreans during the Korean War; that China has been a provider, a protector, a sustainer, not on a consistent basis to be sure, but over time very, very much in evidence. And so when Kim Jong-il meets with Hu Jintao and others, there are lots of ghosts in the room that take us back to the very earliest years of the DPRK.

That said, China enjoys an access and a reach into North Korea more than anyone else. They, at present, provide about three-quarters of the trade that North Korea undertakes. Senior Chinese officials are the only ones that have regular access if they so seek it in traveling to Pyongyang and China is the only country that Kim Jong-il has traveled to since about 2001, I believe.

So there's a lot of history here, but at the same time we have to look at the endlessly littered record of raised expectations, false starts, shattered hopes, and anticipated change in the North, both in its internal and its external policies, which have simply not materialized on any sustained basis.

Now, since the onset of the second nuclear crisis that Jack alluded to earlier, the view of the United States has been that China -- because of this access and because of its economic reach and because it is North Korea's immediate neighbor and still at least normally aligned through

an alliance treaty signed in 1961 -- that China has leverage and influence, if not outright control that can be utilized to constrain North Korea's nuclear conduct and ambitions.

Again, it's compared to whom or compared to what. But as I look at China's views on this question, there's a set of arguments that are often utilized that explain all the reasons why China will not bring its influence to bear as fully as it presumably could at least in theory, uneased about what the Chinese like to call peace and stability on the peninsula, the fear that somehow if China pressures North Korea too much it will have all kinds of unpredictable consequences, fears that there could still be a major contingency that could involve the United States -- draw the United States and China back into a potential confrontation or outright conflict on the peninsula. Fears that if North Korea really is approaching a very uncertain future, that if there were Korean unification, that this would find a unified Korea more aligned with the United States and therefore antagonistic to Chinese interests.

So if you add all of these issues up, and if you add to this as well China's and Hu Jintao's great personal investment if you will, in the six-party process, you come to a default option, which is to help sustain the North Korean regime, keep Korea divided, in some sense make, you know, maintain the status quo. But doing this in a position where China has

relations of a significant sort with both of the Koreas.

Now, we could ask does this suggest a basis on which over time will get us to the outcome that presumably we wish to see. It's hard to know obviously. I sometimes wonder frankly whether in the Chinese calculus leaders in Beijing may know things that we're just not cleared for in some sense. Indeed, the best case, of course, that is being argued by China, is that over time there must inevitably be internal change in the North and that therefore, China has incentives to play for time which over, in some longer term sense, will lead to a more normal North Korea that does not see its security depending on the possession of nuclear weapons.

Now, I understand the logic of that argument. I've had many, many discussions with Chinese about that. Of course, it's an old argument. Indeed, you can find traces of this going back at least since the early 1980s. Early in the Reagan Administration, Deng Xiaoping made some initiatives on behalf of the North Koreans to establish a trilateral context for negotiations. Deng was, frankly, carrying some of North Korea's water. This was discussed with Defense Secretary Weinberger when he visited Beijing in September of 1983, which was followed within a matter of weeks by the bombing in Burma. So it tended to bring this more hopeful expectation to an end. And that story has been repeated in one version or another many, many times.

So, you know, I don't want to dwell on this history too much, but it does suggest to me that history and geography and this very unsatisfactory circumstances on the nuclear issue on the standings between the United States and China continue to limit some of the possibilities for more meaningful movement, at least in the near- to mid-term in pursuit of shared goals. There is to be sure significant debate in China. It comes and goes. It is -- certainly, the atmosphere in which very sharp views of North Korea could be expressed tends to be a function in part of North Korean behavior. So in the immediate aftermath of both of the nuclear tests, the political environment in Beijing is much more conducive to openly expressed anger and frustration at the North, but with China ultimately reverting more to a kind of a policy mean, if you will.

This has been evident. For example, we saw significant cooperation between the United States and China in the aftermath of the second nuclear test, but then we saw last year, months later in the aftermath of the test as North Korea sought to make some of these more flexible gestures that Jack alluded to -- Wen Jiabao -- Prime Minister Wen Jiabao and then Liang Guanglie, the Minister of Defense, both traveled to the North. And even as the Chinese emphasized that they were holding, you know, adhering to the spirit of the U.N. sanctions, it would appear to many that North Korea -- that China had decided to make, if not a fundamental

commitment to North Korea, at least a deeper commitment focused very, very much on economics. But more broadly, keeping things in check. And begging the issue of whether the United States and China were really on parallel paths because the aftermath of the second test is that the Obama Administration emphasized repeatedly and continues to emphasize today that we were at a critical inflexion point on the question of nuclear proliferation and that we could not tolerate a situation to simply acquiesce to North Korean actions. And we certainly did not want to compensate North Korea for its actions. The question, therefore, becomes does Chinese support for North Korea in effect give them the support that it is necessary -- that they require in order to dodge, if you will, the pressure that could otherwise be put against them.

Now, bottom line it seems to me, the Chinese leadership, as distinct from Chinese analysts and scholars, has yet to be fully persuaded that nonproliferation compared to some of China's other competing interests, calculations, and needs, trumps these other concerns. It will -- China will do what is necessary to uphold the letter and perhaps the spirit of 1847, but Beijing has yet to demonstrate despite its declared pronouncements and its presumed disaffection from North Korean behavior that it is prepared to put this wider array of its interests at risk. This leaves us in a situation where although there are areas of cooperation between the United States and

China with respect to this issue, there are also areas that seem to me to be somewhat contentious and problematic.

So what do we do about it? The administration, including Jim Steinberg, our speaker, has emphasized at various times that the United States needs to offer strategic reassurance to Beijing. And perhaps we want the same from China. I think beyond that there's the question of whether we can get to strategic clarification. Are we working from a comparable set of policy assumptions and priorities? How compelling a mutual interest is there in the goal of non-proliferation? Or as I said before, does Beijing's larger set of interests as North Korea's immediate neighbor, tend to trump meaningful coordination?

So are there means by which we can move to a more complimentary discussion because absent that kind of more complimentary framework, North Korea may find itself with some increased room for maneuver. What we should be asking Beijing about is to reinforce whether there are or ought to be demonstrable shared national interests that underscore the risks to both countries opposed by North Korea's nuclear weapons development. We worry -- frankly, I worry -- that there is a tendency to give North Korea too much of a pass. Jack has alluded to some of this because their fissile material, among other things, are totally unconstrained, subject only to their technical and economic and industrial

limitations.

The potential costs, however, including for China in terms of regional stability, seems to me are quite self-evident. More than this, it has the potential to have a longer term undermining affect in U.S.-China relations, not to mention on China's relations with the ROK. More than this, it creates a very unhealthy precedent over the long term for the nonproliferation regime.

Jack asked before whether the United States had a true redline. We might want to ask the same thing of China. China's words are appropriate here. They say that it wants to work actively for the denuclearization of the Korean peninsula. That's all well and good. But there is a larger strategic context here and a set of actions that may be needed to advance that that we need to impart more clearly to the Chinese and, of course, we should entertain their own ideas to some extent on how to proceed.

So I see China, like the United States, confronting some unpleasant policy choices. On the one hand we could say that China could in one context make some kind of a commitment that it will protect and defend North Korea. That I don't think China seeks today, but it is trying to preserve and provide and sustain for North Korea heightened political and economic support that seems at first blush to be independent of North

Korean behavior. Alternatively, we might want to see China move more towards an active prodding of North Korea and even some would argue to a degree to which it might distance itself from North Korea, though I do not see that forthcoming anytime soon.

So I believe we do have a set of overlapping interests that are self-evident. But getting from here to there and finding the effective means and the kind of confident understanding between the United States and China continues to elude us and remains, I think, uppermost on the agenda that both Beijing and Washington need to confront.

Thank you.

MR. BUSH: Thank you very much, Jonathan. (Applause) I'll join the applause.

Let's now shift the geographic focus to the Persian Gulf, and we start with Ken Pollack. And you can stay here or go up to the podium. Whatever you --

MR. KEN POLLACK: Thank you very much, Richard. Thank you, Ken for inviting me up here. Thank you to all of you.

I'm going to give my talk backwards today. What I mean by that is not literally I'm going to speak backwards, although that would be a feat. And yeah, if someday I can pull that off, you'll all be invited.

What I mean by that is that I was taught that you should start

with your interests and then the threats to those interests, and then you lay out different policy options for addressing the threats to secure the interests, and then you pick out the best policy option and you make a recommendation. I'm actually going to start in reverse order. I'm going to lay out the options and to talk about which ones are the best, and then I'm going to come back to the threats and the interests. And I'm going to do that because unfortunately, what I think you will recognize when I start talking about the options is that when you're talking about Iran, the options all stink. Okay? I will say that very bluntly right up front. There are no good options on Iran. The only things that we are arguing about these days is which one is worst and which one is least bad. Okay?

And the problem is, of course, that when you deal with a whole bunch of really bad options, there is a tendency to push the thinker and the arguer toward inertia. You want to just throw up your hands and walk away from the table altogether and maybe focus on another problem easier to solve like North Korea. (Laughter)

And, of course, that's not a very good option when you're talking about Iran. And the reason it's not a good option is because of the potential downsides, the potential threats to our interests. And so that's why I think it's useful to actually start with the options and which one is probably the best of those or the least bad of those options. And then to think a little

bit about what the threats are that we face which can be seen then as potential repercussions, as consequences of what inaction would mean on Iran.

So I'll start with the options. At some level I think it's pretty well known to this group what the preferred option of the United States is, which is a process of increasingly harsh sanctions on Iran to try to put pressure on the Iranian regime. Now, I will tell you that this is not a policy that the U.S. Government or the U.S. establishment came to quickly or easily. It was the product of a long process of debate, deliberation, and also most importantly, of trial and error with the Iranians, and quite frankly with our other allies around the world.

Over the course of the 31 years of the existence of the Islamic Republic of Iran, we've tried a lot of different policies to get the Iranians to do what we'd like them to do. We have tried everything from unilateral concessions to undeclared warfare, and none of them have worked. Okay? And today when we look at Iran and what it is that we and the rest of the world are so concerned about, we are placing our hope in the idea that harsh international sanctions can succeed because quite frankly nothing else has so far.

And there's no question that this, too, is going to be very much a long shot. The Iranian regime has resisted other sanctions in the past.

They have not resisted the kind of international sanctions that the United States and its allies are pushing for, but it has resisted sanctions. And it has resisted sanctions for a long time.

What's more, we've had a very important change in the nature of the Iranian regime in its composition just over the course of the past year. On June 12, 2009, about a year ago, Iran held its presidential elections. And as I think many of you are aware, there were a lot of Iranians who were unhappy with the course of those elections. They believe that the elections were stolen from them, that they were rigged by the government, and that the man who was supposed to lose -- President Mahmoud Ahmadinejad -- won. And he won unfairly.

Now, I can't tell you whether he did or not. I think there's a lot of evidence to show that the elections were rigged. Whether or not they were rigged enough to make him the winner as opposed to something else, who knows? It may, in fact, be true that the elections were rigged and he did win. We don't know. All that matters, though, is that after those elections there was a widespread revolt by a large segment of the Iranian people. That revolt was the single greatest threat to the Iranian regime in its 31 years of existence. And in response to that popular uprising, a very important event happened within the Iranian leadership. It contracted within itself. Large segments of the Iranian leadership -- those groups that we tend to call

moderates, pragmatists, even some of the mainstream conservatives, and certainly all of the reformists -- all of those groups recommended making concessions to the opposition.

Hardliners all said no. No concessions whatsoever. And of greatest importance, the Supreme Leader sided with the hardliners. His reading of his own coming to power, of the taking of power of the Islamic Republic, of the revolution that overthrew the shah was that what doomed the shah was his making concessions. That the moment he started making compromises, he opened Pandora's Box, and, therefore, there would be no concessions. And in doing so, the leader also very systematically went about excluding all of those voices of moderation that had been very important, prominent voices in his regime, excluding them from Iran's decision-making process.

So today what we've seen is a very significant narrowing of the base of the decision-making apparatus of the Islamic Republic, such that, quite frankly, what we have in charge now is the hardest line group of people we have seen in Iran since 1981. And frankly, they're not interested or concerned by sanctions. They want the nuclear program. In many cases, they want nuclear weapons. They want enmity with the United States. They believe that the United States and the West are their enemy. Some for ideological reasons, some for power political reasons, but it is consistent

across the board. They all believe that Iran is more important to the rest of the world than the rest of the world is to Iran. None of them believe that sanctions will have enough of an impact to make them change their minds. And, in fact, many of them even believe that sanctions will be good for Iran because it will encourage greater autarchy.

Now, all of this, of course, or at least much of it, is nonsense. And I have no doubt that at some point in time it will be proven wrong. The problem is that some point in time. It could take a long time for these guys to figure out that they're wrong.

And it's worth keeping in mind that in the 1990s, the international community embarked on a similar program with Libya. We imposed sanctions on Libya, comprehensive sanctions on Libya. And the Libyan response was, ha, we will never give into your sanctions. We can outlast your sanctions. Now, they were proven wrong. Not surprisingly, Muammar al-Gaddafi being proven wrong. Who could think of that? They were proven wrong, but it took 8 to 10 years for them to be proven wrong, for them to realize it. And let's remember that Iran is a much bigger, richer, more powerful country than Libya is, so it could take a very long time.

But we tend to focus on the sanctions because quite honestly all of the other options are much, much worse. First, there is engagement, which to its great credit the Obama Administration tried very hard to

implement during its first 10 months in office. Long after outside observers, myself included, were saying to them, guys, it was great that you tried engagement, but you've got to realize it's done because this Iranian regime isn't interested in engaging, they clung to engagement. They wanted to believe that they could come to a deal with the Iranians; that they could find a way through peaceful negotiations to resolve their differences with the Iranians. And unfortunately, by the fall of last year they finally figured out that it just wasn't going to work; that the Iranians just weren't interested in doing so.

And they came to that honestly at a time after many other countries -- I would say most other countries around the world recognized this. And it's probably true that the Chinese took still longer, but I think that even Beijing has recognized that Iran right now is just not interested. And in fact, we saw a very senior Chinese delegation go to Beijing in the last couple -- sorry, go to Tehran in the last couple of months and try to convince the Iranians that the world meant business -- that they really needed to come around -- and they were badly disappointed by the obnoxiousness of their Iranian interlocutors and the unwillingness of the Iranians to countenance any kind of negotiations over their nuclear program.

So engagement is highly unlikely to work, at least for some period of time. We can all hold out hope that over time the Iranians will

mellow. They will recognize that they are actually in too deep and that these sanctions are causing them problems and their isolation is bad for them. And we can hope that at some point in time engagement will be a realistic proposition again, but it simply isn't today.

At the other end of the spectrum there are certainly people in the United States pushing different options. And I suspect that you're going to hear those voices louder and louder in coming months. There's a group out there who wants to bomb Iran. Now, I'm a old military analyst, and I think some of you at least in this audience know, I'm not exactly a shrinking violet when it comes to the use of force. If I thought that there were a good military option available, I would be very glad to lay it out and to explain under what conditions it would be good to do so. But for the life of me I cannot come up with a good scenario for the use of force.

There's a lot of evidence back there. I'm glad to go into more detail if you want, but I'll simply say for the sake of this summary it's highly unlikely that it would stop an Iranian nuclear program. It might set it back. The best estimates are that even comprehensive massive military strikes by the United States would probably only set back the Iranian program by a year or two. And, of course, it would create the perfect opportunity for Iran to withdraw from the NPT, to bury all of its nuclear programs much deeper, to embark on a massive program with the support of its own people. It

would, in fact, likely rally the Iranian people, so many of whom are disaffected with their government, around the regime, cementing in place this hard-line Iranian government. And what's more, the Iranians would doubtless retaliate and they would retaliate in a whole variety of venues that would be very painful to the United States.

And it's true that Iran is much weaker than we are, and it's true that Iran probably can't do unacceptable damage, but the fact of the matter is the Iranians could do a lot of damage in the Middle East. And the Middle East is not a region that needs more damage, certainly not to American interests and to Western interests there.

The other option that's out there being proposed by those on the right is what's called regime change. What's meant by that is to try to help the Iranian opposition overthrow the Iranian regime. This is a wonderful idea in theory and I think that it is something that the United States needs to look hard at because the simple fact is that as I've just mentioned, for the first time we now do have a large, legitimate, popular opposition to the government. And the United States ought to look at ways that we might be able to help that opposition. And I suspect that other countries will be doing so as well.

But the truth of the matter is that this regime has demonstrated that it will not go gently into that good night. And if our scholars have taught

us anything about revolutions -- and they have only taught us one thing about revolutions, but it's a very, very important thing -- it is that revolutions occur only when a regime loses the will or the capacity to use violence. And unfortunately, this regime has lost neither the will nor the capacity to use violence. And it is unlikely to do so anytime soon. And so we can hold out the hope that someday there will be regime change in Tehran, and I suspect there will be, but I don't think it's going to come anytime soon. And certainly, not in time to head off our problems with Iran over its nuclear program. So if you don't like the harsh sanctions option, the alternatives are much worse.

But, like I said, I hope you don't throw up your hands and simply say this is too hard. We ought to walk away. We can't come to a meeting of the minds on this. That's not a good answer either because then you have to consider the consequences, which brings me to the threats and the interests.

I'm not going to go into too much detail. There's obviously a lot more that could be said, but there are two broad sets of problems that the United States, its allies, and China all will face if Iran is not convinced to give up its nuclear program. The first is the Iranian threat to the Middle East. Now, some repair work needs to be done here. You hear a lot of people screaming from the tops of their lungs about how Iran's acquisition of a nuclear capability will mean that the entire world will explode the next day.

Okay, that's a bit inaccurate. Iran is ruled by a group of people who are aggressive. They're anti-American. They're anti-status quo. They are murderous. They are all of those things, but they are not irrational. And what we've seen from them is that they do recognize deterrence. That they are subject to the force of deterrence. They understand it. They comply with its various strictures.

And what that suggests is that it's highly unlikely that the Iranians would get a nuclear weapon and simply lob it at Tel Aviv or the Saudi oil fields or something else that we care about. I would also suggest that it's highly unlikely that the Iranians would give a nuclear weapon to terrorists, but that's another threat that you hear frequently. The Iranians have had weapons of mass destruction for about 22 years. They've supported terrorist groups for 31 years. And they've never seen fit to mix those two things. And they've had very, very good reasons not to do so.

But that doesn't mean that there isn't a threat to the stability of the Middle East from Iran's acquisition of a nuclear capability. There is. Okay? First, there is the potential for Israel to go to war with Iran. Again, I think that actually unlikely and I'm glad to talk about it in Q&A if you'd like me to do so, but for the sake of this audience I think it's simple enough to say that I actually think that that's an overblown fear, although it's not an irrelevant one. There is a possibility out there and it shouldn't be dismissed.

The bigger problem, of course, is that Iran is, as I've already mentioned, an anti-status quo power. A power that sees the current status quo in the region as being one inherently to its disadvantage. And one which seeks constantly and with all means at its disposal to overturn the regional status quo. What that means is that Iran sees instability. And whenever it sees instability, it does whatever it can to stoke it. It arms violent groups where it can find them. It backs terrorists of all stripe, not just Shiite. It backs secular groups. It backs Sunni groups. It'll back Christian or Jewish groups if actually could figure out a way to do so. Okay. They are nondenominational. They are entirely ecumenical. Anyone who is looking to overturn the status quo, preferably by violence, typically can find some help from the Iranians.

And as I've said before, the Middle East doesn't need any more help on that issue. It has plenty of instability. And when we think about American and Chinese mutual interests in the Middle East, the interest of stability and ensuring a free flow of inexpensive oil is at the very top of that list. It's at the top of that list and everything else is a distant second. And what we've seen from Iran is that Iranian actions have been among those most threatening to those interests over the last 31 years. And there is a great fear that an Iran with nuclear weapons, an Iran with a nuclear capability of any kind, an Iran which believes that it is no longer

vulnerable to an American conventional or military retaliation will feel greatly emboldened. That it will embark on far more aggressive actions. That it will stoke violence everywhere. Not just in Lebanon and Palestine where it loves doing so, but in Iraq, in Saudi Arabia, in Bahrain, potentially in the UAE, and in a whole variety of other countries.

Let's not forget that the Iranians over 31 years have tried to overthrow the governments of virtually every one of those countries I've mentioned except the UAE, and you can also add actually Egypt to the list of governments that it has tried to overthrow. So this is not an idle fear. It is a very real one and it is a very significant one over the long term.

The last interest, the last threat that I'll mention, is of course the wider one of nonproliferation. Right now for a lot of countries around the world, nonproliferation has a very mixed record. There are countries out there that the international community has punished very severely for its pursuit of a nuclear capability in contravention of international public opinion. I'd put in that category Libya, obviously; Iraq, in its own way; and even North Korea. It's true that North Korea acquired the capability, but North Korea paid a price that no other country on Earth would be willing to pay. And in that way it actually did help reinforce the nonproliferation norm.

But set against those three good cases are three bad cases -- Israel, India, Pakistan -- all of whom acquired nuclear weapons. Not

necessarily scot-free, but at a price that many other countries probably would consider acceptable. And Iran is out there as the rubber match. Iran will be the decider. And Iran is important because the entire world, including all five members -- all five permanent members of the U.N. Security Council have stated clearly, unequivocally, and repeatedly that Iran cannot be allowed to acquire this capability. And we now have four resolutions in the United Nations Security Council under Chapter 7 of the U.N. Charter, which makes them binding on all members, stipulating that Iran cannot be allowed to have this capability.

And if Iran acquires it nonetheless, and if it's seen as not paying too high a price for having done so, which again is one of the reasons that the Obama Administration -- why the United States and its allies have embraced the idea of imposing harsh sanctions on Iran to at least demonstrate to other countries that there is a real price to be paid for this kind of proliferation. If Iran is allowed to acquire it anyway, it is highly likely that you will see the nonproliferation norm begin to erode, if not collapse entirely.

Within the Middle East, I think that it is highly, highly likely that Saudi Arabia and the UAE will acquire nuclear capabilities of their own. They're already embarked on civilian nuclear programs, which are intended for a variety of purposes, but wink-wink, nudge-nudge, they're making it very

clear to Iran that this is meant to match their capability if the Iranians do not cease and desist. And in private, Saudi officials have told American officials and American former officials that if Iran acquires a nuclear weapon, they will acquire one, too. And they are fully capable and willing to do so.

Beyond that people talk about Turkey, about Egypt, about other countries in the region. I'm less convinced about them. I can give reasons for why that's the case if you want me to do so. But I think that it is clear that you will see other states in the Middle East following suit. And beyond that, of course, if Iran can get nuclear weapons, a country that everyone else in the world realizes is a tremendous threat to international peace and stability and economic prosperity, why should other countries stop? Do Brazil and Argentina really think that the world will treat them worse than it treated Iran? Would Taiwan or South Korean or Japan, for that matter, believe that it would be treated worse by the rest of the world? And if some of these countries start down that path, where does it end?

This is exactly the kind of Pandora's Box that quite frankly the United States of America doesn't really want to know the answer to. They'd be much better to simply keep the box closed. And keeping the box closed means keeping this capability out of Iran's hands.

Thank you. (Applause)

MR. BUSH: Thank you very much, Ken. That was terrific.

Finally, we turn to John Garver. If you want to go up to the podium --

MR. GARVER: No. I'll just stay there. That's fine.

SPEAKER: You can move it a little closer.

MR. GARVER: Ladies and gentlemen, good afternoon.

I'm honored to be here. Let me begin by thanking Richard Bush and Ken Lieberthal for the invitation.

I will talk about Chinese policy, not U.S. policy. And I propose to address the question that Richard asked us to address about the geometry of the interests of the two countries or the extent to which Chinese and U.S. interests overlap regarding the Iran nuclear issue.

China, of course, supports the nonproliferation treaty regime, the NPT regime. That, of course, was the logic underlying China's signature of the regime -- of the treaty -- in 1993. And the logic is easy to understand. As one of five permanent members of the -- one of the five nuclear weapon states under the NPT regime, China's interest is in having fewer, rather than more states with nuclear weapons. And also by having fewer nuclear weapon states, China's relative military capabilities as capabilities vis-à-vis other countries are also enhanced. Same logic as the United States.

So the first cut is that we have converging interests. But when you look at it a little bit closer, actually, China's interest in nonproliferation in

ways. First of all, China does not have any allies in the Middle East. And I'm setting aside Pakistan, saying Pakistan is a quasi-ally, not in the Middle East. South Asia, maybe, but not Middle East. But other than Pakistan to the West, there's no -- China doesn't have any allies. The United States has a whole lot of them. Saudi Arabia, Kuwait, Israel, Bahrain, Qatar, Egypt, so on and so forth. Probably the United States has a dozen or so allies in the region.

Second, the People's Republic of China doesn't have any military forces in the region, which might be targeted by Iranian nuclear weapons. The United States, of course, has a lot of military forces in the region. China has not assumed responsibility for the safe passage of oil through the Straits of Hormuz at stable and reasonable prices. The United States, since the Carter Doctrine of 1979, has assumed exactly that responsibility.

China -- another discrepancy is that China has had very cordial relations with Iran, both under the shah and under the Islamic Republic. Now, in the first couple of years of the IRI, there was a period of turbulence, but by 1982, China had succeeded in rebuilding its relations with the IRI and relations have been very cordial, even to the extent that I'd suggest to you that China is probably Iran's major strategic, political partner in these debates we're talking about.

So, the United States has a lot of problems with these countries: with Iraq, with Iran, not China. China -- another cut-- China, unlike the United States, has never contemplated war with these countries. The United States has. We had two wars with Iraq and, you know, the tanker war with Iran in the 1970s. And now we're debating will there be another one. So the United States continually confronts this question of war or peace with these countries that, you know, we think have nuclear programs. China, no. China has had fine, cordial relations with Iran and Iraq. So second cut is that although we share a broad interest in nonproliferation, on closer inspection there's a series of very significant, divergent interests regarding the importance of nonproliferation in the Middle East.

So why is China so unenthusiastic about the U.S. push for biting sanctions? For tough sanctions? Well, this isn't new. China has opposed U.S. sanctions since 1970 -- 1980, when Iran seized American diplomats and held them hostage. And the U.S. Administration and then the Carter Administration responded with sanctions. China said we thought this was a bad -- they thought it was a bad idea. On the one hand, China opposed the violation of diplomatic privileges involved in the seizure of the hostages. On the other hand, it condemned American's resort to sanctions. And even more, condemned the attempted U.S. military rescue of the

hostages in 1979. So this is an old song.

Now, of course, China has thus far supported three sets of Security Council sanctions against China in 2006, 2007, and 2008. And my hunch is at the end of the day China will again sign onto another set of sanctions -- of Security Council sanctions. But, you know, to characterize China's policy towards this, I would say that China has delayed the process and sought to limit the scope of the sanctions so that those sanctions would not really interfere with the substance of China's economic or political relations with Iran. You know, maybe to delay and water down to use simple terms, the sanctions.

And if you look at, you know, China's statements at the IAEA Board of Governors or the Security Council debates or foreign ministry statements, you find a lot of Chinese objections to U.S. pushes in this direction. Not only the current round, but going back again to -- actually, to 2003 when the new stage of the Iranian nuclear issue came before.

And, you know, China would say that they're standing on principles. And China has a number of principles that it feels are being involved in this issue. For example, the principles of -- insisting that this question be solved by dialogue and negotiation. That any use of military force or threatened military force would make the situation more complex, would be antithetical to a resolution, and that all reference to the use of

force, the possibility of use of force, should be ruled out, and all parties should undertake to resolve this purely by negotiation and dialogue.

Or that sanctions -- the resort to sanctions make the matter more complex and more difficult, make resolution more difficult, and doesn't move the situation forward, but instead, moving it back. And another level of this same objection is that the United States is far too willing to resort to sanctions and presumes to bully countries around the world, especially developing countries, and through the frequent resort to sanctions. And that this really isn't a good way to run the world. And the United States should get over this gunboat diplomacy or bullying.

Interference in the internal affairs of other countries is another principle that China stands on. And a lot of Chinese, the things that Dr. Pollack just mentioned, you know, Chinese think that -- a lot of Chinese analysts that I've talked to think that -- and people that write the articles and journals I read -- suspect that the real U.S. objective is regime change in Iran and even if that's not, this is -- regime change is not one factor, then U.S. interference in the internal affairs of Iran, revulsion at the internal affairs of Iran, is one factor feeding into the current U.S. drive for sanctions. Then again, this is an unprincipled stand by the United States.

So, principles. Well, a couple of observations about China's stance on principle. It's protection of principle. Its use of principles to

oppose U.S. policy. First observation is that China's stance on principle is a way of protecting China's relations -- its economic and political relations with Iran. China receives about 12 percent of its imported oil from Iran. Iran has a lot of very rich copper deposits, undeveloped copper deposits box site. The biggest slice of China's imports, like 80-some percent of China's imports are from Iran -- are crude oil. And about another 12 percent are mineral deposits -- mineral ores. So China needs those; Iran has a lot of them.

Iran also is a big market for Chinese exports, capital goods. Prior to the Revolution -- in 1978, the year before the Iranian Revolution, China's trade with Iran accounted for about one percent of Iran's foreign trade. Iran's big trading partners were the U.K., the United States, European countries, and so forth. Those countries have by and large left Iran. And in 2009, China became Iran's major trading partner. Iran is a big and important market. They have a lot of money. They have very ambitious development objectives.

Now, Iranian engineers and managers would often prefer German equipment or French equipment, you know, because of the technological capabilities of it. And they really don't like Chinese stuff because it's not as good. It's not as reliable. It's cheap, but those factors are set aside by Western sanctions. So, in effect, Western sanctions, U.S. sanctions, have opened the door and allowed China to shoehorn itself into a

very lucrative and big and important market. Export promotion is the modus operandi of China's development. It needs export markets, and Iran is a big export market.

So, the first cut on China's stance in defense of principles is that I think that that stance in defense of principles serves China's interest in developing friendly, cooperative relations between the peoples of the two countries in accordance with the five principles of peaceful coexistence.

A second observation about the role of principles in Chinese foreign policy is that I think principles serve interests. And a question before Chinese leaders is when they decide to stand firm on China's principles or to be flexible in the application of those principles is whether firm defensive principles or flexibility of principles serves China's interests. And, in fact, flexibility on China's -- on these principles and the application of these principles, in other words, going along to some degree with American wishes for sanctions serves China's interests.

So what Chinese interests would be served by flexibility on these principles? Well, the main Chinese interest that is served, I think, is protecting the favorable macro climate for China's development drive which began in 1978 when the new paramount leader, Deng Xiaoping posited China's becoming rich and strong through participation in the global capitalist system, which for better or worse was dominated by the United

States. And China has hued to a core since then of basically trying desperately to remain amicable relations with the United States for the sake of maintaining a favorable macro climate for China's long term development drive to make it a rich and strong country.

The problem is, from the Chinese view, is the Middle East is the locus of American drive for world hegemony, for world domination. During the Cold War, the Middle East was a center of contention between the super powers with both of the two super powers contending with one another to control the oil of the Middle East because we live in an era of internal combustion engines and we need gasoline. And there you go. So the two superpowers sought to control the Middle East during the Cold War to achieve their goals of world hegemony. But the disappearance of the Soviet Union has created a very unbalanced situation in the global situation, and the crux to that is the Middle East.

And in this unbalanced situation, the United States has seized the opportunity to push forward aggressively with the drive to bring the oil of the Middle East under American control so that the Americans will have their hand on the oil spigot of the Middle East and say you can have some and you can't have some. And the countries around the world that depend on that oil will need to kowtow to the Americans: the Japanese, the South Koreans, the Indians. Oh, yes. China. Right?

The unbalanced situation in the Middle East released the United States to wage the first hegemonious war against Iraq in 1991. China's analysis is basically that's -- both sides are hegemonious. A big hegemonist and a little hegemonist. And, you know, the big hegemonist won, but they're both hegemonists. And then the 2003 war and so forth. Some analysts in Beijing, based on interviews and articles that I've read, suspect that in the American heart of hearts, in the secret blueprint in some office over here in Washington is that, you know, Iran is next on the agenda to bring the oil in the Middle East under control.

But the problem is from China's perspective, you've got to have good relations with the Americans and the Middle East is the center of the American drive for hegemony. So, the Americans are doing a lot of bad things in the Middle East, but at least that's a region of the world which is pretty far from China's strategic interests -- core strategic interests, which are in the Western Pacific and Southeast Asia. So the Americans are doing a lot of bad things and might be hegemonious run amuck, but at least they're not doing it in an area of crucial concern to China. Oh, and by the way, the Americans just might exhaust themselves and wear out their national will and treasure in this region of the world leaving us in a better situation.

So what this takes us back to, I think, is again, flexibility on the application of principle. But, of course, if China is going to be flexible on the

application of its principle, for example, opposition to the use of sanctions and interference in internal affairs, if it's going -- if China is going to go along with the Americans, it needs to get a quid pro quo. Now, Mr. Steinberg this morning said that China doesn't really seek a quid pro quo and that might be the situation now, but I've looked at China's interactions with the United States in earlier periods. For example, in 1990, during the run up to the first Iran -- Iraq war. Or during the 1997 when the United States pushed for Chinese disengagement from nuclear cooperation with Iran. And in both of those junctures China sought and received from the United States a quid pro quo. So, China could be flexible, but will, I suspect, need some type of, again, satisfaction from the United States in terms of giving something on the interest of concern to China.

There are several other areas in which China's interests would -- are not convergent with American interests in the Middle East. Or let me even go a little bit more further and be provocative perhaps and say that there are other ways in which Chinese interests might actually be served by the failure of American interests -- American policies towards Iran. China's objective is multi-polarity. Long-term objective, there's been an ongoing debate in China whether this should be what stress should be given on this. But the broad idea is that China should seek to move the world in the direction of multi-polarity. The relative reduction of the U.S. position of the

world. And the failure of U.S. -- this policy directive I think would substantially diminish American prestige and influence of the world and put China in a better position.

China also -- in terms of China's energy security, China would receive certain advantages from a nuclear Iran. Again, to put maybe too blunt of a point on it, China is -- one of China's fundamental problems in energy security, of course, is the sea lines of communication. The movement of oil across the Indian Ocean, right below India's Navy and so on and so forth. China's solution to the slack problem, of course, is over land pipelines through Kazakhstan or through Pakistan or through Myanmar. But the problem -- one of the problems of the pipeline solution is input.

Where is China in the event of some type of U.S.-China conflict or confrontation over Taiwan? Where would China find some country that was willing to anger the United States by putting oil into those pipelines to pump to China? Probably not -- well, probably not Pakistan. Not Myanmar. But Iran would be probably the best bet. And a nuclear-armed Iran would be more -- perhaps more willing and confident to do that.

Okay. But, hey, don't the United States and China have a fundamental convergent interest in guaranteeing the safe, uninterrupted supply of oil from the Persian Gulf at stable and moderate prices? We hear that argument again and again. To my mind that is basically an American

argument that we pitched to the Chinese. And my sense is the Chinese haven't really bought that argument. A couple of years ago, someone -- a colleague here in Washington and I spent a couple of weeks in Beijing going around, knocking at different think tanks and talking to Chinese analysts and talking to retired Chinese diplomats and people like this, and we deliberately pitched that argument to the people we met. With the exceptions of a couple of professors, we didn't get any biters. We didn't get any takers. The basic response was basically what you Americans want is for we Chinese to be junior partners in hegemonism. You want us to be junior partners to American hegemonism. And we're not interested in that. We're not interested in that. And again, that was pretty much the response across the board, except for a couple of professors.

Now, there may be people in the Chinese diplomatic apparatus who don't agree with that line, but my sense is that they are not very influential yet. They may become influential, and I hope they do, but my sense is they're not influential yet.

So, bottom line, I think the United States and China have a convergent interest in preventing Iran from acquiring nuclear weapons and nuclear weapon capabilities. But I think that the interest of the two countries in that regard are very asymmetrical. American interests are much heavier than Chinese interests, and there are very few American interests that would

be served by Iranian nuclear capabilities. Unfortunately, I don't think that's the case with China. I think in the case of China there are, in fact, several identifiable interests which would be served by a nuclear Iran.

So, those are my views on the situation, ladies and gentlemen.

Thank you. (Applause)

MR. BUSH: Thank you very much, John.

So we have two situations, different in some very profound ways, but in each the stakes are high. The options are poor. The convergence of U.S.-China interests is not as great as the administration would like us to believe. And so the degree of cooperation is not as great as one might hope.

So now we are going to open the floor for about a half an hour of questions. I had some mischievous ones for the panel, but I'll defer those because I'm sure there's a lot of interest here. We'll start with the gentleman right there.

MR. HARRIS: Thank you. Good afternoon.

MR. BUSH: Please identify yourself.

MR. HARRIS: Richard Harris from Momentum Private Equity in New York. And my question is for Mr. Pollack.

SPEAKER: Which one?

MR. HARRIS: The one on my left.

Mr. Pollack, it seems to me that the thesis of your talk could be that pretty much all hope of a negotiated settlement -- some sort of grand bargain with Iran is pretty much dissipated. And I'm wondering if in the Administration, is anyone laying the communicative and strategic groundwork to prepare the American people for the fact, not if Iran gets nuclear devices, but when.

MR. K. POLLACK: That's a great question. No, categorically not. Absolutely. I think it's a very big mistake. What's interesting is it's taken the Administration a lot of time even to go from preparing the American people to move from engagement to confrontation with Iran. It took them a very long time and Secretary Clinton has been almost alone in going out there and saying, you know, engagement has kind of run its course. You know, they actually have a very good argument that they make in private to people, including the Chinese, about how, look, engagement is not off the table. We prefer engagement. But engagement is now going to become a passive policy whereas we need to turn the active phase toward pressuring Iran. It's a very good line. They don't use it in public. Again, the Secretary has occasionally said it, but it's not a major element of what the administration is doing.

But I think you're absolutely right. Is that we have to be very realistic about the likelihood of all of this working and the likelihood that there

will be a nuclear Iran at some point in time. And the problem is, of course, that politically the President backed himself into a corner by saying that this would be unacceptable. And he said it during the campaign and you can understand why he said it during the campaign because all of his rivals were saying it. In fact, his rivals were saying even worse. So he, you know, that was in some ways the minimal position he felt that he could take. But, you know, he's not come away from that and, you know, he's had a few other things on his plate so I don't think that this has been a high priority for him, but I think it's a very real problem because I think that at some point in the next five years we're going to wake up and realize that the policy has probably failed and that we are dealing with a nuclear Iran.

That's what we're doing here at Brookings, is we're doing a lot of work on what dealing with a nuclear Iran is going to be all about. And it would be really helpful to us if the administration would go out there and get the American people ready for it so that they have -- so that when we put this stuff out there on the street they're ready to read it.

MR. BUSH: Scott Harold.

MR. HAROLD: Hello. Scott Harold from the RAND Corporation.

A question really for the panel as a whole. I want to put it in four words. Is China the problem? And then I want to unpack it a little bit

because from one perspective, looking at Premier Wen's visit to Pyongyang, Defense Minister Liang to Pyongyang, and the words that were said to the effect that China and North Korea have as close a relationship as they have ever had, the defense commitment still exists, \$10 billion in promised cooperation or some large amount of money -- Jonathan, I can grant you that that figure may not be accurate -- suggests that Beijing is not actively -- current policy is not actively causing North Korean to have to face any consequences for its actions. Similarly, Dr. Garver and Pollack, as you know I'm sure, Beijing after the uprisings in Tehran last year sent crowd control devices, political support, any number of activities that shield the Iranian regime from its own -- the effects of its own actions.

However, the other argument -- as Jack having dealt with North Korea I'm sure you know -- is that even China at its most determined - - if China were to adopt every policy that even the most hawkish American president were to ask of it, the North Koreans would not budge. The North Koreans are very difficult. And the North Koreans are very skeptical and suspicious of Beijing. And similarly, I suspect, the Iranians well known, as Ken you know, for resisting any pressure from outside, highly nationalistic, would not necessarily bend just because Beijing would ask them to do so.

So it seems to me a very interesting question. If you were to have a fully committed leadership in China that really wanted to try to bring

either of these two regimes "to heel," really put the screws to these regimes in the order -- in the quest for a non-proliferation policy victory, would that really succeed? And if the answer is no, should the U.S. back off? And if the answer is yes, then should the U.S. pursue some kind of a policy that makes these regimes -- whether it's Iran or North Korea -- more dependent on Beijing so that Beijing can no longer claim, as it has in the past, we don't have the leverage. In other words, should the U.S. pursue a variant of the 1950s strategy that we had towards the Soviet Union and China? Open up slightly to Moscow, put tons of pressure on Beijing, and pressure Beijing into becoming more dependent on Moscow so that it annoys the Muscovites, annoys the Soviets, and creates dissent in that relationship. And at the same time creates leverage that Beijing could then effectively at some point in the future -- as all of you have recognized this is a long term process -- be called upon to use by a future or current American Administration that could then compel Beijing to recognize that logic.

Thank you.

MR. BUSH: That's a good merged question.

I'm going to ask the panelists to give short answers. Start with Jack and move down the line.

MR. PRITCHARD: Thank you, Scott.

The answer is -- in my opinion, Beijing is not deliberately doing

this, but yes, it is by its actions extending the problem. I concur Wen Jiabao's October 5th visit of last year reversed what I described earlier as that moment in time when Pyongyang was thinking that it was on the wrong path. It needed to do something. It began a charm offensive. After the Wen visit, the North Koreans absolutely reversed course and it gave them a new lease on life. They didn't believe the sanctions would affect them. They understood that the lifeline that the Chinese were providing was substantial.

But I don't agree with -- the second part of that was if the Chinese adopted all the U.S. hard-line positions the North Koreans would not budge. I think the reverse is true. The problem is you are not going to get the Chinese to do that. I think Jonathan put it best by saying that until the Chinese own national security interests trump -- if proliferation issues trump all their other concerns, you know, then we'll be on the same page. That's not going to happen. So.

MR. J. POLLACK: A couple of quick comments.

First of all, this \$10 billion figure is a fraudulent number. I mean, the Chinese actually don't have that much at risk in a purely economic sense.

I would also contest that they have a real defense relationship anymore. I mean, part of what Wen was seeking to establish when he went there and Liang in a different way, was to, you know, make this -- in fact, this

has been a process over a longer period of time. In effect, to say to the North Koreans that we are not tethered to your strategy as such. It doesn't mean that they're going to hang the North Koreans out to dry, but I think the Chinese have been fairly explicit to the North Koreans going back actually also early as the mid-1980s for where there is a defense commitment under circumstances where North Korea was attacked, but certainly not beyond that.

I would agree with Jack that to some extent the new aid packages from China have given North Korea kind of a "get out of jail free" card to an extent. But again, coming back to what I said in my talk, is there something the Chinese think they know that we don't? And I guess the best-case scenario I could give you is that there is still a belief in significant quarters in China that over a longer period of time, particularly after Kim Jong-il is gone -- not to say that all of a sudden overnight you undergo some kind of a transition -- but that North Korea cannot indefinitely, you know, forever defy the laws of gravity political and economically.

Now, again, as you know, there have been lots of predictions over the years that the end is at hand. We go through waves of this. We're going through another cycle of this right now when this is a resilient, determined regime that really doesn't depend that much on the outside world. But if they depend on anyone, it is China. You know, again, I think

just both because China is the immediate neighbor, this does to some extent inhibit their options. But there is a kind of -- in some circles at least -- a kind of a quiet -- I don't call it confidence; that's way too strong -- a belief that over time this will not be sustainable. Indeed, as you know, there's lots of anxiety in some South Korean quarters that, my goodness, the Chinese are gobbling up whatever is there to gobble. I don't quite buy into the idea that North Korea now becomes another province of China. But, you know, you could paint a picture over time where there are avenues that China has.

Indeed, if you look at what Hu Jintao said to Kim Jong-il on his visit, there was this five-part list. I won't go through all of it, but he was basically mapping out what a normal relationship would look like between China and the DPRK. They don't have it. Kim did not allude to this. It's independent, of course, of the nuclear weapons issue, and that's -- in effect, the Chinese say that they're setting aside that question just to see whether or not you could put the pieces in place over time for a more normal relationship. But then that presumes a system that decides that its long-term interests are to in some measure at least, achieve a normal or a quasi-normal relationship with the outside world.

One last point. I mean, one thing that really strikes me about the North at this point is that the degree of dependence on China has grown significantly. Usually that's not North Korea's style, but, you know, they

haven't got the United States. They've lost South Korea. They certainly don't have Japan. In the Russian case, the North Koreans still owe them about \$8 billion. The Russians have tried very hard. They haven't gotten back a kopeck. It's a very unsettling picture. So as Richard said when -- before the question was posed to Mr. Pollack and it was a question from a private equity firm, Richard said to me, you know, it's got to be for the other Pollack because who's interested here?

Now, again, it's not to say that North Korean couldn't be a productive society and system under alternative circumstances, but it's a long way from here to there. And, you know, frankly I think the Chinese have just decided to play a waiting game, which again, they could be disappointed yet again, but it is also a way in which they think it's kind of a damaged limitation strategy. But it begs the issue about how much there is an intrinsic concern about the existence of some kind of a nuclear capability in the North. Some kind of a belief that the North will still be constrained from undertaking major risk-taking behavior. But that remains to be proven.

MR. GRAVER: PRC has significant leverage with Iran in terms of engineering services, in terms of involvement of the infrastructure, in development of the oil industry, new fields and so forth. China has capabilities that say Russia doesn't have. So Russia could provide cover in the Security Council, but couldn't step in the gap in terms of development of

the economy the way China has. Will China agree to roll that back? That's another question.

But addressing the other points you raised. What should be the U.S. approach? I really doubt that trying to pressure China would be that effective. My hunch is that that would confirm the Chinese notions of America as a bullying hegemonist power prone to power politics and this type of thing. I think more effective would be to solicit China's genuine partnership in the cooperation in dealing with these issues. I mean, that appeals to the, you know, the -- maintaining the favorable macro climate for development. It flatters China's notion as a rising global power. It provides a framework for dealing with the problem of, you know, power -- great power succession and war and peace. And China could grow into the steps of the incumbent great power.

So that would offer, you know, I think an appeal to China for genuine partnership to deal with these things would probably pay off better than an attempt to drive a wedge between Iran and China.

MR. K. POLLACK: Thanks, Richard.

I love your question, Scott. I'll answer a little bit more bluntly in terms of, you know, is China the problem. I'd say no, yes, and yes.

No, China's not the problem if the problem is the Iranian nuclear program and how do you turn it off. As I described the real problem

is Iran. They want the program. They're not interested in changing their minds. And it would certainly be helpful to have the Chinese onboard, but nobody is saying that even if the Chinese were onboard that that would be enough to stop the Iranians in their tracks.

Yes, in the sense -- and actually here I apologize. I wanted to make a joke at the beginning. As you at least know, I'm a former member of the Clinton Administration so the answer to the question depends on your definition of what "is" is. (Laughter) So if the "is" is stopping the Iranian nuclear program, no. China is not the problem. If the "is" is nonproliferation, then yes. There I would say that China is part of the problem because again if what you're afraid of is that Iran acquiring this capability sends a terrible message which will then spur further proliferation, potentially at a much greater pace than we've seen in the past, China's unwillingness to sanction Iran, to make it clear to other countries that there is a steep price to be paid for this kind of defiance of the international community, then that definitely is a big part of the problem.

And then my third point is actually on a somewhat different issue, which is about stabilizing the Middle East. And here, John, I was so struck in your comments. Listening to everything that you were saying about how you could have taken every -- almost word for word and actually made it about American policy in the 1920s, '30s, and '40s with the hegemonic

power being Great Britain. That is exactly almost word for word how the United States felt about Great Britain, including our stance on principles, them being a hegemon, all these -- everything. It's remarkable.

And what it also gets to is that in many ways China is, in fact, you know, treading the exact history that we went through in the Middle East. I was also struck by your point that the Chinese just don't buy it when we say we have this mutual interest. And again, you know, the British kept trying to make that case to us. We didn't figure it out until it was too late.

MR. K. POLLACK: Right. In fact, later than that. I would actually argue 1973 is when we figured it out. And we figured it out way too late and we've been trying to play catch up ever since.

And, you know, where I'd come back to is I completely agree with you, John, that the answer is partnership. And here I do give the Obama Administration credit because I think that's the argument they've been trying to make about what it means to be a stakeholder. And I think that a big part of it is helping the Chinese not repeat our mistakes. Now, I will give us a little bit of credit in that I think the British really were rapacious and hegemonic in a way that we aren't. But, you know, nevertheless, the British did have some good arguments that we tended to ignore about the importance of this region and their role in providing a public good that we tended to simply ignore. And I think a lot of what we need to do with the

Chinese is to kind of come to an understanding about those issues and then, yes, as partners move forward in the Middle East.

MR. BUSH: For any officer from the British Embassy here, Ken was talking about Britain in the past, not today. (Laughter)

Scott, I would also say that in my limited understanding of both North Korea and Iran, I think victimization at the hands of outside powers is a core part of national and state identity. And so that constrains, you know, whatever outsiders can do, however sort of strong their capacity and will is.

MR. NELSON: Thanks. Chris Nelson with the Nelson Report.

Since I do mostly Asia and North Korea as you know on these things, I'm totally innocent on how to think about the proliferation implications in the Middle East. And it's fascinating to me the way Ken Pollack especially talks about it. The Iranian bomb means the Saudis and the -- you know, and you go down the list. Why does it mean that? Why is it in their interest to have the bomb? Is Iran their enemy? Because the parallel is drawn with, well, then, you know, the North Koreans mean the Japanese have to, the South Koreans have to, the Taiwanese have to. You know, I know the answer to that one. If you're an Asian country and you get the bomb, you automatically become a first strike target for the Chinese. So why is that in your interest, you know? You can argue that one, but it seems pretty clear.

Because otherwise, really you're left with one thing. We sit

back and let this happen or we have to say to ourselves we will take the chance and roll the dice and really use a military option. And I don't mean screwing around with bombing the cave. You know. That's what one gets from listening to you. And I don't mean that in an argumentative way. But, you know, the person sitting next to me said, yeah. You know, if it's that bad and nothing we have works and nothing we're going to do will work as long as this regime is in place, then what other option do we have if it's really proliferation all over the Middle East? Period. That's what's going to happen.

Thanks.

MR. K. POLLACK: Thanks. Thanks, Chris. I appreciate you asking that. I was waiting for someone to ask that question.

MR. NELSON: It takes the innocent mind (inaudible).

MR. K. POLLACK: There is another option. And, in fact, again as was suggested to answer Richard Harris' question, it's the one that we're working on very hard here, which is containment. And you know, containing a nuclear Iran is not going to be fun. It's not going to be easy. But there's no reason to believe a priori that it's impossible. It's, you know, it's more than simply saying, look, we can contain the Soviet Union and the Soviet Union was a lot bigger, meaner, tougher, stronger, than Iran. It's a fair point.

But Iran is going to be hard in other ways. And as I said, we were already looking very hard at it. And I'll just give you one. But again, I don't want you to -- I don't want to suggest that containment is impossible. I just simply want to point out the difficulties and why it would be much better to not do so. Which is--even if you imagine that Iran has the best of intentions, which I don't, especially given the change in leadership since June 12, 2009. But even if you do, during the Cold War with the Soviet Union, which didn't want to incinerate us, we nevertheless got into some very, very nasty crises with them over the Cuban Missile Crisis -- Cuba, most obviously, but also Berlin several times, the Middle East a couple of times.

And what we learned from that experience is that it really takes three things to make crisis management work. And the literature is, you know, replete with this. It takes both sides understanding each other basically, having good communication between the leadership, and the two leaderships being able to signal each other in ways that are recognizable to each side. Okay? That's how we got through all those crises.

We have none of that with Iran. None of it. None. None. None. We don't understand the Iranians; they certainly don't understand us. We have no communications with them. And all of our signals are misunderstood by them, and all of their signals are misunderstood by us.

Okay? Again, I don't want to suggest that containment is impossible. I believe that it absolutely is possible. It's just going to be hard.

MR. BUSH: I would argue that the trajectory of the North Korean issue is in precisely the same direction -- that we end up with containment. But if it's hard enough to get China and Russia to go along with what we're doing now, just think of how much more difficult it will be to get them to go along with that.

Ken, I'll give you the last question. And then we'll give each -- right here. Each panelist a chance to wrap up briefly.

MR. LIEBERTHAL: Ken Lieberthal, Brookings.

Forgive me if this question has been asked. I had to duck out for just a minute. But it seems to me from both what Jonathan and Jack were saying, that it would be -- that the U.S. should think in terms of what we could do that would be a wake-up call for North Korea. Right? Reinforce redlines that we've allowed them to march across without consequence. I wonder whether you could suggest what we might be able to do that would be a consequence given the context of our policies at this point. Are we -- is that something that would be nice, but there are no realistic options for it?

MR. BUSH: Jonathan?

MR. J. POLLACK: Ken, we actually may be confronting soon an opportunity, dare I say, less with respect to their nuclear weapons

capabilities and more with respect to their actual behavior. And this is over the result of the Cheonan investigation, which is multilateral as Jim Steinberg pointed out earlier.

The North Koreans, despite their fearsome rhetoric -- I mean, this is -- at a lot of levels this is a very, very diminished state. They are a diminished state that now is in possession of a minimal nuclear capability. Whether they could deliver a weapon or not, we don't know. Whether they even want to deliver a weapon or not, we don't know. This is where we're bumping up against what we don't really understand.

But I do think that there have been some historic episodes where they have and can be sobered. I'm not arguing that the United States or anyone else go off halfcocked. Quite the contrary. But I think what we may be facing to just follow up on what Chris said a couple of moments ago -- is the need in some sense for an inhibition strategy, a containment strategy that finds us again, much to China's chagrin I might add if it happens, to be more militarily active and in an effect compelling South Korea in a lot of ways to turn its attention towards the continuing problem that they face. I mean, to be frank, I think in a lot of ways Lee Myung-bak, the president of the ROK, really looks upon his own country as a major actor in and of itself. That he would prefer to see unification, but he doesn't have unification. South Korea is going to have to find its strategic and economic

destiny apart from that. Well, there are ways they're going to have to make sure that North Korea is inhibited from the use of any of its capabilities, lest bigger risks do transpire.

One other point here, and I can't emphasize this enough, it does seem to me that the challenge for the United States, and China, and others, is not to allow political space to be created between them such that we lose sight of fundamentally a shared objective to prevent long term a nuclear armed North Korea. And the risk right now where there's this kind of separate tracks, if you will, between on the one hand the United States holding to a very consistent and very explicit fashion, to not compensate the North, whereas China in its own interest is seeing the basis for -- if not building up the North, at least keeping them on some kind of a lifeline. That is worrisome only because it creates room for -- that the North Koreans have shown historically they are only too capable of exploiting very, very effectively.

By the way, one last point I would make and it didn't come up in any of our discussions and it warrants an entire separate session, and that is the degree to which Iran and North Korea interact on a whole variety of programs because then you're really talking about a significantly more worrisome scenario -- something that might even get China's attention.

MR. BUSH: Jack, do you want to --

MR. PRITCHARD: I can do it in the wrap-up.

MR. BUSH: Okay. Why don't you start wrapping up?

MR. PRITCHARD: Wrapping up and answering your question.

I do think that unless we do something -- in your words, sending a wake-up call to North Korea -- we are, as Richard pointed out, headed for a containment policy. That doesn't get us anywhere. You'd have to be very lucky with North Korea that that's very effective. And so what I have suggested is that we understand the vulnerability of North Korea. What's important to them. And for them it is movement towards 2012 in terms of some successful economic progress that enhances from their perspective the transition from current leadership to future leadership. And I think that we need to get inside of that decision cycle of the North Koreans and begin to interrupt it to the point where it causes the North Koreans great concern that their stability of the regime is at risk -- the future beyond Kim Jong-il is at risk -- and then you've got something that very well may get their attention.

MR. BUSH: Jonathan?

MR. J. POLLACK: Jack has reminded us that although we do not have easy means of entry or influence into the North Korean system, that consideration of how you do this and what kinds of tools are at our

disposal warrants much more careful consideration than we have given it to this point.

I would only conclude to say 2012 is going to be one hell of a year between North Korea, South Korea, Taiwan, the Chinese succession, and I think there's going to be an American presidential election, too, so.

MR. BUSH: John, any wrap-up comments?

MR. GARVER: Yeah. I was struck by the congruence between Jonathan Pollack's description of Chinese policy towards Korea and my own take on Chinese policy towards Iran. And it seems to me in the case of Iran, there are deep, deep domestic roots for this. China's public opinion has been educated at least since Tiananmen in '89 to be deeply suspicious of the United States. And this public opinion resonates through the Internet and interplays with succession politics so that any leader that aspires to be a paramount leader cannot afford to be weak in dealing with the United States or to be willing to play second fiddle to the U.S. hegemony and so forth. So deep roots of this in terms of domestic policy.

There is also, I think -- the Chinese political system is fragile in many ways. And it lacks the legitimacy which leaders based upon elections have, which means I think that Chinese leaders are very cautious because they're afraid of being embarrassed. And if they undertook to be partners with the United States, they would be second fiddle. And I think they

perceive a great danger of setback and failure and criticism. So in terms of addressing this fundamental question of how to persuade China to move towards closer cooperation -- genuine cooperation with the United States as a strategic partner in the Middle East, I think we need to be cognizant of these deep domestic roots of China's reticence.

MR. BUSH: Ken, any final words?

MR. K. POLLACK: Just a very quick one, which is that I'm struck once again in this conversation about how difficult it will be to have this relationship with China related to the Middle East moving forward. But also, of course, how important it is. And one of my great fears is that -- it was again motivated by John's description of Chinese thinking about American policy in the Middle East. You know, the actual -- the experience of the United States in the Middle East has been that everyone assumes that we want to conquer the region. And in fact, all we want to do is get the hell out. Pardon my French. All the United States has ever wanted to do is to leave the region behind and have nothing to do with it, even the Bush Administration. The whole goal of conquering Iraq was we were going to put our guy in charge. He would be good and leave us alone and we could walk away.

And what I would just be afraid of is that the differences between the United States and China, while simultaneously recognizing --

and we haven't really talked about the importance -- the growth of Chinese power and influence in the Middle East, I would just hate for that to be yet another incentive for Americans to walk away from the Middle East because that's been the bane of our policies towards the Middle East over the last 50 years.

MR. BUSH: Thank you very much. We'll take about a 10-minute break. I made a pledge to Ken Lieberthal that the audience I delivered to him would be as large as the one that I had, so please don't let me down.

Second, I would like to thank the various Brookings people who have helped make this event possible: communications staff, my staff, the China Center staff, especially Kevin Foley.

Third, I want to thank the panelists for a really outstanding session.

Thank you very much. (Applause)

MR. LIEBERTHAL: -- U.S.-China topic, which is the economic and trade side, both bilaterally and multilaterally. We clearly have -- the U.S. and China clearly have highly interdependent economies, and the two are clearly the two key drivers of global economic growth at this point, or at least that is the role that ideally each can step up to.

But there are some really big questions on everyone's agenda

regarding our relationship at this point. How are the global economic and financial systems being restructured, and what will the relative positions of the U.S. and China be a couple of years down the pike as all of this settles out. And to what extent will the operating principles of the global economy have changed in a significant way because of the events of the last several years and how we work our way out of it. Are we and the Chinese going to manage our interests in a way that contributes to open trading and investment regimes? Or will we end up in a position that has created new obstacles to the free flow of goods, capital, and know how. And will the global economic and trade issues become a source of growing mutual trust and of strength in the U.S.-China relationship? Same basic question we've asked about the nuclear nonproliferation agenda and also earlier about the climate change agenda. Or alternatively, is this an area that's going to end up creating new frictions and new levels of distrust between the two countries?

We have two wonderful speakers to address these issues and others that they may choose to add. Anne Krueger is professor of International Economics at SAIS right next door. She, I believe, is still a fellow of the Center for International Development at Stanford University.

Is that correct? Yes.

She has held a series of very important positions over the

years including being first deputy managing director of the International Monetary Fund for five years a little earlier in this decade. She's both a distinguished fellow and past president of the American Economic Association. She's published very widely on economic development, international trade and finance, and economic policy reform.

Barry Bosworth, as I'm sure you all know, is a senior fellow of long standing in economic studies and in global economy and development at The Brookings Institution. He's also the Robert V. Roosa chair in International Economics at Brookings. I love the fact that he received his PhD from the University of Michigan, which is the place where I've spent most of the last quarter century and more. Clearly a man of great quality.

And we'll, as in the previous panels, first do the two presentations and then we'll open it up for Q&A at the end of both presentations.

Anne, if you'd like to begin, please.

MS. KRUEGER: Thank you. The subject of China, the U.S., and international economic relations is already a broad one. If I speak of that and if I try and take on the questions that you said, too, we'll have the audience here till midnight. So I'm going to have to be somewhat briefer than that.

The two big issues bilaterally in U.S.-Chinese economic

relations -- which is where I'll start because they lead into the global. I have basically been a large -- I don't know whether you want to call them the Chinese current account surplus or the large U.S. current account deficit on the one hand, and out of that the U.S. has chosen to raise very strongly the issue of the Chinese exchange rate because of the first issue. And there's been a lot of pressure from that and a lot of misunderstanding.

There is no doubt that China's trade has grown rapidly. China is the new kid on the block in the world. It is estimated that if not this year, then for sure next year China will have the number two spot in the world in exports denominated in current exchange rates. There's no more purchasing or parity or anything, just number two in the world in exporting, and growing very rapidly.

Whenever a country's growing rapidly, there are always some juggling of shares and that always leads to some problems. But in this case the size of the current account surplus and the speed at which it has come up has been an issue.

But I want to back off from that just for a bit and talk a little bit about why the issues really are multilateral and not bilateral. And why in fact it would probably be desirable for everybody, including the Chinese, the Americans, and the rest of the world if these were not regarded so much as bilateral issues as they now are. In general, most issues have spillovers to

other countries. Trade and exchange rate issues probably have about as much spillover as you can think of.

Let's for the sake of argument imagine that the U.S. did something very punitive with regard to imports from China, says it's going to cut them 50 percent or some such thing. The U.S. has no tools to do that. It's illegal under the WTO. I'm not suggesting you should--I want it as a mental experiment. Okay. Let's imagine the U.S. says, okay, they've got to go down by half.

Well, among the things that would happen would be that a lot of things that were previously coming from China would anyway come in from countries such as Korea, South Korea, from India, from Thailand, from Malaysia, from Indonesia, from Australia, from Japan, from Taiwan, and everywhere else.

Trade is multilateral in so many ways it is hard to think of how you do something bilaterally, and yet much of what has been the focus in all of this has been bilateral. And that I think has been a big mistake both for the obvious reason that it isn't the way to go at things and because it's not a bilateral problem, but also because I think it's been very ineffective and is indeed, because of issues that were raised in earlier sessions, Chinese nationalism, Chinese suspicion of the U.S. and our role and desires, the Chinese once again are likely to react and say or to believe that indeed this

is something the U.S. is pushing on them because the U.S. is unhappy with Chinese economic success. So I think there are a whole variety of reasons why it is not the way to go. Trade is not a bilateral thing.

The history of economic sanctions in the world is one of failure after failure after failure when even one or two very small countries don't go along because they become the entre par route through which the trade actually flows which flowed from before and it takes very much universal agreement and what have you before anything happens. So the argument for multilateralism in trade is huge.

Now that takes me then to my first sort of global issue, which is related but not quite exactly the same thing as what Ken was talking about, and that is that among other things that have not happened in the past year and a half and should, an important one has been there has been no serious definition of U.S. trade policy going forward. And most importantly in that regard there has been since 2001 a Doha Round in trade negotiations that is still legally underway; where from about, well, certainly from the summer of 2008, but even before that, the round was held up waiting for the new Administration to figure out what it wanted to do with it. There has so far been very little signal on that. And so at the moment the Doha Round, which would be the best way forward on all of these things, is at an impasse and is leading to all sorts of things including more

protectionist reactions from a number of countries and so on that are likely to move the entire world trading system in the wrong direction. And that's independent of the current financial situation, which of course is making it a little bit worse but not as much worse as I would have expected.

But underneath everything I would argue that taking the issue of the Chinese current account, U.S. deficit -- and I'll come back to that in a minute because it's got a macroeconomic dimension which is very important -- taking that issue multilateral and not trying to handle it on a bilateral basis would make economic sense. It would also have a chance of success, which a bilateral deal does not. And in other regards as well it'd be perfect.

But on top of that we had an issue from about 2003 onward that was widely discussed, at least by some at the global level, which talked about global imbalances. Global imbalances were the argument that the very large U.S. current account deficit, which as you know got up to 6 percent of GDP, was too large, was not sustainable, and the current account surpluses that were the counterpart of that, which first came mostly from China with a few other countries and then with the oil exporters as well, that these global imbalances were a source of major difficulty for the world economy and were unsustainable.

The IMF actually did spot this, despite the fact that nobody remembers it. The then managing director of the IMF called for multilateral

consultations, with a view to bringing together the surplus and the deficit countries in a multilateral forum and to get just a few key players, six was the exact number, and have them agree as to what the problem was and what measures each would take in order to try and resolve the problem.

There were meetings held and everybody agreed on the problem. There was no disagreement whatsoever but that that had to be resolved. This agreement was of course how do you resolve it? Should it be the deficit country or the surplus country? The United States thought of course it should be the surplus country, and the oil exporters and the Chinese thought it should be the deficit country. There the matter stood.

Now, what happened subsequent -- oh, let me just say that the large current account deficit of the United States enabled or was a result of - - and I won't argue which here -- very low real interest rates in the United States and in much of the rest of the Western world. Those low real interest rates, according to some, including me, were a very major factor in contributing to the financial crisis. This was the way that sort of signaled it was unsustainable. Very low real interest rates certainly encouraged housing. They certainly encouraged the Carry Trade. They certainly encouraged or made cheaper the development and more rapid development of the various derivatives and hedge funds and so on that everybody's now so mad at. Okay.

So global imbalances were unsustainable. And as it happens, the way they blew up was through the financial sector. And those global imbalances were real. And there were real underlying causes, namely these big surpluses and deficits on current account in two major parts of the world.

With all of that we've now seen a situation where China's current account surplus went down somewhat. The U.S. current account deficit is down somewhat. But there's nothing that I know of, and nothing that anybody that I know of knows of, that is to prevent it from happening again. As the world economy picks up, it's certainly likely that U.S. imports will rise more rapidly than exports, especially with the recent dollar appreciation. It is more likely with the U.S. as it picks up that the Chinese exports will pick up again. And with all that, if nothing else goes wrong in the next 5 or 10 years, and, of course, it may even before that, we are likely to see another global imbalance and another buildup.

This is not a China-U.S. problem; it is a global problem. It is as much in China's interest as in the U.S., but it is not a bilateral problem. And therein I think lies the difficulty because, well, the Chinese hear the Americans saying you should change your exchange rate, you should do all these things, then it looks bilateral.

Now, China is certainly the biggest, and China may have other problems ahead of time that might reduce it. China's savings rate right now

-- or let me say it differently. China's consumption as a percentage of GDP is below 40 percent, which is about the lowest, except in wartime or except in other very unusual circumstances, that has been heard of in human history, as far as we know. Forty percent is a very low number. And the current account surplus is of course the difference between investment or expenditures and income. And so China is saving for domestic investment a lot, but even then has a lot left over for current account surplus. The U.S. was doing the opposite, namely investing a great deal more than we saved, and the financing of course came from China.

Given all that, the question is what can be done. And the answer is that there does need to be some kind of global regime to work out a mechanism whereby we get realistic numbers so that unsustainable current account surpluses and deficits cannot last. That's not an easy thing to do and it won't be simple. And it's not two countries. For all we know, China, with the demographic changes coming and other things coming along, may not any longer be the saver in the future. Maybe some other part of the world that will be saving huge amounts. Maybe it'll even go back to the United States. It doesn't matter. The point is that the world does not have a regime right now to do this and yet the discussions don't progress because we're focused on, I think, the wrong issues.

Now, as to the exchange rate, Chinese exports are about 25

percent of the GDP, which is large. But the 2.5 percent Chinese imports -- sorry, are 2.5 percent of U.S. GDP, 2.5 percent only.

SPEAKER: Chinese imports to --

MS. KRUEGER: To the U.S. are 2.5 percent. Now, what that tells you, that even if we cut them in half we'd get a change of about 1.25 percent. That's not where the trouble's coming from. And all the screams about jobs and everything else are overdone. The Chinese macroeconomic impact, insofar as there is one, is global, and it's their large savings not their exports to the United States per se. Savings may fall as a percent of GDP; they won't fall absolutely. But, of course, China is huge, and as it grows everybody notices it.

We need to strengthen the multilateral trading system for its own sake because it's good for growth of everybody, including China, including India, including the United States. We need to find a regime so that we cannot get back to the unsustainable global imbalances the way we had it. But most of all we have to do it in a multilateral and not a bilateral fashion.

So I would argue that the big issues between the United States and China are not the big issues between the United States and China, they're global issues. They're more important than either country alone. They cannot be solved by either country alone.

One of the interesting things is perform the mental experiment: If in 2005 the United States went and said okay, we can't keep up these current account deficits. We're really going to change quite abruptly our fiscal policy so that we indeed cut down our expenditures relative to our income quite drastically, and so we're going to go into balance very quickly. If nobody in the rest of the world had done anything, there would have been one very big worldwide recession. And if the Chinese had decided to cut down, without anybody else doing so, we would have had quite a bit of inflation. There needs to be mechanisms -- or it needs to be a mechanism that can work for both sides, and that both sides aren't necessarily the same countries over time.

One of the interesting things to me is that much of the rhetoric about China now on trade and exchange rates is not that different from what we heard about Japan in the 1980s. In the 1980s, Japan was the new kid on the block. And everything you heard about American manufacturing going wrong was all Japan's fault. Now, everything there -- the Japanese were saving too much. It was their current account surplus, et cetera, et cetera, et cetera. Well, what happened to Japan wasn't very pretty, but it didn't happen because of what -- that discussion. It happened because indeed the issues in Japan were inflation and things like that that then caught up with them in the 1990s and they went another way. For all we

know, the same kind of thing may happen to China. But that's not the issue. The issue is to find a global regime so that indeed we do not have the kinds of imbalances that we had.

Let me at this point stop there. If you want to get into the global financial crisis, it's such another topic that I don't dare start on it because I wouldn't know when to stop, and give Barry a chance.

MR. BOSWORTH: Thank you. I think I'm going to end up repeating a lot of the same themes of Anne. But I want to take it a little bit more from the U.S.-China perspective.

The first point I want to make is that surprisingly the economic crisis has been good for China, I think, on balance. One reason is it simply has not been part of the global financial crisis. The financial system that many people were critical about was helpfully closed during this crisis and therefore largely unaffected by the disruptions in the rest of the world.

The negative shock to China was through the trade mechanism. And so there was a very powerful distortion of trade. But China's response to that was a big stimulus program. I think the other point about the stimulus program is it was amazingly successful. China's stimulus program was much more successful than the American one, mainly because the speed with which it could begin to operate. As a result, China had a very modest slowdown in 2009 and has come out of the recession with basically

no worsening of its structural economic conditions.

But the second thing I think that's happened that gets overlooked a little bit is that the financial crisis was very helpful in highlighting for China the risk that it followed by its past economic policy of too much reliance on an export surplus-led economic expansion. And the exposure to an unstable world economy as compared to China's policies, say, before 2004 or 2002, which were much more domestic growth oriented, I think was a warning to the Chinese that they needed to back off from this excessive emphasis on export growth.

Looking ahead to 2010, I think you now see China back on a growth path of about 10 percent a year. Inflation is one concern, but still the projections are that it's going to just stay in the range of about 3 to 4 percent. But they are worried about a real estate bubble and they are paying the consequences of accelerating world commodity prices. But the other thing is China has no significant fiscal problems looking forward. Its debt levels are extremely low. Balance basically in the budget. What it does need to do is shift its monetary policy now that the stimulus requirements are over, and it relied so heavily on a big explosion of lending. It's now got to shift monetary policy back towards restraint.

But I think what you're also seeing is the emergence of an emphasis on growth in their domestic economy, particularly an emphasis on

promoting growth in the western provinces as opposed to the coastal areas. Second, an acceptance that appears of urbanization as an inevitable part of economic growth, and it appears that the government is going to quit resisting as it has in the past a lot of the urbanization measures.

And I think the major domestic problem that they have about getting balanced economic growth is the households, although I know other economists characterize Chinese households as high savers, to me the data suggests they save about the same percentage as the Japanese did in the 1960s and the Koreans in the 1970s and '80s. High growth economies, people save a lot because their income's going up so fast they can't figure out how to spend it. The same would happen to us if we could only have a rapidly growing level of income.

But the problem for China is that not very much of the income gets to the households. They would be perfectly willing to spend it if they could get their hands on it. The trouble is that the government and the enterprises or the corporate sector drains off enormous proportions of income in China away from the household sector. And so although we see 10 percent growth in GDP, we show relatively slow rates of growth in household incomes. And they've got to figure out a way to get more money into the hands of households, either through reform of dividend policy or tax policy on the corporations. But I think that's their big challenge. If they want

to have a domestic restructuring, they have to find a way to promote the household sector as being more significant in the growth process.

From the economic relationship of the U.S. and China as we go ahead, and we're going to have I guess a meeting this month, I think the major focus will be and I agree with the two countries have to rebalance their two economies. And this is something on which they should be able to cooperate closely. And as Anne emphasized, cooperation between the two outliers in the global system to reduce their extremes should be very helpful to the world economy as a whole. So China has to move towards greater emphasis on domestic demand, particularly consumption. And the United States has to increase its saving and move towards greater efforts to export. Neither was interested in this prior to the crisis. But now that the crisis is over, or seeing the effects of it, we're both extremely interested. And so you see China much more interested in trying to promote domestic demand and reduce this reliance on these unstable Westerners.

And I agree completely with Anne that in the process of working this out the major risk is a replay of the U.S.-Japan unproductive relationships and discussions when the last time we had a dialogue with another country. Maybe because both of us are older, but I have strong memories of that. And to me it sounds just like déjà vu, that if I took all these columns in the New York Times and other places and changed the name

from China to Japan, it would be a perfect replay. And I think that is a major threat that we face in doing it.

Yet the basic problem is an important one and something that we should find a way to get a solution to. I'm not so convinced, I guess, that multilaterally we'll ever do anything. Multilateral meetings tend not to be very productive. So there's at least an opportunity to try this on a bilateral basis and see what happens; if both countries can maybe deal with it better.

I think China worries mainly -- one issue for them is what's the value of their reserves going forward? They've accumulated an amazing amount. They've learned it's not a good idea to hold them in euros. They got a lot of them in dollars, but now they're going to be worried about the decline in the value of the dollar. You see their efforts to promote some system they've referred as like SDRs. I can only say it's not going to happen because what they really want is fixed exchange rates within that kind of a world, and they're not going to get fixed exchange rates. If you accumulate a lot of foreign exchange, you've got to worry about the changes in the price of it. And you can try to diversify your risk, which I think China can make some progress in, by not emphasizing so much the dollar. But as long as they got large international investments, they have to worry about the value of them.

I think, and I'd agree very much with Anne, that it is a mistake

for the United States to focus on the exchange rate. The reason is what we ought to be worried about is trade flows. And there's probably a connection between exchange rates and trade flows, but I think when you're dealing with a country like China, with all its other distortions and the stage of development it's at, there's a lot of slip between those two. The United States is likely to get some movement on exchange rates and no progress on trade, and that's not what we should be interested in.

So I think that it's also important that the U.S. realize we don't compete with China. If you look at the things we produce and we have a comparative advantage in, China does not produce them. We compete with Japan and the EU. And what we ought to worry about is what happens to the U.S. exchange rate vis-à-vis those two countries, or two regions if you like. And what we also should be interested in is improving our access to the Chinese market as a market because there's a growing recognition in the U.S. that it's very important. In terms of the exchange rate, I would think Mexico and Vietnam would be fighting much more over what the Chinese exchange rate ought to be because they're more directly affected, not the U.S.

The other thing is I think thus far this year there's been a little bit too little appreciation of how much adjustment has occurred on the Chinese side. The current account surplus peaked way back in 2006,

declined sharply in 2009. It was down to about 6 percent. China has now released its trade data through the first four quarters of 2010. It's running at one-fifth the level of the balance that it was running at in the first four quarters of 2009.

MS. KRUEGER : Four months.

MR. BOSWORTH: First four months. What did I say?

MS. KRUEGER : Quarters.

MR. BOSWORTH: Oh, I'm sorry. Months.

The Chinese exchange rate has also now, over the past two years, increased quite a bit relative to the U.S. And when you look at it on a real exchange that is adjusted for inflation, basically the Chinese exchange rate and the American exchange rate departed several years ago and they're now moving in opposite directions. They have altered their relative relationship by about 25 percent. So China's facing a rather substantial increase in its real exchange rate in recent years and the U.S. is in the midst of some depreciation.

I would share the concerns that the current situation has exaggerated those adjustments and maybe it will explode in the future. But the point is, so far this year China has made a lot of adjustment. The growth is domestically led. We now know in 2009 over 6 percentage points of the growth in GDP came from consumption. That's about 60 percent of the

total. So China has moved quite a bit in the direction of relying more on domestic demand. There was a lot of infrastructure spending. And I think the major question with all of this is simply can China sustain it. But we don't know the answer to that question. But I think if you just start with have they done anything, the answer should be yes, they have.

In contrast you would think, okay, the United States had to restructure on the other side. Right? And so what rebalancing have we undertaken as a country. Well, instead the United States is stuck in a deep de-session. The trade balance has improved, not because we're doing better in that respect but because our imports collapsed more than our exports.

MS. KRUEGER: And oil prices.

MR. BOSWORTH: And oil prices are down, although they're headed back up again, it would appear.

The United States also for the first time in its history now has a negative national savings rate. That is rather remarkable that we now spend more than we earn. And the only reason that we don't have an explosive problem on the external balance side trying to finance such a situation is that domestic investment has fallen to only 2 percent of national income. So we've now turned into a country that's got negative savings and extremely low rates of domestic investment. The combination of those two, so far, are

keeping down our foreign borrowing requirements.

Economic growth has accelerated in the United States in recent months and I think we can be much more optimistic about 2010. But unfortunately, it's because we all return to the habits of the past. We're back on a consumption binge again as the household savings rate has fallen back to where it was before the crisis, and basically our economic recovery is being led by consumption. The trade balance actually worsened in the first part of 2010 and it appears to be going in the wrong direction.

I think the big interest for the United States at the present time is why do we want to export more. We have to; otherwise we're not going to be able to create enough jobs. We can't go on as an economy anymore with its really strong domestic consumption where we can afford the type of trade deficits we had in the past. So the U.S. has to move back to a more balanced economic situation where exports are growing rapidly (inaudible) close to exports and imports being equal.

In that regard it seems to me the one promising area of the world where we're doing better is China. Since compared to 2009 a year ago, our exports have doubled to China. Our imports have increased about 11 percent or so over that same period. I wouldn't be too happy about it because you should realize that our exports to China are historically only about one-fourth of our imports from China. So we have a long ways to go.

But in terms of ability to respond on the export side, the improvement in U.S. exports has actually been to Asia, and we do seem to be doing better on the export side.

Looking ahead, what bothers me about having a discussion with China on this issue of our economic relationship I think it's important for American negotiators and Americans to keep our focus on jobs, that ultimately the objective here is to increase U.S. exports. I'm a little distressed to hear all the discussion of improving business conditions in China. I'm not that interested in whether or not American firms can do business in China. I'm more interested in whether or not Americans can export things to China. And they are not the same thing. So just the fact that American service companies can operate freely in China doesn't translate into a lot more jobs here in the United States. What we need to make sure is we get access for capital goods, which is the biggest area of U.S. specialization in export. And I would hope that we would keep our focus on those sort of measures and those sort of changes that would influence our access of American exports to the Chinese market, not just American business in the Chinese market.

Thank you.

MR.LIEBERTHAL: Well, thank you both for raising a very substantial array of significant issues and restructuring a lot of what the

popular discussion has tended to focus on.

The floor is now open for questions, and I see a bunch of them. Right back here, please.

And again, as with the other panels please wait for the roving mic, briefly identify yourself, and then please focus on a question rather than a set of comments.

MS. MILDNER: I'll keep that in mind. I'm Stormy Mildner from the German Institute for International and Security Affairs in Berlin. And I do have two questions.

The first one concerns how we deal with macroeconomic imbalances. And you seem to be in disagreement whether it should be bilaterally or if it should be multilaterally. And my question is, if there was a multilateral mechanism, where should it be? Should it be with the WTO or the IMF? And what would be the teeth of this mechanism? Should there be a WTO kind of dispute resolution, should there be sanctions, what would be the teeth?

The second question is regarding exports. I very much see the point the exports need to be increased, but the question is how are they going to be increased?

Thanks.

MR.LIEBERTHAL: Thank you.

Anne, do you?

MS. KRUEGER: Yes. On the macro imbalances, getting teeth is the issue. The current status is that the G-20 has instructed the IMF to get macroeconomic projections from the major countries, i.e., the G-20 plus a few, and then to work out how they will be consistent, et cetera. And then peer pressure is supposed to bring things into line. I believe peer pressure may have some chance of working, but I wouldn't put great faith in it.

There are other alternative mechanisms that could indeed be used. One can think of them. But so far, at least, there's no agreement on them. So that's number one.

As to WTO or IMF, my own instinct would be very strongly IMF. The WTO has been a trade organization. It's used to trade negotiations and that's where its comparative strength lies. The IMF has done much better in terms of looking at macroeconomic consistency, on getting the macro balances right and getting the projections right. The most recent evidence of that comes actually from your part of the world, as finally the Europeans had to call in the IMF to do the macro. And I think the IMF does already have enough strength there that that's where I would look for it.

But the more important point, as you recognized, was the one with regard to how you get the sanctions right. And that's going to take I

think some more work. But it's not too hard to imagine mechanisms; it's just hard to get agreement on them to get enforcement.

As to how to export, I'm less concerned than Barry is with exporting. I'm more concerned, as he said, too, with getting the saving-investment balance right. Because if that happens, then the exchange rates and other issues will move in the other direction. President Obama has announced a plan to double exports by -- or he has announced an intent to double exports by 2015, but so far the instruments or the policy tools or the incentives to do that I have not noticed.

MR. LIEBERTHAL: Barry.

MR. BOSWORTH: Some disagreement, I guess, but not seriously. I would love to do it by multilateral means if it was possible. But I don't think countries are willing to give up sovereignty over these sorts of issues like, say, budget policy. The idea that other countries are going to start to dictate to you your budget policy, unless it's a crisis where the IMF, you're the only source of money, I don't see that happening.

I think instead we should be emphasizing for these two countries, because they're so much the outliers, it's in their own self-interest to do this correction. And I think in fact China has made more progress in realizing that it's in their self-interest to get away from this overemphasis on export surplus-led growth and shift back towards more on the domestic

economy than the U.S.

And the issue is complicated for the U.S., because normally I fully agree the issue is saving and investment. If you'd save more, and I don't think you want to say invest less, so you're saying you want to have a savings surplus over domestic investment, and then you could export. I agree with that. But we are currently in a highly depressed economy. So it's not true that you have to increase saving before you can do something to expand exports.

The biggest barrier to U.S. export promotion at the present time unfortunately I think is price. The dollar in that sense is overvalued. I wish that Americans were better at exporting, but a long tradition of ignoring issues like exports, we're not particularly good at it. And I think the only way to effectively increase your exports is to cut the price. So I would expect to see the U.S. exchange rate ought to depreciate in future years. I think that's exactly what was happening before the financial crisis, the dollar fell. And then the trouble is, in the midst of the crisis everybody had a rush to Treasury Bills and that drove the dollar back up again. This is maybe an issue on which we'd like to have a population exchange between the United States and Germany because Germany's good at exports, but the United States is not so particularly true. I think it's mainly in the short run a question of price.

I fully agree, as we go forward from that, then the U.S. has to increase its national saving as a way to continue to finance this kind of recovery. But right now we've got lots of resources to export. We don't have to cut consumption in order to export more. A few years from now that may be necessary.

MR. LIEBERTHAL: Let's see. Jonathan, back here.

MR. J. POLLACK: Yes, Jonathan Pollack, Naval War College.

This question is more to Barry, although to both speakers, but you've emphasized the importance of export. But to what extent, if there were modifications, significant modifications in U.S. export control strategies, permitted technology limits, and so forth, how much would it affect that picture? It would seem to me intuitively that would be certainly one way of boosting what we sell.

MR. BOSWORTH: I think that's a very good point. It would certainly go in the right direction. I would only argue it's really small. There just is not very many commodities anymore which the United States has that big a technological advantage. For example, what we call high tech in the United States in our trade statistics we are now a deficit country in, right? It shows up as, oh, China's a big exporter of high-tech products to the United States. Now, that's not true. What is it because? Apple Computer in particular has an iPod and iPhone and an iPad, I guess, right? All designed

in the United States; not a single thing produced in the United States. They're all produced in Asia. They are labeled as coming from China in all three cases. China is a trivial -- they're the assembler of all this stuff that's being made in Taiwan, but principally in South Korea. And so it's a good example of where Apple Computer just plugs in to a global production network. And unfortunately, we're not really part of that production network anymore because we don't seem to have much of a comparative advantage in the production of those products.

So I think what you suggest would go in the right direction, but it would be a relatively minor measure.

MR. LIBERTHERAL: It's also interesting on the U.S.-China trade balance, if I can just interject something here, our imports from China really are imports from Asia.

MR. LIBERTHERAL: Yes.

MR. LIBERTHERAL: More than two-thirds of the value of those imports China itself imported and then assembled in China. But our exports to China actually are exports to China. Very little of that is put in something and then exported out of China. So we're really comparing apples and oranges when you look at these things bilaterally.

Yes, sir. Please wait for the microphone. It's coming right over. Thank you.

MR. HARRIS: Good afternoon. Richard Harris from Momentum Private Equity in New York.

And my question is actually for Mr. Bosworth. I believe you made the comment that no country is going to cede sovereignty when it talks to the restructuring of its deficit imbalances. But may I posit the point that that has indeed already happened vis-à-vis Greece, even though that is not germane to this discussion. And that the EU and the IMF having to come to its rescue, the market said we simply don't believe that you can restructure your debt through purely internal processes. And I will say, sir, what is to prevent the bond markets and people who I, you know, work with from making the same conclusion about the United States and Great Britain?

MR. BOSWORTH: Well, I thought I'd followed that remark by qualifying it by saying that Greece was an exception, if you can't get money from anyplace else.

No, I think the U.S. in the long run, this policy of running these external imbalances year after year is not sustainable. I think we all agree with that. So it's in our own self-interest to make the correction. I think mainly the argument is about how. One way to do it is wait till you have a crisis and then you have to. And there's a lot of countries who have done it in those sort of situations. They face an external crisis, they're forced to adopt, and they do. I wish the United States would do it before a crisis

occurs. But you may be right that we will refuse to act.

But it's a much different case. I mean, the U.S. is a huge economy at the center of the global economy. I don't know how that would play out. I do agree that the U.S. ultimately has to make the adjustment. I guess the only analogy I would give you, though, that kind of goes the other way: the children of John D. Rockefeller, been living off his wealth for over 100 years, right, and they're just fine. They haven't run out of wealth yet. And you could argue that's what's going on in the U.S. We are an extraordinarily rich country. We have been selling off assets and issuing debt to the rest of the world for about 20 years now with no signs that we've run out of debt yet. And they seem perfectly willing to buy our assets.

Actually, that's what they do, though. They buy our assets, not buy our debt. We are much more characterized by a country in which foreigners own a lot of assets here in the United States, rather than that pushed behind the debt. China's a big exception. China buys our debt. Everybody else buys our assets. We'll see who turns out to have the best deal.

MR. LIEBERTHAL: Let's see. Back here, yeah.

MR. LI: Li Zhongxin from Caijing Media, China. This is the follow-up of the Greek question. What are the potential impacts of the great crisis on the payout to Asia and to China? And particularly on the policy

front, will that make China's revaluation and move on interest rates easier or more difficult?

Thank you.

MS. KRUEGER: Well, as Barry said, so far China and Asia in general has generally had a good crisis in the sense that they've been able to avoid most of the fallout from the banks and stuff because they were not involved holding very much of the toxic assets that were part of the trouble, and they were able otherwise to have the fiscal stimulus because they did not have the high levels of debt. I don't see any reason why China would -- or East Asia or Asia in general will be any more affected. If the Greek bailout is successful of course you would expect Europe to begin to grow a little faster than it is, and that's good for Europe and the rest of the world. But it's not a big deal as far as Asia is concerned, as far as I can see.

MR. LIBERTHERAL: Let's see. Back here. No, right. Right turn. That's it.

MR. CHEN: Yeah, Chow Chen, freelance correspondent, Bethesda, Maryland.

Question for both of you. The reason as I see it for the every nation is co-bilateral trade because the Doha Round can know where. And so my question is this: would a world leader have political will to get the Doha Round done?

And talk about China I want to talk about U.S. now. We maintained a strong currency and low interest rate. This already show is unsustainable. And so what do you think to think so? And also you think the current administration have a political will to make a (inaudible) change so for U.S. have a sustainable future?

And China is rated a poor country. Why not use all this deposit to improve their standard of living overall?

Thank you.

MR. LIBERTHERAL: Thank you. Whatever you want to pick up.

MR. BOSWORTH: I'll take a crack at a couple of these things.

I'm more extreme than Anne on the trade. I believe the Doha Round is dead. Fast track has lapsed for the United States. I think it is unacceptable to the rest of the world to negotiate trade when the United States does not have fast track authority. The probability that this President can get fast track authority out of this Congress I would put close to zero. So I do not think that trade negotiations on a multilateral basis are likely to move forward, even though I fully agree with Anne that any other basis has been a disaster. I think a lot of the problems in trade is precisely because people tried to do it on a bilateral basis.

On the other hand, I think the international trade system has

held together amazingly well in this current crisis. I think they really did try to adhere to the G-20 prescription of minimal trade restrictions. Our country faltered a couple of times, but nothing big, just a lot of screaming. So I don't think there's that.

On the strong currency, I agree. I hope that our government officials in the future will keep their mouth shut about they want a strong currency. I think that's ridiculous to express any opinion one way or another on that. As I've said, I personally would like to see a weak currency. But I also realize that doesn't have much weight.

On political will, I think, yes, but it's a little premature. I think right now in the United States the focus of the politicians is on a single event: getting the economy growing rapidly again and getting employment up. And they put off the issue of rebalancing; that's something for the future. When they get there will they do it? I don't know.

In the 1990s, we were just fantastically lucky. Right? The Cold War came to an end. That saved us about 2 to 3 percent of GDP on the Defense budget. And then we had an economic boom that raised tax revenues. And the budget deficit just disappeared overnight. Well, then, of course, we were not content with that situation so we brought it back fairly promptly. But I think when you say political will, at the present time the U.S. focus is on increasing aggregate demand. And I believe a cornerstone of

that should be a very strong effort to promote exports. And that that's one of the reasons that's a key. I just am convinced we will never get back to full employment again unless we can rebalance and have a much larger share of GDP going into exports.

MR. LIBERTHERAL: Does that require a lot of government action?

MR. BOSWORTH: Well, only in the sense of something that would lower the exchange rate to make American goods cheaper in world markets. But otherwise, no.

MR. LIBERTHERAL: Otherwise, no.

MR. BOSWORTH: Although I think some other countries do have policies that are very effective in increasing their exports.

MR. LIBERTHERAL: No, I'm thinking of things like investment in infrastructure, you know, other policy options that are sometimes associated with export promotion.

MR. BOSWORTH: I don't think our ability to export at the present time is inhibited by our infrastructure system. I just think that American companies, number one, they don't really care about exports. If you're going to do business overseas, they'd just rather move overseas, and produce abroad and sell abroad. They're not oriented towards exporting out of the United States. And a lot of other American companies just don't want

to bother with exporting. They have a great big market here at home. For 25 years they could sell everything they got their hands on in a fully employed domestic economy. So I think they just didn't care. We are now suddenly very interested, but it's not so easy to generate an interest and a skill in exporting.

MR. LIBERTHERAL: Thank you.

MS. KRUEGER: If I could just add one thing.

MR. LIBERTHERAL: Please.

MS. KRUEGER: I do think that the tendency toward bilateral or regional preferential trading arrangements has already caused some problems. Some countries have faced them more acutely than others. But I'm pretty convinced that going forward we will see, I don't know exactly when and I don't know exactly how, some major difficulties, complications, what have you from this eruption of the bilateral and preferential regional and what have you agreements. And that at that point there will be a recognition that we have somehow to get back to some kind of multilateral discipline over trade.

MR. LIBERTHERAL: Thank you.

This is going to have to be the last question. Boy, that dropped hands like a rock.

Eric? You can always count on an admiral to step forward in a

time of need.

MR. McVADON: Thank you, Ken. Eric McVadon, the Institute for Foreign Policy Analysis.

From this stage a few months ago I think I heard a Chinese economist argue that since China was switching to the domestic from the export market that we ought to get involved. You seem to be arguing against that. Are you simply saying that we should give more attention to export or that we should not get involved in trying to be part of the domestic market?

And on another quick point. I think it goes back to 15 years ago that a Chinese interlocutor told me that China had realized that it simply didn't have the wherewithal to throw money at the North Korean problem. That it couldn't resolve it that way. It was too big. Even after what we've gone through in recent years and so forth, you think that's still the case?

MR. BOSWORTH: Well, let me try the first one. I have some reluctance to argue in favor of government involvement because I think that is usually translated into some form of industrial policy. And I think the United States is uniquely ill equipped to conduct a rational industrial policy. We have a system of government aimed at helping the losers, not promoting the winners. And so the moment the government gets involved it's always in there trying to stop the normal market adjustments in some industry that's

been adversely affected, like, say, clothing or shoes or some of the other more popular ones where we've had a lot of trade restrictions.

So I think the truth is we have to stay to the macroeconomic policies, from the government perspective. If you had a government that promoted saving, in this case that means reducing government dissaving, and didn't interfere in the exchange rate, I think we could get a competitive environment in which it would pay for U.S. exporters to focus more on foreign markets.

On North Korea, what I know about this you could stick in your ear. And I have a brother that's involved with it, so I'm not going to say anything.

MR. LIBERTHERAL: Anne, do you want to?

MS. KRUEGER: Yeah, there are some proposals for things like shifting -- the incidence of corporate tax here is much higher than in Europe and so on. And there are things that could be done to remove -- reduce at least some of the distortions in the tax code in ways that could make exporting more attractive and that would enhance American economic growth more generally. I think that there -- obviously, if infrastructure improves and you cut delays in ports and all that kind of thing it helps. But I think Barry's basically right that it is not a matter of getting the government into the act, it's a matter of getting sort of a level playing field and getting the

incentives right.

MR. LIBERTHERAL: This wraps up not only this panel, but this conference.

And before I let you all go, I do want to again thank Richard Bush and CNAPS for joining with the Thornton Center to put this on, and especially to thank the staffs of the two centers who did a tremendous job in making all of this feasible.

I also want to thank the speakers for all of the panels, many of whom flew in just for this event today. All of you for coming, and especially the speakers on this panel for just a wonderful way to wrap up what was a very busy day. And so thank you. (Applause)

* * * * *

CERTIFICATE OF NOTARY PUBLIC

I, Carleton J. Anderson, III do hereby certify that the forgoing electronic file when originally transmitted was reduced to text at my direction; that said transcript is a true record of the proceedings therein referenced; that I am neither counsel for, related to, nor employed by any of the parties to the action in which these proceedings were taken; and, furthermore, that I am neither a relative or employee of any attorney or counsel employed by the parties hereto, nor financially or otherwise interested in the outcome of this action.

/s/Carleton J. Anderson, III

Notary Public in and for the Commonwealth of Virginia

Commission No. 351998

Expires: November 30, 2012