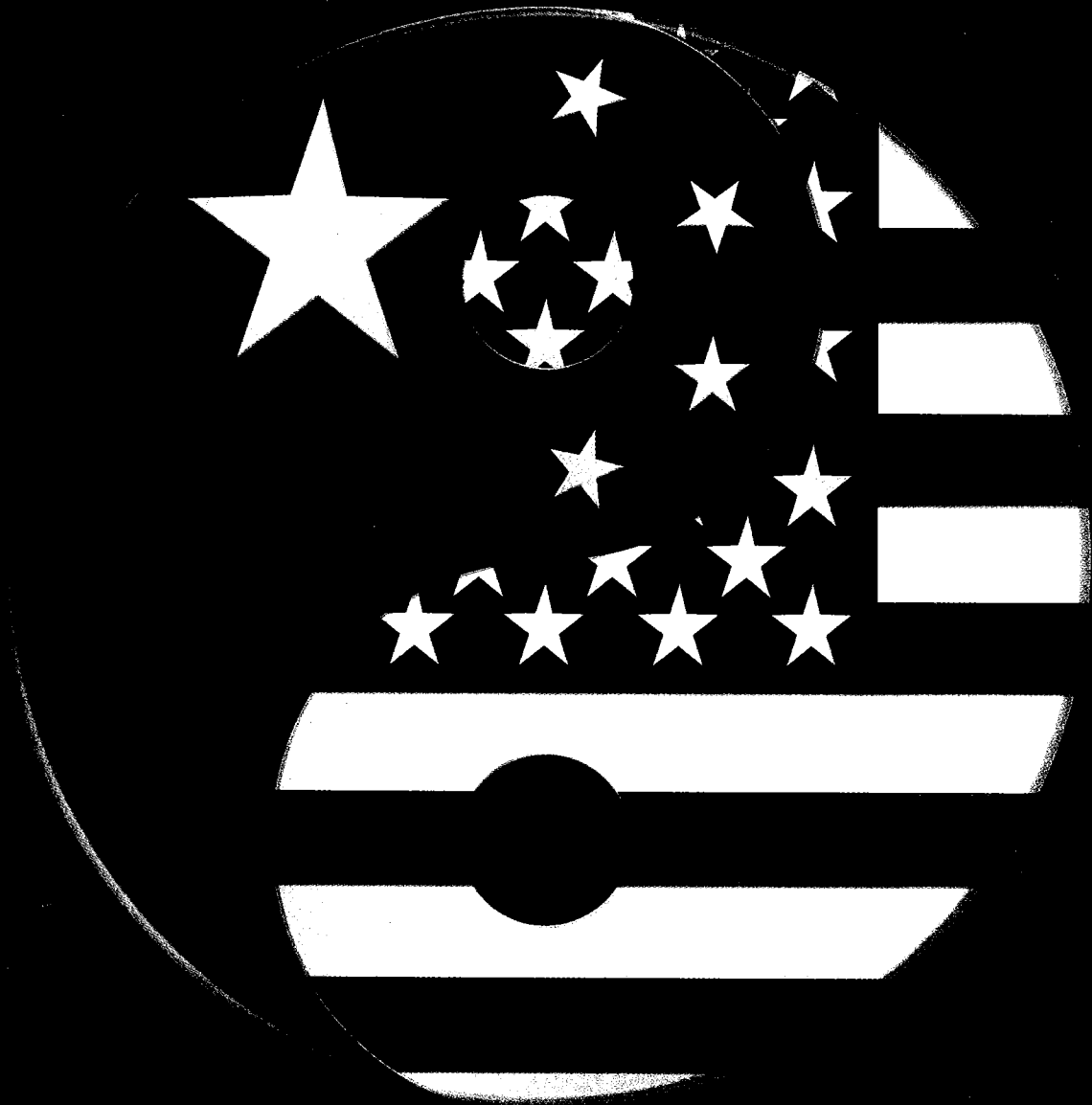


The
Economist



A wary respect

A special report on China and America | October 24th 2009

A wary respect

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Acknowledgments

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A list of sources is at

Economist.com/specialreports

An audio interview with the author is at

Economist.com/audiovideo



America and China need each other, but they are a long way from trusting each other, says James Miles

“OUR future history will be more determined by our position on the Pacific facing China than by our position on the Atlantic facing Europe,” said the American president as he contemplated the extraordinary commercial opportunities that were opening up in Asia. More than a hundred years after Theodore Roosevelt made this prediction, American leaders are again looking across the Pacific to determine their own country's future, and that of the rest of the world. Rather later than Roosevelt expected, China has become an inescapable part of it.

Back in 1905, America was the rising power. Britain, then ruler of the waves, was worrying about losing its supremacy to the upstart. Now it is America that looks uneasily on the rise of a potential challenger. A shared cultural and political heritage helped America to eclipse British power without bloodshed, but the rise of Germany and Japan precipitated global wars. President Barack Obama faces a China that is growing richer and stronger while remaining tenaciously authoritarian. Its rise will be far more nettlesome than that of his own country a century ago.

With America's economy in tatters and China's still growing fast (albeit not as fast as before last year's financial crisis), many politicians and intellectuals in both China and America feel that the balance of power is shifting more rapidly in China's favour. Few expect the turning point to be as

imminent as it was for America in 1905. But recent talk of a “G2” hints at a remarkable shift in the two countries' relative strengths: they are now seen as near-equals whose co-operation is vital to solving the world's problems, from finance to climate change and nuclear proliferation.

Choose your weapons

Next month Mr Obama will make his first ever visit to China. He and his Chinese counterpart Hu Jintao (pictured above) stress the need for co-operation and avoid playing up their simmering trade disputes, fearful of what failure to co-operate could mean. On October 1st China offered a stunning display of the hard edge of its rising power as it paraded its fast-growing military arsenal through Beijing.

The financial crisis has sharpened fears of what Americans often see as another potential threat. China has become the world's biggest lender to America through its purchase of American Treasury securities, which in theory would allow it to wreck the American economy. These fears ignore the value-destroying (and, for China's leaders, politically hugely embarrassing) effect that a sell-off of American debt would have on China's dollar reserves. This special report will explain why China will continue to lend to America, and why the yuan is unlikely to become a reserve currency soon.

When Lawrence Summers was presi- ►►

dent of Harvard University (he is now Mr Obama's chief economic adviser), he once referred to a "balance of financial terror" between America and its foreign creditors, principally China and Japan. That was in 2004, when Japan's holdings were more than four times the size of China's. By September 2008 China had taken the lead. *China Daily*, an official English-language newspaper, said in July that China's massive holdings of US Treasuries meant it could break the dollar's reserve-currency status any time. But it also noted that in effect this was a "foreign-exchange version of the cold-war stalemate based on 'mutually assured destruction'".

China is exploring the rubble of the global economy in hopes of accelerating its own rise. Some Chinese commentators point to the example of the Soviet Union, which exploited Western economic disarray during the Depression to acquire industrial technology from desperate Western sellers. China has long chafed at controls imposed by America on high-technology exports that could be used for military purposes. It sees America's plight as a cue to push for the lifting of such barriers and for Chinese companies to look actively for buying opportunities among America's high-technology industries.

The economic crisis briefly slowed the rapid growth, from a small base, of China's outbound direct investment. Stephen Green of Standard Chartered predicts that this year it could reach about the same level as in 2008 (nearly \$56 billion, which was more than twice as much as the year before). Some Americans worry about China's FDI, just as they once mistakenly did about Japan's buying sprees, but many will welcome the stability and employment that it provides.

China may have growing financial muscle, but it still lags far behind as a technological innovator and creator of global brands. This special report will argue that the United States may have to get used to a bigger Chinese presence on its own soil, including some of its most hallowed turf, such as the car industry. A Chinese man may even get to the moon before another American. But talk of a G2 is highly misleading. By any measure, China's power is still dwarfed by America's.

Authoritarian though China remains, the two countries' economic philosophies are much closer than they used to be. As Yan Xuetong of Tsinghua University puts it, socialism with Chinese characteristics (as the Chinese call their brand of communism) is looking increasingly like capital-



ism with American characteristics. In Mr Yan's view, China's and America's common interest in dealing with the financial crisis will draw them closer together strategically too. Global economic integration, he argues with a hint of resentment, has made China "more willing than before to accept America's dominance".

The China that many American business and political leaders see is one that appears to support the status quo and is keen to engage peacefully with the outside world. But there is another side to the country. Nationalism is a powerful, growing and potentially disruptive force. Many Chinese—even among those who were educated in America—are suspicious of American intentions and resentful of American power. They are easily persuaded that the West, led by the United States, wants to block China's rise.

This year marks the 30th anniversary of the restoration of diplomatic ties between America and China, which proved a dramatic turning point in the cold war. Between the communist victory in 1949 and President Richard Nixon's historic visit to China in 1972 there had been as little contact between the two countries as there is between America and North Korea today. But the eventual disappearance of the two countries' common enemy, the Soviet Union, raised new questions in both countries about why these two ideological rivals should be friends. Mutual economic benefit emerged as a winning answer. More recently, both sides have been trying to reinforce the relationship by stressing that they have a host of new common enemies, from global epidemics to terrorism.

But it is a relationship fraught with contradictions. A senior American official says that some of his country's dealings with China are like those with the European Un-

ion; others resemble those with the old Soviet Union, "depending on what part of the bureaucracy you are dealing with".

Cold-war parallels are most obvious in the military arena. China's military build-up in the past decade has been as spectacular as its economic growth, catalysed by the ever problematic issue of Taiwan, the biggest thorn in the Sino-American relationship. There are growing worries in Washington, DC, that China's military power could challenge America's wider military dominance in the region. China insists there is nothing to worry about. But even if its leadership has no plans to displace American power in Asia, this special report will say that America is right to fret that this could change.

Politically, China is heading for a particularly unsettled period as preparations gather pace for sweeping leadership changes in 2012 and 2013. Mr Hu and the prime minister, Wen Jiabao, will be among many senior politicians due to retire. As America moves towards its own presidential elections in 2012, its domestic politics will complicate matters. Taiwan too will hold presidential polls in 2012 in which China-sceptic politicians will fight to regain power.

Triple hazard

This political uncertainty in all three countries simultaneously will be a big challenge for the relationship between China and America. All three will still be grappling with the aftermath of the global financial crisis. Urban Chinese may be feeling relaxed right now, but there could be trouble ahead. Yu Yongding, a former adviser to China's central bank, says wasteful spending on things like unnecessary infrastructure projects (which is not uncommon in China) could eventually drain the country's fiscal strength and leave it with "no more drivers for growth". In recent weeks even Chinese leaders have begun to sound the occasional note of caution about the stability of China's recovery.

This special report will argue that the next few years could be troubled ones for the bilateral relationship. China, far more than an economically challenged America, is roiled by social tensions. Protests are on the rise, corruption is rampant, crime is surging. The leadership is fearful of its own citizens. Mr Obama is dealing with a China that is at risk of overestimating its strength relative to America's. Its frailties—social, political and economic—could eventually imperil both its own stability and its dealings with the outside world. ■

Round and round it goes

America buys Chinese exports, China buys American Treasuries. Can it continue?

AT ONE stage it all seemed to be working. Even if it appeared a little surreal. China, a developing country, lent vast amounts of money to wealthy America to feed its spending habit. Americans spent the money on Chinese-made goods, sending the dollars back to China, which lent them to America again. But now many talk of a decoupling of the two economies. Niall Ferguson, a Harvard historian who, only a couple of years ago, popularised the term "Chimerica" for the symbiosis between the two, now says it is a marriage headed for the rocks.

China's export figures appeared to support the idea that the country depended hugely on overseas markets for its growth, and on America in particular. By 2007 the value of China's exports amounted to about 36% of its GDP, up from just over 20% in 2001. America was (and remains) second only to the European Union as a customer for Chinese exports, and by far the biggest single country. This year China is on course to regain its position as the biggest supplier of goods to the American market, overtaking Canada. And by September 2008 China had surpassed Japan as the largest holder of US Treasuries (see chart 1), in other words as America's principal creditor.

But the marriage was not quite as close as the headline figures suggested. China certainly helped its exporters by keeping the value of its currency low, buying dollars that were used to buy US Treasuries. Those Treasury holdings helped keep American interest rates low and American consumers spending. But sustaining such growth in exports was not as vital to China as many assumed. The value-added component of its exports accounted for a much smaller share of its GDP than the gross figure because much of the value of Chinese goods consumed in America was created elsewhere. The biggest driver of growth in China was investment, and that has become all the more true as China tries to pump up its economy with nearly \$600 billion in stimulus spending. So although China's economy no longer enjoys the double-digit growth rates of a few years ago, it is on course for 8% growth this year and a similar rate next year, says Nicholas

Lardy of the Peterson Institute for International Economics in Washington, DC, even as America's economy is still trying to emerge from recession.

No wonder that China is feeling a little smug. Millions of migrant workers have been laid off from their jobs in the ravaged export industry, but now a rush of Christmas orders is opening up new opportunities. Some factories even complain of labour shortages. In many cities house prices have been rising rapidly (a new bubble, some fear) and consumer spending—though never as strong as the government would like it to be—is holding up well. Students face a tough job market when they graduate, but that is partly because college enrolment has surged in recent years. Official statistics show that urban unemployment has risen only a whisker since the beginning of the year. Chinese job figures can be unreliable, but anecdotal evidence points the same way.

American officials have developed a tendency to put the two economies on a par, but despite all the talk of a G2 (though not by the two governments themselves) they are far from equal. China's GDP in 2008 was \$4.4 trillion, smaller than Japan's (although next year it could overtake Japan) and less than a third of America's. Albert Keidel, a former Treasury official, says it makes little sense to equate the economies of China and America. "But in terms of influencing China to think that it is a partner with us and therefore it has certain responsibilities and should listen to what

we think is important, that has some salience," he says.

To help cajole China into joining hands with America, Mr Obama has set up a new annual forum called the Strategic and Economic Dialogue that held its first meeting in Washington, DC, in July. The idea was to bring together leading policymakers from both countries to discuss the entire range of problems confronting them. "The pursuit of power among nations must no longer be seen as a zero-sum game," the president said as he addressed the gathering.

You lose, we lose

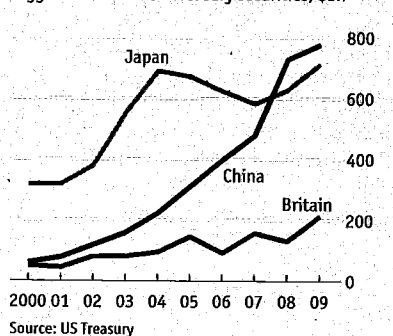
As far as the economy is concerned, China heartily agrees. It may grumble about the dollar's dominance in the global trading system, but it has no desire to pull the rug from under America's economy. A run on the dollar would be a blow to China itself, slashing the value of its stash of over \$800 billion in US Treasuries. Chinese officials also worry openly about a possible resurgence of inflation in America, which would also drive down the value of the dollar. The American budget deficit spooks China, but appears to make little difference to its willingness to lend. China, says Wu Xiaohu of Renmin University, has been "kidnapped" by America's currency. China's purchases of US Treasuries will naturally slow down along with its export growth. But for now the country is still piling them up.

China may dream of a different world in which the yuan ranks alongside the dollar, euro, sterling and yen as a reserve currency. It is beginning to promote use of the yuan instead of the dollar in transactions with some of its trade partners, but it has set no timetable for making its currency convertible. In September it bought \$50 billion in IMF bonds to boost its influence in the institution and strengthen the role of non-dollar currencies (IMF bills are linked to a basket of currencies). But China has not sought to ease the Americans or Europeans out from their dominant roles in the World Bank and the IMF.

When Timothy Geithner, now treasury secretary, said during a Senate confirmation hearing in January that Mr Obama believed China was "manipulating" its cur- ▶▶

Treasury trove

Biggest holders of US Treasury securities, \$bn



►rency to gain an unfair trade advantage, the administration was quick to back away from the remark. The yuan's value has hardly been mentioned in public since. A recent study by the Peterson Institute says that the yuan remains "significantly undervalued", by 15-25% against a weighted average of the currencies used by China's trading partners. But American officials know just how prickly China can get when it is accused of mercantilism.

As Americans save more and buy less from China, America's trade deficit with China—which has been its biggest with any country since 2000—will shrink anyway. But protectionist sentiment in both countries will remain strong. Mr Obama's decision in September to impose punitive tariffs on imports of Chinese steel pipes and tyres infuriated the Chinese government, although it has so far resisted lashing out (summitry with Mr Obama being too

big a party to spoil).

American businessmen, meanwhile, worry no less about protectionism in China. Many saw China's decision in March to reject a takeover bid by Coca-Cola for a Chinese juice company as a bad omen. As Chinese businesses look around America for bargains, they will get a mixed reception: sellers are eager for China's cash, but worried about the survival and security of Brand America. ■

Tug-of-car

Detroit's and China's carmakers both want a piece of the action

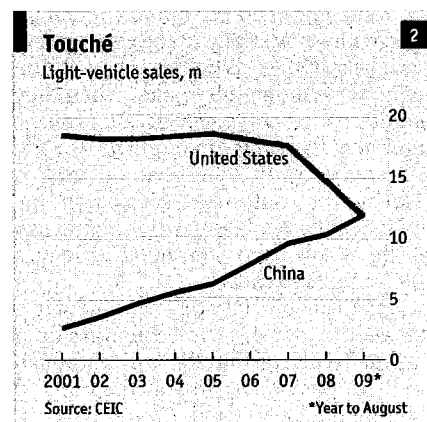
“SHANGHAI, Guangzhou, Changchun, Beijing, Wuhan, Chongqing: six cities with six dreams. But what they really all dream of is the same—Detroit.” So concluded an article on the rival centres of China's fast-growing car industry published by one of China's leading newspapers, *21st Century Business Herald*. That was a long five years ago. Now Detroit dreams of China.

Earlier this year, as the American government was buying 61% of General Motors and 8% of Chrysler to prevent them from collapsing, the two manufacturers' sales in China were rocketing. Indeed, China's car market was overtaking America's in sales volume for the first time (see chart 2), several years earlier than analysts had predicted before the financial crisis. Plummeting demand in the West was to blame.

GM's sales in China in August more than doubled on a year earlier. For 2009 as a whole the company predicted a 40% rise. Sales of all car brands in China in August were about 90% up, helped by a cut in the purchase tax on smaller, more fuel-efficient cars. There is huge pent-up demand as a new middle class takes to the road.

The Chinese government wants to emulate America's rise to industrial glory by making the car industry a pillar of economic growth. This is a boon to foreign carmakers—not least American ones—which have formed joint ventures with Chinese state-owned companies to build their cars in China. The relentless growth of cities and huge government spending on expressways offer prospects for carmakers reminiscent of those in America in the mid-20th century.

The sales figures may be impressive, but the benefits to American car compa-



nies' bottom lines are far less so. One senior manager of a Detroit carmaker says that rather than actual profits, China offers more in the way of psychological solace for companies eager to show they can still do business. The boom in China is generating far less revenue for American car manufacturers than the growth in car sales in Europe did in the 1990s, he notes. The cars selling fastest in China—as the government intended—are the smaller models with the lowest profit margins.

But China still offers huge potential, not only because its citizens will get richer and upgrade their cars, but also eventually—or so China likes to believe—as a base for producing cars at low cost and selling them into developed markets. “The irony is that some of the first cars that the Chinese export might have an American brand name on them,” says Stephen Biegun, a senior manager at Ford.

Another possibility is that some American brand names will become Chinese. Dollar-rich China, encouraged by the fi-

nanical crisis, is telling its companies to look abroad for bargains. A little-known private company from Sichuan Province, Sichuan Tengzhong Heavy Industrial Machinery, earlier this month reached a deal with GM to buy its Hummer brand (subject to Chinese government approval). A state-owned company, Beijing Automotive Industry Holding, is planning to join a Swedish-led consortium in a bid for GM's Saab unit. Geely, a private company, is looking at Ford's Volvo operation. Buying a foreign brand makes sense for Chinese car firms, which have little international reputation or experience of their own. Quality and safety issues have proved enormous barriers for Chinese brands trying to enter Western markets.

Just as Japanese carmakers rattled the American car industry in the 1970s, the arrival of Chinese makers, though not yet imminent, will be upsetting for some when it comes. The United Auto Workers union (UAW), which represents the Big Three's blue-collar car workers, was outraged when GM said earlier this year that it was planning to make the Chevrolet Spark, a subcompact car, in China and ship it to America. Many politicians sided with the union, pointing out that the company was majority-owned by the American government. “If you're going to build them in China, sell them in China,” says the UAW's president, Ron Gettelfinger.

Buy American

Chinese companies buying American ones will also cause anxiety. In 2005 the plan of a Chinese state-owned company, CNOOC, to buy an American oil company, Unocal, sparked widespread fury among American politicians. They worried, mis- ►

▶takenly, that America would lose a strategic asset. CNOOC meekly withdrew its \$18 billion bid. "It's not necessarily the Chinese [government] making decisions," says Ford's Mr Biegun. "It is the Chinese people and Chinese companies." Politicians, however, have so far been muted in their response to the possible sale of Hummer, a gas-guzzling, loss-making brand. These days, what counts is keeping jobs.

Jim Farley, who is in charge of marketing at Ford, says that "over time the whole industry absolutely has to be prepared" for the day when finished cars will be shipped from China to America. The industry should "welcome that with open arms", he insists. Another car executive says it may not make sense to set up dedicated factories in China to serve the American market, but production lines in China could be used to plug gaps in supply that might open up in America.

American consumers might be slow to embrace Chinese-branded vehicles, which so far have made inroads only in emerging markets that care more about price than quality. But the Chinese government sees



Pillars of economic growth

an opportunity in hybrid and other "green" cars, demand for which is likely to grow fast. With its economies of scale and abundant labour, China is hoping to gain an edge in what promises to be a lucrative new industry.

That would help to brighten the environmentally gloomy prospect of a China moving towards American levels of car ownership. Sceptics say China is unlikely

to mandate the use of new fuel technologies so early in the development of its car industry. Others disagree. China, says one American car executive, could leapfrog ahead in adopting cleaner car fuels, especially batteries, for which it already has a strong manufacturing base. "I do think they are going to be formidable competitors," she says. The UAW may one day have to brace itself. ■

The price of cleanliness

China is torn between getting greener and getting richer

THE Taiyanggong Thermal Power Plant in north-east Beijing is delightfully green. Unlike most of China's smoke-belching power stations, it has such low emissions that luxury flats are being built next to it. They are fetching high prices. Owners will look out over something that looks more like a cluster of office buildings (apart from a couple of grey chimneys) than a power plant. The cooling towers, near a grove of date trees and an ornamental pool, look a bit like the Great Wall.

With the help of two natural-gas-fuelled turbines built by America's General Electric, Taiyanggong produces only half the carbon emissions of a coal-burning facility of comparable size in China. It also generates much less smog-forming nitrogen oxide. Its steam supplies heat to 1m homes. When Hillary Clinton visited the power station in February, she called it a "wonderful collaboration" between China and America in clean-energy production. "We need to figure out ways to do more and more of this," Mrs Clinton said. That is where the problems begin.

The Beijing authorities built Taiyanggong to impress the world in the run-up to the Olympic games which opened in the city in August 2008—on the same day that America opened a new embassy in Beijing (heated, American officials say proudly, by Taiyanggong). Some 5,000 workers toiled night and day to deliver on the Chinese government's promise to provide an environmentally friendly power source for the games. Taiyanggong was connected to the grid with nearly eight months to spare.

Money was no object. It was clear that natural gas would be considerably more expensive than coal, the fuel used by most power plants, and American-made state-of-the-art turbines would be far costlier than those made at home. Maintaining the GE machinery would keep running costs high for years to come. But the government was in a high-spending mood, pouring about \$40 billion into an infrastructure makeover for the games.

Now the power station's owners, led by a municipal state-owned company, are struggling to make it work financially.

Luckily for them, Taiyanggong has qualified for funding under the UN's Clean Development Mechanism (CDM), which enables rich countries to offset carbon emissions by paying for carbon cuts in developing ones. Zhang Yandong, a senior manager at the plant, says it will receive about 80m yuan (\$12m) in CDM money this year. Even with this, he says, the plant will at best break even. A CDM project report estimates that it costs 50% more to generate electricity at a plant like Taiyanggong than it does at an equivalent coal-fired facility.

But American officials hope this will change, and that co-operation on climate change will even help strengthen the relationship overall. At the UN in September Mr Obama said America was "determined to act" on climate change. When he visits China next month, the topic will be the centrepiece. He is likely to secure an agreement on greater co-operation over clean-energy development between the two countries. He might even prise out of Mr Hu what he meant when he spoke of a ▶▶

► “significant cut” in China’s carbon intensity (the amount of carbon emitted per unit of GDP) by 2020.

But even if Mr Hu and Mr Obama appear in broad agreement on what needs to be done, persuading politicians and the public in both countries will not be easy. China has set impressive targets but struggles with ill-motivated bureaucrats. In America even lacklustre climate-change legislation now before Congress could founder as Mr Obama devotes political energy to what he clearly sees as a higher priority: health-care reform.

The road to Copenhagen

In Beijing the two presidents will avoid airing public doubts about each other’s countries’ fitness for the task. If China and America—the world’s two biggest greenhouse-gas polluters, which between them account for 40% of the world’s carbon-dioxide emissions—are seen to be in accord, their officials reckon, there will also be a better chance of agreement at the UN climate conference in Copenhagen in December. That meeting is meant to come up with a successor to the Kyoto protocol of 1997, a treaty on cutting carbon emissions that Congress never ratified.

Securing vague agreements will be the easy part. Having recently overtaken America as the world’s biggest carbon emitter (see chart 3), China is anxious not to be singled out as the main obstacle to climate-change prevention. To China’s leaders, image counts for a lot. China will cling to the view (shared by most developing countries) that the developed world bears the main responsibility for dealing with the problem. But it is also keen to co-operate. Cutting the growth of its carbon emissions happens to fit well with China’s longstanding campaign to use energy less wastefully and reduce its dependence on

imported oil (see chart 4). If the rich world, through CDM arrangements, can help China achieve that, so much the better.

What China will want in return is lots of money. Unfortunately for its environment, coal is plentiful and cheap. About 70% of China’s electricity supply comes from coal-fired power stations. So the question is how fast China can introduce technologies to reduce carbon emissions from coal-burning, or else replace coal with cleaner forms of energy, both of which will be expensive. China will demand that developed countries foot the bill and also help provide the technology.

This will be hard for Mr Obama to sell to Congress. Politicians will worry about how to monitor China’s success in achieving its targets. China pledged in 2006 to reduce the amount of energy used per unit of GDP by 20% by the end of this decade. Officials say the country is on track to achieve this. But stimulus spending is flowing into energy-burning industries. In the pursuit of growth local governments are even less inclined to take energy-saving targets seriously. And verifying whether China is meeting its energy targets will be hard. For China to measure its carbon emissions and for America to be satisfied with the results will be even harder. Even a pledge for emissions to peak by 2035 will not go down well in America. Kenneth Lieberthal of the Brookings Institution says China will be under pressure to make it earlier, perhaps 2020 or 2025.

Technology transfer will also be a thorny issue. China resents the idea of American clean-energy companies taking advantage of China’s predicament to profit from their expertise. But American companies will not be keen to hand over advanced technologies without adequate protection for their intellectual-property rights. China’s lack of attention to this area is bitterly resented by many American businesses, not just high-tech ones.

American climate-change experts say there are grounds for optimism that China will do its best. The country’s leaders, they say, are beginning to appreciate how much of a threat climate change poses to China itself. It has taken a while to convince them. In a country where every year hundreds, if not thousands, of people die in natural disasters, crops are devastated by droughts and millions of peasants migrate to cities, the extra disruption and loss of life that global warming might cause have not seemed like pressing concerns. But Mr Lieberthal says leaders now worry that climate change could pose a serious addi-

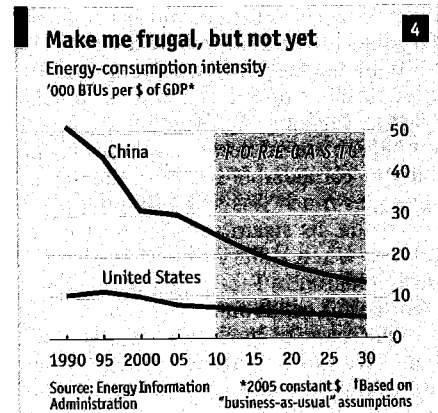
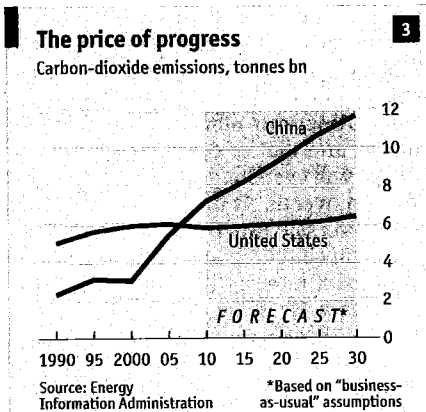
tional threat to stability. For a party that places stability above everything else, this could be a clincher.

China will enjoy the *Schadenfreude* of watching Mr Obama’s struggle with a recalcitrant democracy. The climate-change legislation now before Congress has little chance of being passed by the Senate before the Copenhagen conference even though it was watered down as it passed through the House of Representatives. This will make it difficult for America to claim the moral high ground at Copenhagen. China may even garner more praise.

Whatever accord is reached at Copenhagen, scepticism will still be rife in America about China’s intentions, and in China about America’s willingness to provide the money and technology. At a time when trade friction between China and America is growing, such misgivings could lead to more shouting matches. The climate-change bill threatens to impose carbon tariffs on countries that are deemed not to be doing enough. China will rightly argue that it is doing a lot, but it will worry that Americans will not see it that way.

Mr Hu will also have to watch his own back. Just as in America, implementing carbon-emissions cuts will upset powerful interest groups: fossil-fuel-energy producers, for one. Unless the West, including America, is prepared to help out on a large scale, he will be under pressure to go slow. His decisions on climate change will be a clue to whether domestic or global interests take priority.

Like Mr Obama, he will vacillate. Copenhagen is likely to be just the beginning of a long, hard, struggle between the two countries over what the other is doing. An often defensive and secretive Chinese bureaucracy up against a bewilderingly complex mishmash of competing interests in America will not make for harmony. ■



Overkill

China is piling up more weapons than it appears to need

WHEN Hillary Clinton said in January that America should exercise “smart power”, Chinese officials and commentators pricked up their ears. Here was a neat way of describing, some of them said, what China too was trying to do: find the right mix of military might, cultural influence and economic clout—hard power and soft power—to secure its place in the world. Yet both countries are at risk of dangerously mishandling this exercise in carefully calibrating their dealings with each other.

China’s demonstration of military might and authoritarian muscle on October 1st, its national day, was one recent example of how its judgment can go awry. The parade of thousands of goose-stepping troops through central Beijing, along with military hardware intended mainly to intimidate America and its quasi-ally Taiwan, was a throwback to the imagery of cold-war days. It did not help that dissidents were rounded up and the public kept away from the event (except on television).

Such scenes touch raw nerves in America, where intellectual and political opinion has long been bitterly divided over how to assess China’s rise. Left-wing Democrats, alarmed by China’s human-rights abuses, find themselves in league with right-wing Republicans who see China as a new Soviet Union, to be distrusted and contained. The October 1st extravaganza also worried a third, more centrist, camp: those who see the Communist Party’s resort to nationalism as a sign of its weakness and of China’s vulnerability to upheaval that could have damaging global consequences.

Mr Obama’s smart-power strategy towards China resembles that of his predecessor, George Bush, who after the attacks of September 11th 2001 abandoned talk of China as a “strategic competitor” and sought instead to downplay differences. China, no less smartly, began in 2003 to emerge from its diplomatic shell by organising six-nation talks to deal with the nuclear crisis on the Korean peninsula. By the middle of this decade it had also begun to back away from its belligerent rhetoric on Taiwan (while continuing to amass more weaponry should it ever wish to attack the island). America breathed easier.

The Centre for Strategic and Interna-

tional Studies, a think-tank in Washington, DC, that helped popularise the notion of smart power with a study on American foreign policy in 2007, issued a report in March which drew attention to a “strategic mistrust” between the two countries’ leaders. American policymakers, it said, should start a “new narrative” and show respect for China’s status as a rising power. Mr Obama, who has put more emphasis than Mr Bush did on China as a solver of global problems, appears to agree.

America’s friendly rhetoric may help to secure more constructive thinking in Beijing about issues such as tackling climate change or dealing with North Korea. But the intractable problem of Taiwan will continue to fuel a dangerous escalation of the two countries’ hard-power capabilities with respect to each other. In the realm of soft power (a term defined by Joseph Nye, a Harvard professor and former senior official, as a country’s ability to persuade or influence others without the threat of force), China has only recently begun to play a global part. Its efforts so far, whether in securing oil and mineral deals in Africa or in trying to promote its view of the world through the internet, have often merely raised American hackles.

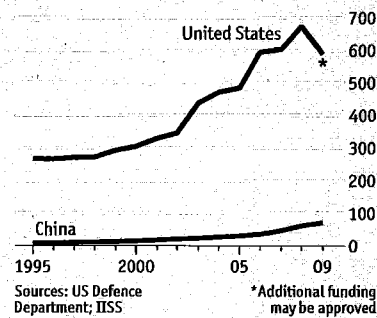
Unlikely but not unthinkable

On the military side, the Pentagon worries that China is acquiring capabilities that go beyond what is needed to deal with possible conflict over Taiwan. China does not speak publicly of displacing American power in Asia. It has good reasons, indeed, to support it, given that America’s presence helps to deter North Korean aggression against South Korea, keep Japan from becoming militarily more assertive and protect shipping lanes in South-East Asia. But China’s military build-up, which began to gather pace in the late 1990s and has shown no sign of slacking, could one day tempt Chinese leaders to think that they could fight and win a war, either over Taiwan or over a host of mostly uninhabited islands whose sovereignty China disputes with countries from Japan to Malaysia.

China’s growing armoury would make it far more difficult for America to respond to a crisis in the Taiwan Strait in the way it

Still a world apart

Defence budget, \$bn



did in 1996 when it sent two aircraft-carrier battle groups close to the island. The Pentagon says China is developing medium-range ballistic missiles that could be guided to their targets far out into the Pacific beyond Taiwan: a clear threat to the American navy. Medium-range missiles are also being targeted at American bases in Japan and Guam. China, says the Pentagon, has the biggest missile programme of any country in the world.

Although it is well aware of the dangers of misunderstandings, China has brushed off repeated American overtures for more dialogue. Talks between the two armed forces typically sputter on for a few months before being called off again by China to express its disapproval of American military support for Taiwan. There have been glimmers of progress. This year multinational anti-piracy operations in the Gulf of Aden (China’s first active naval engagement beyond Asia) saw Chinese and American ships operating in the same zone and communicating with each other in a friendly enough manner.

But Pentagon officials have never been allowed to visit the headquarters of the Chinese armed forces, an underground facility in the Fragrant Hills west of Beijing. Attempts by the Pentagon over the past few years to persuade the chief of China’s strategic nuclear forces to visit America have so far failed (although he has visited other countries). In 2008 the two countries agreed to establish a hotline between their two defence ministries. But for unex-▶▶

plained reasons the two sides did not use it when Chinese boats harassed an American surveillance ship, the *Impeccable*, in the South China Sea in March.

Few expect rapid progress. Dennis Wilder, a former adviser to the National Security Council under President Bush, says there is a dangerous lack of knowledge even about basic issues such as China's nuclear-alert system. China has a few dozen land-based nuclear missiles capable of hitting some or all parts of America and is soon expected to deploy them on submarines. America's nuclear force is far larger, but as Richard Bush and Michael O'Hanlon of the Brookings Institution argue in a book published in 2007, nuclear

war between the two countries over Taiwan is not unimaginable.

No less worrying to the Pentagon is what appears to be a lack of effective communication between the Chinese armed forces and other parts of the bureaucracy. This was evident in April 2001 when an American EP-3 military spyplane hit a Chinese fighter jet off the Chinese coast. American officials believe the crisis was escalated by distorted information that was fed to Chinese leaders by the armed forces before other departments were able to weigh in with sounder analysis. It seemed that the Chinese armed forces did not promptly inform China's foreign ministry about the *Impeccable* incident.

China bristles at any American suggestion that its behaviour could be construed as threatening. America's latest National Intelligence Strategy, the first issued by the Obama administration, makes one brief mention of China, saying that its "increasing natural-resource-focused diplomacy and military modernisation are among the factors making it a complex global challenge." This statement of the obvious was enough to trigger howls of protest. The Chinese foreign ministry called on America to abandon its "cold-war mentality and prejudices". At an annual gathering of regional defence ministers in Singapore earlier this year, a speech by the deputy Chinese chief of staff, Ma Xiaotian, was ►►

A message from Confucius

ON THE ground floor of one of the University of Maryland's redbrick Georgian-style buildings is the small office of the Confucius Institute. When it opened five years ago, it was the first of its kind in America. Now there are more than 60 of them around the country, sponsored by the Chinese government and offering Chinese culture to win hearts and minds.

China's decision to rely on Confucius as the standard-bearer of its soft-power projection is an admission that communism lacks pulling power. Long gone are the days when Chairman Mao was idolised by radicals (and even respected by some mainstream academics) on American university campuses. Mao vilified Confucius as a symbol of the backward conservatism of pre-communist China. Now the philosopher, who lived in the 6th century BC, has been recast as a promoter of peace and harmony: just the way President Hu Jintao wants to be seen. Li Changchun, a party boss, described the Confucius Institutes as "an important part of China's overseas propaganda set-up".

China's partial financial backing, its hands-off approach to management and the huge unmet demand in many countries for Chinese-language tuition have helped Confucius Institutes embed themselves in universities that might have been suspicious. The University of Maryland's institute does not offer courses that count towards degrees (and nor do many



Back in fashion

of the others). It helps with Chinese-language teaching in the wider community, not just on campus. The director, Chuan Sheng Liu, is appointed by the university, as most of them are.

There are occasional hints of politics. Earlier this year the University of Maryland's institute organised an exhibition of photographs from the Tibetan plateau. At an opening ceremony a senior Chinese diplomat made a speech criticising the Dalai Lama. The pictures, he said, showed

New ways of projecting soft power

the "remarkable social changes and improvement" in Tibet under Chinese rule and demonstrated that Tibet had been "part of China since ancient times". But the website of the Confucius Institute in Edinburgh promotes a talk by a dissident Chinese author whose works are banned in China. Even the Pentagon has been helping to fund some language courses at Confucius Institutes under the National Security Language Initiative, launched by George Bush in 2006 to promote the study of "critical-need" languages.

The late Samuel Huntington, in his 1996 bestseller "The Clash of Civilisations and the Remaking of World Order", describes a Confucian world, with China at its centre, that will find itself in growing conflict with the West. This is the kind of view that the Confucius Institutes are intended to dispel. Mr Liu, a long-time physics professor at the university, says his mission is to promote cultural understanding. He speaks of the "amazing similarity" between Confucian teachings and George Washington's etiquette guide, "Rules of Civility and Decent Behaviour in Company and Conversation".

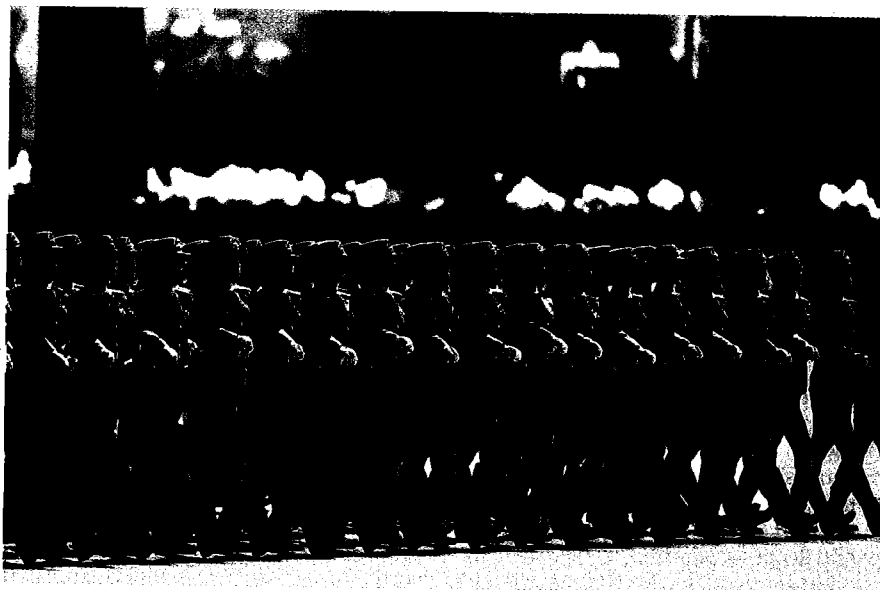
Some American officials grumble that Chinese universities are far less receptive to America's cultural-promotion efforts than American ones are to China's. But as one comforts himself, "if you're in a system that's that paranoid, your soft power is self-limited."

► sprinkled with critical allusions to American "cold-war" behaviour in Asia.

China has reason to feel uncomfortable about the imbalance between its own military power and America's. American ships and spy planes claim the right to operate only 12 nautical miles from the Chinese coast (a boundary observed by Soviet and American military craft off each other's coasts during the cold war). They routinely come closer than the 200-mile boundary that China insists on. China does not have the means to project its power anything like as close to America's shore, and shrewdly refrains from suggesting that it would like to.

But some Americans worry that China could make a cold war with America a self-fulfilling prophecy by trying to acquire more of the trappings of a global military power. For example, China is quietly developing its first aircraft-carrier. The Pentagon reckons the country is unlikely to have one in operation before 2015, but is considering building at least two by 2020, along with associated vessels. "The Indians have one, the Italians have one, so why can't China have one?" asks a Chinese general.

Pentagon officials profess not to worry. America's navy would be well equipped to deal with a Chinese carrier-borne force, particularly one with little experience (it would be an "easy target", says one former senior official in the Bush administration). But China's deployment of a carrier would send a powerful signal that its naval interests are no longer confined mainly to coastal defence. A senior Chinese officer once quipped to Admiral Timothy Keating, who is about to retire as America's top com-



A sight to terrify the enemy

mander in the Pacific, that when China has aircraft-carriers the two countries should draw a line down the middle of the Pacific through Hawaii to define their spheres of operation. Mr Keating politely declined.

Culture wars

On the soft-power side, China is slowly learning. After much complaining from Western politicians and NGOs, it has used its considerable economic clout to give Sudan and Myanmar at least little nudges towards accommodating Western concerns in those countries (less so, however, in the case of Iran). Soft power was mentioned for the first time by a Chinese leader in public in 2007. Culture, said Mr Hu (oblivious, it seemed, of the cold-war overtones of his remarks), was of growing significance in the "competition in overall national strength". China should therefore "enhance culture as part of the soft power of our country".

A cursory glance at the streets and shops of Chinese cities suggests what Mr Hu may have had in mind: the all-pervasiveness of American brands and cultural products, from Coca-Cola to (pirated) boxed sets of a comedy series, "Friends", from Kentucky Fried Chicken to Starbucks. America's intellectual drawing power is evident in the queues of students waiting for visas at the American embassy: in the 2007-08 academic year more than 81,000 Chinese were studying in American colleges. Such exposure to American ideas does not always work in America's favour. Many of the nationalists who have staged protests against America in recent years have been members of an internet-savvy generation immersed in American popular culture. But the Chinese government now hopes that by taking its own cultural message to foreigners it can help to convince them that China's rise is nothing to be feared (see box, previous page). ■

Sore points

How Taiwan and North Korea complicate the Sino-American relationship

TAIWAN, as Chinese officials never tire of reminding their American counterparts, is the most important and sensitive issue in the two countries' relationship. In the mid-1990s the two nuclear-armed states inched to the brink of war over the island. Since then Taiwan has been the pretext for a massive military build-up by China. Pragmatism has so far restrained China's nationalist instincts, but for how long?

Both China and America were relieved that elections in Taiwan in March 2008 returned a China-friendly president, Ma

Ying-jeou. For nearly 15 years Taiwan's transition to democracy, and the growth of Taiwanese nationalism which it fostered, had been adding dangerous unpredictability to cross-strait relations. America had been getting fed up with Mr Ma's predecessor, Chen Shui-bian of the Democratic Progressive Party, who revelled in riling China.

China has offered Mr Ma some carrots. In May it allowed Taiwan to send a delegation to the World Health Assembly, the WHO's governing body—the first time it had agreed to Taiwan taking part in any UN

activity. Recently China criticised CNN for running an online poll asking whether Mr Ma should step down over his handling of the aftermath of a typhoon in August that killed hundreds of people. Its response to Mr Ma's decision later in August to allow the Dalai Lama to visit Taiwan to pray for the dead was unusually muted. Mr Ma, notes Sun Yan of Peking University approvingly, bows regularly before a statue of Sun Yat-sen, a pre-communist revolutionary who is also held in reverence by China's leaders. This, she says, "suggests in ►

► his heart he thinks of himself as Chinese”.

But Taiwan will remain a problem for China and America. Mr Chen was sentenced to life in prison for corruption in September, but his pro-independence views still enjoy a vocal, if minority, backing. Mr Ma's popularity has been badly dented by the typhoon response. Taiwan's economic malaise will not help. The Democratic Progressive Party has been in disarray since its defeat in last year's election, but it might still be a strong contender in the next presidential polls in 2012. That would deeply worry the two big powers.

More immediately, Mr Obama needs to think about arms sales to the island. Mr Ma says he wants new F-16 fighter jets. “We simply want to maintain the military balance” with China, he says, by replacing ageing military hardware. Mr Obama, anxious to secure Chinese co-operation on a range of issues, will want to tread warily, but Taiwan has many friends in Congress.

Mr Obama could argue that the improvement in cross-strait political relations reduces the need to sell more weapons to Taiwan. China will certainly argue, with some justification, that selling Taiwan more advanced F-16s is hardly in keeping with what America promised in a 1982 joint communiqué with China: that America's arms sales to Taiwan would not exceed “either in qualitative or in quantitative terms” the level of those supplied in the three years prior to the agreement.

American law complicates the issue. The Taiwan Relations act of 1979 requires the administration to arm Taiwan sufficiently to defend itself. In 1992 President George Bush senior agreed to sell the island 150 F-16s, a package worth vastly more than the arms America had sold Taiwan annually since the beginning of the previous decade. China, which was far less powerful then, dragged its heels for a while in international arms-control talks. Today it might respond more robustly.

The North Korean conundrum

Military contacts with the Pentagon would be an obvious first casualty. But China might also become less co-operative in dealing with another issue of huge importance to American security: North Korea. China is an enthusiastic organiser of the six-party-talks process that brings together the two countries, both Koreas and Japan and Russia to discuss ways of rolling back North Korea's nuclear programme. The talks, which began in 2003 but are now on hold because North Korea is angry about Chinese-backed sanctions, have helped

China ingratiate itself with America. Victor Cha, who was Mr Bush's top adviser on Korean affairs and a one-time participant in the talks, describes them as “the only thing they [the Chinese] have ever contributed to the international system”. But China still would like to keep the status quo on the Korean peninsula. Even a nuclear-armed North Korea it sees as less threatening than a North Korea in political meltdown or, worse still, one occupied by American troops.

If China and America have talked about how to handle a political collapse in North Korea, they have managed to keep it secret. Mr Cha says China has shown interest in informal low-level discussions. But



Spotting trouble on the border

without top-level agreement there remains a considerable risk that the Chinese and American armed forces could find themselves drawn into a North Korean political vacuum, with little knowledge of each other's intentions.

China at the very least would want to establish a buffer on the North Korean side of its border with the country in order to stop a flood of refugees. The Americans would want to secure North Korea's chemical and nuclear weapons, some of which are stored near the Chinese border. “How will you get there, will you fight your way there?” asks a senior Chinese officer. China and America, he says, will have to co-operate in order to “prevent another war”.

Shen Dingli of Fudan University in Shanghai argued in an essay in 2006 that from China's strategic perspective, North

Korea and Taiwan were “intrinsicly linked”. As long as China worried about American intervention in the Taiwan Strait, he said, it would value North Korea's role in pinning down American forces in the region, so regime change in the North would be “unacceptable” to China.

For all China's rhetoric about the central importance of Taiwan (and constant whispering to Western officials that any Chinese leader seen as “losing” Taiwan would be overthrown in an instant), the country is reassuringly careful to avoid letting the issue become prey to Chinese public sentiment. Lin Chong-pin, a former Taiwanese deputy defence minister, says that as early as 2006, two years before Mr Ma took office, China had decided that it was “cheaper to buy Taiwan than to attack Taiwan”. Chinese officials would certainly worry about public reaction in China if it were to lose a war over the island, as well as about the long-term viability of controlling Taiwan, noting that the wars in Iraq and Afghanistan have shown that even a superpower can find it difficult to impose its will on occupied countries.

Mr Ma himself plays down the worries about the growth of Chinese nationalism and its potential to disrupt the region's stability. He says he was “quite startled” last year when China reached an agreement with its hitherto arch-rival Japan on joint exploration of disputed gasfields in the East China Sea. Relations between China and Japan, which is a bigger *bête noire* to Chinese nationalists even than America, have improved “beyond my imagination”, Mr Ma says.

But others worry that Chinese nationalism is dangerously unpredictable. Susan Shirk, a former senior State Department official in the Clinton administration, argued in her 2007 book “China: Fragile Superpower” that “the more developed and prosperous China becomes, the more insecure and threatened” China's leaders feel. China's “emotional responses” to external crises “may undermine its more moderate aims and get it, and us, into trouble”.

The confluence of political uncertainty in the region early in the next decade makes such advice worth heeding. Taiwan's presidential polls in March 2012, China's change of leadership in the autumn of that year and American presidential elections in November will create fertile ground for emotional responses in all three capitals. The poor health of North Korea's leader, Kim Jong Il, adds a wild card. Mr Obama would do well to keep the dialogue with China wide open. ■

Aiming high

China is moving heaven and earth to put a man on the moon

FIELDS of peanuts and paddy, water buffaloes, deserted beaches, coconut trees and the odd building site are about all there is to see for now at what will eventually become one of the world's most important centres for space exploration. Very few people outside China have heard of the town of Wenchang on China's tropical island of Hainan, but in a mere four years, Chinese officials say, it will become "China's Kennedy Space Centre". It is from here, eventually, that China's first man on the moon is likely to take off.

Just as President Kennedy aimed for the moon to boost American morale in a struggle for supremacy with the Soviet Union, Chinese officials now see a Chinese moon landing as a way to bolster patriotism (although no formal target date has been declared yet). On the streets of Wenchang, whose sole (non-astronautical) claim to fame at the moment is a form of boiled chicken, the authorities are already trying to get the public in the mood. "Building a Space Centre, Take-Off for Wenchang's Economy", says one slogan against a background of waves crashing on the town's sun-soaked shore. In China money talks just as loudly as appeals to nationalist

pride, despite Wenchang's languid air.

China already has three space centres: Taiyuan in the north, Xichang in the south-west and Jiuquan in the north-west. Jiuquan earned a name for itself by launching China's first man into orbit in 2003, followed in 2005 by a two-man crew and last year by a three-man mission, including China's first spacewalk. But these three facilities are in remote locations deep inland, reflecting China's secretive approach to space flight, a venture under the control of the armed forces. The Wenchang centre will have a space theme park and beach resorts right next to it. China's space programme is at last coming out.

America in particular will turn its eyes on Wenchang as China gets ready to shoot for the moon. No Chinese official, any more than anyone at NASA, would dream of talking of a space race between the two countries. That would smack too much of cold-war rivalry. But in 2007 Mike Griffin, then NASA's chief administrator, said he believed China would be the first country to go back to the moon and that "Americans will not like it."

The plan is to open the new launch centre in 2013 (good timing for China's next

generation of leaders who will want to start their terms on an inspirational note). Some time in the following year China's new *Long March 5* rocket is due to be ready. This will be the workhorse of China's lunar programme. Chinese press reports have suggested that a manned lunar landing could take place around 2020, preceded by an unmanned mission that would return lunar samples to Earth. Unlike America, which is dithering over its plans to return to the moon, China does not appear troubled by financial constraints. Little is revealed of what China's space programme actually costs.

A race of sorts

A Chinese moon landing might chip away at America's sense of its scientific superiority, adding to the worries that were aroused in 2005 when a panel commissioned by Congress gave warning that America was losing its technological edge. The panel cited statistics showing that China produces 600,000 engineering graduates a year against America's 70,000 (though a detailed report published by the panel two years later gave a far narrower gap and questioned whether degrees from the two countries were comparable).

Even before China gets to the moon, it aims to have a rudimentary space station of its own. The first orbiting module (*Tiangong*, or *Heavenly Palace*), which will be used to gain docking experience for the space-station project, will be launched as early as next year. Work on the station itself could begin in 2015, Chinese media say.

When the first *Long March 5* is delivered to Wenchang in 2014, America may not even have a space-launch vehicle of its own. Unless Mr Obama decides otherwise, the Space Shuttle will retire next year. Its successor, the *Ares* rocket, is not due to be put into service until 2015. Some scholars in America see this gap in their country's launch capability as an opportunity to reach out to China. The current plan is to rely mainly on Russian and commercial American launch services to get Americans to the International Space Station (ISS). The relationship with Russia can be tricky, as the invasion of Georgia last year demonstrated. Teaming up with China ►►



The start of something big at Wenchang

► would help spread the risk.

But the prospects are dim. Many American officials are still seething at China's test of an anti-satellite missile in 2007. It blew up an ageing Chinese weather satellite, leaving thousands of pieces of debris in orbit that pose considerable danger to other space-based equipment (a small chunk came close to the ISS in September). Even if the Americans wanted to get Chinese help with the ISS project, they would have to get agreement from other ISS partners. The

Russians might object to the introduction of a competitor to their space-transport service. Japan has similar ambitions, and launched its first unmanned spacecraft to the ISS in September. A NASA official says that any co-operation would require "total transparency" from the Chinese. This would include allowing the Americans to go to China's launch-control centre and get to know the nuts and bolts of its launch vehicle. There seems little chance of this.

But the Americans hardly have to wor-

ry that the Chinese are about to surpass them, as they certainly did in 1957 when the Soviet Union became the first to put a satellite into orbit. Jiao Weixin of Peking University says China's space-exploration capabilities are 30 years behind America's. A billboard on a main thoroughfare in Wenchang tries to whip up space excitement with a huge picture of a launch pad at take-off. It shows flames pouring from boosters attached to what is clearly America's very own Space Shuttle. ■

The rich scent of freedom

Will a wealthier China become less authoritarian?

FOR Americans, the psychological tremors of a Chinese moon walk could coincide with another shock. Some time in the next 20 years, if China's growth stays on course, its economy will overtake America's to become the largest in the world.

By the 2020s China's middle class, today in its toddler phase, will be striding into maturity. And by 2050, some economists predict, China's economy will be double the size of America's at current exchange rates. As with China's space efforts, there will be less to this than meets the eye. In 2020 income per person in America will still be four times China's, and vast swathes of the Chinese countryside will look much the same as they do now.

The numbers may say little about the relative strength of China and America, but they will raise big questions about China itself. With the growth of a middle class, many observers have long believed, the country's politics will change too. Henry Rowen of Stanford University has predicted that by 2020 Freedom House, an American NGO, will rate China as "partly free" in its annual country rankings (putting it in the same category as relatively open but not fully democratic societies such as Singapore and Hong Kong). Freedom House currently rates China as "not free", one of 42 such countries in 2009.

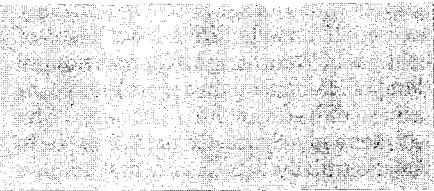
For China, which routinely imprisons dissidents, heavily censors the media, bans any opposition to the Communist Party, bars citizens from electing the country's leaders and officially allows religious activity only in places of worship controlled by the government, this would be a big step forward. Mr Rowen bases his optimism on the numbers. By 2020, he reck-

ons, China's GDP per person at 1998 purchasing-power parity will be over \$7,500. In 1998 all but three of the 31 countries above this level of GDP per person were rated as free. People who live in rich countries (oil-rich ones notably excepted) generally enjoy high levels of political rights and civil liberties, Mr Rowen concludes.

But what if he is wrong? An unsettling possibility for America is that China could grow richer and yet remain authoritarian. In his book, "The China Fantasy: Why Capitalism Will Not Bring Democracy to China", James Mann, an American journalist, argues that his countrymen like to believe they are changing China and that the Chinese are becoming Americanised. "These assumptions have never been borne out in the past," he writes. American political debate tends to concentrate on two scenarios: the gradual liberalisation of China and, occasionally, the possibility of political upheaval there. A third, highly plausible scenario—that there will be no real political change—is also worth considering, says Mr Mann. American officials have often said that their country's trade and engagement with China would help to change it politically, but they may have been mistaken.

Unchanged, and yet changing

Mr Mann may have understated the extent of recent changes in China. Its political institutions and its treatment of organised opposition to the party remain unaltered. But property rights, which hardly existed in China until the 1990s, have widely taken hold. Citizens protest against forced evictions from their homes to make way for development. A new army of private lawyers take on the state in court (and usually



Not happy, and not afraid to protest

lose, but at least they try). The middle class, armed with the internet (users of which remain a step ahead of censors), demands, and sometimes gets, redress for abuses of power by local governments.

But for a disconcertingly large number of urban Chinese, authoritarianism has its attractions. The government's swift response to the financial crisis—a huge stimulus package adopted without any reference to legislators—has reinforced this view. Chinese often say local officials are corrupt and uncaring, but describe the party leadership as well-intentioned and capable. There are no dissidents who are household names across the country. "In ►

► this financial crisis, China's political system has proved no worse than America's," says Yang Fan, an economist.

It is becoming increasingly possible to imagine that when China puts a man on the moon and surpasses the output of America's economy, it will still be a one-party state that brooks no organised opposition. For America this should be cause for concern. The resilience of Chinese authoritarianism will inspire dictators around the world. It will frustrate America's efforts to cajole China into using its soft power to intervene more actively in humanitarian crises. China may be shifting slightly away from its lie-low policy in international affairs; its willingness to engage in anti-piracy efforts off Somalia has been praised in Washington, DC. But as an authoritarian country it will remain fearful of setting a precedent that could justify Western "meddling" in China's own internal problems.

Mr Obama's predecessors found themselves having to backtrack. President Clinton realised soon after taking office in 1993 that America's attempts to force change in a then more fragile China were of no avail. In not much more than a year he abandoned his attempt to make the annual renewal of China's low-tariff trade terms dependent on China's progress with human-

rights protection. Mr Bush in his second inaugural speech in 2005 said it was America's policy to support democratic movements everywhere, "with the ultimate goal of ending tyranny". During his visit to China later that year China rounded up dissidents or put them under house arrest. Mr Bush, anxious not to upset his hosts, remained tight-lipped in public.

One argument commonly heard for keeping quiet is that criticism of China's human-rights policies, especially in public, plays into the hands of nationalist hardliners. But if America is ill-equipped to influence the development of democracy in China, it is almost as impotent when it comes to managing the growth of nationalism. Trade between the two countries more than tripled in value between 2000 and 2008, with a huge surplus in China's favour. Mr Bush kept human-rights differences largely hidden. Yet virulent anti-Western nationalism erupted in China after the protests in Tibet in March 2008, with America and its allies accused of trying to break up the country. Some Western journalists received death threats.

As president, Mr Obama has refrained from being too ambitious about human rights in China. He declined to meet the Dalai Lama during the Tibetan leader's Oc-

tober visit to Washington, DC, an unusual break from past presidential practice. He preferred to wait until some time after his trip to Beijing. Mr Obama's administration has even signalled that human rights are not among its top priorities. Before her trip to Beijing in February, Mrs Clinton said that pressing China on human rights must not interfere with talks on the economic crisis, climate change and security issues.

You never know

China is well aware that its critics' priorities are shifting. A senior American official says the environment has become a greater threat to China's international image than repression in Tibet. Chinese leaders might well interpret this as meaning that a greener China could get away with locking up dissidents. But human-rights differences with China could suddenly cloud the relationship, just as they did in the final months of Mr Bush's presidency with the upheaval in Tibet. Mr Bush decided not to boycott the opening ceremony of the Olympic games, as some NGOs and politicians had suggested he should. They included Mr Obama and Mrs Clinton, both then candidates for the Democratic nomination. China's stubborn resistance to political change could still embarrass them. ■

A dragon of many colours

America will have to get along with China. But which China will it be?

“OUR policy has succeeded remarkably well: the dragon emerged and joined the world.” So said Robert Zoellick, then deputy secretary of state, in 2005, in a speech suffused with confidence in America's ability to shape China's progress. But, said Mr Zoellick, who is now president of the World Bank, China's behaviour on the world stage left room for improvement: the country needed to become a “responsible stakeholder” in the global community.

This anodyne catchphrase helped to redefine the two countries' relationship. It was, in effect, an admission that America could cohabit with a powerful China. Many in his audience of American businessmen in New York, however, felt uneasy. As Mr Zoellick recalls, they saw his remarks as “too harsh and demanding”. Had he delivered the same speech to the political elite in Washington, DC, he reckons, he might have been criticised for being too

soft. But China, despite being a bit unsure at first how to translate the word “stakeholder” (a term for which a standard rendering in Chinese had yet to be found), quickly warmed to the new formulation.

It was not then obvious to Chinese officials that America really could accept the rise of China as it was, a one-party system controlled by communists. China saw the invasion of Iraq in 2003 and the “colour revolutions” against authoritarian governments in former Soviet-block countries as evidence that America wanted to go it alone as a superpower and was bent on recreating the world in its own image. The Chinese media accused America of instigating the pro-democracy movements in Georgia, Ukraine and on China's doorstep in Kyrgyzstan. A young Chinese diplomat proudly told Mr Zoellick that he spent until 4 o'clock the next morning explaining the significance of the New York speech in a

cable to Beijing. “The Chinese saw it as just about right,” says Mr Zoellick.

Mr Obama's administration has made less use of the “responsible stakeholder” tag, but its strategy is clearly the same. Mr Obama and Mr Hu have agreed to forge what they call a “positive, co-operative and comprehensive relationship” (a step up, presumably, from what was previously dubbed a “candid, constructive and co-operative relationship”). Notwithstanding the tyre tariffs, Mr Obama can expect a warm reception in Beijing next month. China's leaders see acceptance by America as a boost to their legitimacy at home.

Prepare for all eventualities

“We no longer have the luxury of not getting along with China,” John Podesta told a congressional committee in September. Mr Podesta was the head of Mr Obama's transition team and now heads the Centre ►►

► for American Progress, a think-tank close to the Obama White House. He said it was time to move beyond the past strategy of “engage and hedge” and adopt one that “maximises opportunity but also manages risk”. But American respect and goodwill, as this special report has argued, cannot be relied upon to ensure that relations remain on solid ground. And whether called hedging or managing risk, America has no choice but to prepare for the possibility that China might one day threaten American security.

The risk is not that China’s current leaders might one day discard their pragmatism and march into all-out conflict with America, whether in the economic or military sphere. It is rather the instability of China itself. So far the most disruptive influence on Sino-American relations has been public and political opinion in America. China’s bloody crackdown in Tiananmen Square in 1989 was hugely destabilising, but consistent with a time-honoured approach to political threats.

What do the Chinese think?

Increasingly, however, public opinion in China will play a role as well. Chinese censors ensure that criticisms of the Communist Party quickly disappear from the internet, but xenophobic opinions are usually left untouched. The internet magnifies nationalist sentiment in China, sometimes even putting the government on the back foot. Such sentiment is invariably hostile to America.

Elite-level politics is another worrying factor. Over the past 30 years leadership changes in China have had remarkably little effect on the relationship between the two countries, but there have been occasional deviations. The Taiwan Strait crisis of 1995-96 erupted at a time of heightened political uncertainty in China, with Deng Xiaoping’s health fading and his relatively inexperienced successor, Jiang Zemin, trying to burnish his credentials. The spy-plane crisis of 2001, which resulted in a tense stand-off as China detained 24 American crewmen for 11 days, broke close to a period of leadership transition.

China’s preparations for another change at the top in 2012 and 2013 appear to be in hand, but America would be wise to be cautious. The workings of China’s leadership remain as much of a mystery to outsiders as they were when China and America established diplomatic relations in 1979, if not more so. Mr Hu is more cautious in his meetings with foreigners than his predecessors were (which may be a



Xi Jinping, princeling-in-waiting

blessing for Mr Obama, probably safe from Mr Jiang’s predilection for bursting into song). Leaks from politburo-level deliberations, few and far between at the best of times, are now almost unheard of.

Vice-President Xi Jinping looks the most likely man to take over, with Li Keqiang as his prime minister. Mr Xi is a “princeling”, as the descendants of communist China’s revolutionary founders are often called. As the party chief of Zhejiang Province from 2003 to 2007 he promoted greater openness in grassroots government. But in February a widely circulated video clip of Mr Xi accusing “well-fed foreigners with nothing better to do” of interfering in China’s affairs suggested that he might incline towards nationalist crowd-pleasing. And the succession is still not certain. Party leaders meeting in Beijing in September failed to announce Mr Xi’s widely expected promotion as deputy commander-in-chief of the armed forces. He currently has no military post.

It is reasonable to think that China may well get richer yet stay authoritarian, at least for the next 10-20 years. But there are

two other scenarios that are worth thinking about. One is that China might in fact become more democratic. A politically more liberal China would put enormous strains on the multi-ethnic empire that China’s communists inherited from imperial times. Minorities across the Tibetan plateau and in Xinjiang would step up demands for greater autonomy. That, in turn, would jeopardise either China’s democratic development or the unity of the state. And a more democratic China would be unlikely to countenance the permanent separation of Taiwan. It might even pursue irredentist claims more aggressively.

The other possibility is that China might be convulsed by the same kind of tumult that occurred in much of the rest of the communist world two decades ago. This would be a nightmare for America. In such a scenario, the conservative and inward-looking armed forces would play a critical role. As President Clinton put it in 1999, “as we focus on the potential challenge that a strong China could present to the United States in the future, let us not forget the risk of a weak China, beset by internal conflict, social dislocation and criminal activity; becoming a vast zone of instability in Asia.” Ten years and much economic growth later, his words are still worth heeding.

The threat posed by China is not (yet, anyway) one of military expansion but one of great new uncertainty looming over the global order. Mr Obama will need to keep reminding China that America would be irresponsible not to prepare for the worst even as it hopes for the best. Chinese leaders would be wise to be just as cautious about their own future. ■

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