

Iran Nuclear Deal

A New Day in Global Governance



CHINA^{US} Focus

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Editor's Note

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The historic agreement on the Iranian nuclear issue is an encouraging event for the development of China-U.S. relations, at a time when growing pessimism dominates American media and academic communities. Such cooperation between China and the U.S. will help improve the overall bilateral ties if the two countries forge practical collaboration on a number of the “global governance” issues.

In our cover story, Yang Jiemian, President Emeritus of Shanghai Institutes for International Studies, hails that the cooperation between China and the U.S. in the Middle East affairs reflects the potential for a “new model of major country relations.”

China's A-share market has been extremely volatile in recent weeks, making headlines throughout the world. Chinese economist Yi Xianrong assures in his article, “After Corrections, China's A-Shares Resurgent,” that the upswing in the Chinese stock market will continue in the second half of the year.

On the South China Sea issue, we selected articles by Wu Shicun, President of China Institute of South China Sea Studies; Doug Bandow, Senior Fellow at Cato Institute; and Joan Johnson-Freese, Professor at U.S. Naval War College. All three authors urge the decision-makers in both countries to try their best to prevent conflicts by avoiding miscalculation and misjudgment. Professor Johnson-Freese warns, “If one scorpion stings the other, both will die.”

In his article titled, “Thinking Beyond Conflict,” Zhou Wenzhong, former Chinese Ambassador to the U.S., calls for both sides to focus on the big picture, discard a confrontational approach, and improve internal coordination.

Wang Dong from Peking University observes that the desire for an improved China-U.S. relationship is already winning the hearts and minds of ordinary people on both sides of the Pacific. “They are a critical foundation of this important relationship,” claims Wang.

Commenting on China's forthcoming events commemorating the 70th anniversary of World War II, Chinese scholar Yu Sui believes that China will have an opportunity to strengthen mutual trust with its wartime allies, including the U.S.

Lastly, we include an article by Curtis Chin, former U.S. Ambassador to the Asian Development Bank. He predicts the Asian Infrastructure Investment Bank (AIIB) will help finance billions in infrastructure projects around Asia and also challenge the existing financial institutions.

Chinese President Xi Jinping will pay an official state visit to the U.S. in September this year, which will be the main theme of our October issue. In the meantime, please keep up to date with all the latest articles on ChinaUSFocus.com!

Thank you.



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Iran Nuclear Deal: A New Day in 'Global Governance'

As the world becomes increasingly multi-polar, there has been much discussion of a new model for major-power relations and how they might shape a modern world order. The recent breakthrough in negotiations with Iran shows that the idea is moving from rhetoric to reality.

A historic agreement was reached between Iran and Britain, China, France, Germany, Russia and the United States (“P5+1”) over the Iranian nuclear issue on July 14. A week later, President Xi Jinping and U.S. President Barack Obama highlighted their nations’ cooperation in resolving the Iranian nuclear issue, which may herald a new way of doing business on the stage of global politics.

President Obama appreciated China’s contribution to the historic agreement, praising China for its very important role in the process. The Chinese president pointed out that China and the United States had close communication and coordination during the talks – testimony to the two nations’ decision to jointly build a New Model of Major Country Relationship (NMMCR). Indeed, China put its interaction with the United States over and related to the Middle East affairs within the

NMMCR framework.

The new relationship model was endorsed by both presidents during their informal summit at Sunnylands, California in June 2013. Over the past two years and more, the NMMCR has been reflected in some encouraging developments in the China-U.S. interactions over and related to the Middle East affairs.

First of all, China and the United States have more constructive interaction in the Middle East than in some other regions of the world. The two countries have overlapping interests in maintaining peace and stability of the whole region in general and the Gulf sub-region in particular: managing the Iranian nuclear issue, continuing the Palestine -Israel peace process, safeguarding vital energy supply lines and supporting orderly and peaceful transitions of political, social and economic systems in the countries concerned.



Yang Jiemian

*President Emeritus, Shanghai
Institute for Int'l Studies*

Moreover, both countries are facing intensified challenges of international terrorism and extremism given their trends towards re-groupings, so-called state building and the accompanying wars and violence. However, international terrorism is

the United States have realized the seriousness and damage that terrorism and extremism could bring to the region as well as the world. There has been increasing awareness from both countries to combine efforts in tackling both the root causes and symptoms.

China and the United States have more constructive interaction in the Middle East than in some other regions of the world.

not an isolated phenomenon and is closely related to economic poverty and social stagnation, which create hotbeds for radical ideologies and extremist movements. China and

Furthermore, the two countries cooperate with other major actors on Middle East hotspot issues. China maintains good relations with almost all the regional countries. The United States is the most important player in the region, but China and the United States together with the EU and Russia succeeded in averting a war over the Syrian chemical weapons issue. Because of the U.S.-Russia confrontations resulting from the Ukraine Crisis, China played an even more important role in facilitating the Iranian nuclear issue negotiations, thus not only creating more conducive conditions for the overall improvement of the Gulf Region but



China's Foreign Minister Wang Yi, French Foreign Minister Laurent Fabius, German Minister for Foreign Affairs Frank-Walter Steinmeier, High Representative of the European Union for Foreign Affairs and Security Policy Federica Mogherini, Iranian Foreign Minister Mohammad Javad Zarif, British Foreign Secretary Philip Hammond and U.S. Secretary of State John Kerry pose for a picture during the final press conference of Iran nuclear talks in Vienna, Austria on July 14, 2015. (U.S. State Department Photo)

also the global non-proliferation efforts.

Last but not least, China and the United States conduct regular consultations on Middle East affairs and building institutions there. According to relevant arrangements of the fourth round of the China-U.S. Strategic & Economic Dialogue, the two countries started the process of Consultations on Middle East Affairs at Vice Foreign Minister Level in August 2012. Moreover, China became a proactive part of the "P5+1" and played an indispensable role in the Iranian nuclear issue negotiation. This mechanism looks likely to evolve into a more regular one in the years to come.

However, one should not overlook the difficulties and challenges in the China-U.S interaction over, and related to, Middle East affairs. First, China and the United States have different, sometimes even colliding philosophical and guiding principles. China has kept to the principle of non-interference in internal affairs, especially in face of the sudden and drastic changes in the so-called Arab Spring. The United States has stressed its leadership and responsibilities to protect. The two countries differed in their policies in the Second Iraq War, Libya War and

the ongoing Syria Civil War.

Second, the two countries differ in their strategic weights and strategic goals related to the Middle East. So far, the United States is the most important outside player with political, economic and military leverages, trying hard to maintain its dominant position of international involvement. China's strategic goals and actual influence are much smaller and greatly

China needs to gradually readjust its Middle East strategies and policies while moving towards becoming a global power.

restrained by its limited strength. Therefore, the two countries are actually asymmetrical in their interaction in the Middle East, and their different attitudes and policies are natural and expected.

Third, both countries have their own pressures to readjust respective strategies and policies concerning the Middle East. The United States has the dual-difficulties of winding down its

involvement in the Middle East and maintaining a balance among different geopolitical priorities. It also has to consider the extent by which China can play a greater role without damaging vital US interests. For instance, the United States is very much concerned about China's increasing political and military presence in the region and on the maritime routes. China is in a dilemma, too. China's stake in the Middle East has risen in recent decades, propelling Beijing to play a greater role and assume more responsibilities. However, a greater amount of military responsibility

concerned.

Therefore, China needs to gradually readjust its Middle East strategies and policies while moving toward becoming a global power. Mainly, China has four strategic goals towards the Middle East as a whole: maintaining regional peace and stability, promoting energy and non-energy cooperation, enhancing cultural interchanges and people-to-people relations, and striving for more synergy with other major powers, the United States in particular.

For future interaction involving Middle East affairs, both China and the United States must work together for more strategic consultation, policy coordination over the hotspot issues, and economic cooperation with third parties as both find ways to manage political and ideological differences. Moreover, "the devil is in the details". Both China and the United States need to further outline and implement their cooperation in ensuring the safety and security of the sea lanes, meeting the challenges from terrorists and extremists, working with key regional countries such as Egypt, Saudi Arabia, Turkey and Iran, and working together on China's Silk-Road initiative ("Belt & Road").

All in all, the Iranian Nuclear Issue Agreement should encourage both China and the United States to redouble efforts to flesh out the NMMCR through more effective cooperation in Middle East affairs for the benefit of themselves as well as the region and the world as a whole.



would require for China to change its strategic thinking and actual policies dramatically, and even drastically. Besides, there is a big gap between China's real capabilities and the expectations from the countries

Iranian people celebrate the nuclear agreement between Iran and the P5+1 world powers on July 14, 2015 in Tehran, Iran. Iran and the world powers group, P5+1, have reached a milestone agreement over the nuclear issue in the Austrian capital of Vienna on Tuesday. (Photo by Fatemeh Bahrami)

After Corrections, China's A-Shares Resurgent

Despite the recent unprecedented slump in the stock market, Beijing will continue to foster healthy development of the stock market through market-oriented reform policies. This unchanged policy ensures that the upswing in the Chinese stock market will continue in the second half of the year.

The Chinese equity market suffered a three-week plunge. The index tumble began on June 12 after the Shanghai Composite Index climbed to 5,178 points, and by July 7, it had nosedived to a low of 3,507 points, declining more than 33 percent. This was the biggest three-week slump for the A-share market since 1992, and constituted a severe stock-market crisis. To cope with the crisis, the Chinese government had to launch full-scale measures to rescue and stabilize the market. On July 8, the Shanghai Composite Index finally snapped its losing streak to close at 3,709 points. After the turbulent corrections, this is likely to mark a new starting point for the A-share market to re-embark on its continuous surging trend.

To understand why the stock

market crisis occurred, it is essential to analyze the reasons behind the massive surge prior to the free fall. An important factor behind the market rally was that the Chinese government wanted to follow the example of the U.S. financial market and shore up the sagging economy, which has been driven by the real estate industry through a bullish stock market. Reductions in interest rates and reserve requirement ratios as well as the Shanghai-Hong Kong Stock Connect program were all meant to foster a bull stock market.

The A-share market, however, is different from the U.S. equity market. On the one hand, the Chinese stock market is still far from mature and well-developed; on the other hand, the Chinese institutional structure and



Yi Xianrong
Researcher, Chinese Academy of Social Sciences

fundamentals are also greatly different from those of the United States. Under such circumstances when the Chinese government had the intention of fostering a government-stimulated “national bull market,” stock investors all developed strong anticipations for surges in the stock market. The A-share market, for the third time in about 10 years, became a risk-free hedging market.

The Shanghai Composite Index, since the end of June 2014, rose from 2,039 points to 5,178 points in mid-June this year, surging by more than 150 percent with only some minor adjustments and corrections. Such a fast rise and frenzy gave rise to an illusion among the investors that stock

investment would be risk-free, and that even blind purchases of stocks would lead to handsome gains; that they could make big money through excessive leveraging of margin trading.

With the prevailing illusion or fantasy of a risk-free stock market, many investors resorted to high-leverage borrowing to bet on the stock market, particularly with the inflows of excessively leveraged borrowings from the “gray or shadow lenders,” or the non-official channels. Pushed by massive inflows of capital, Chinese stock market indexes successively surged to new highs in a short span of time, and along with the market rally, risks were also rapidly accumulating



(By Li Min)

and magnifying. Against such a background, the market regulators had to strictly regulate and curb excessively leveraged financing. The stock market then began to tumble.

The massive slump not only exposed stock market risks brewed by high-leverage financing, but also led to the shattering of illusions about the “risk-free market.” With the tightening regulation and supervision and in order to mitigate huge risks that were likely to occur with stock-index plunges, panic ensued and anxious investors all wanted to dump their holdings as quickly as possible. This further worsened the stock market decline, and the sell-off rush also magnified risks of the equity market, and ultimately led to the stock-market crisis.

With dangers from the stock market lurking, the Chinese government, at the beginning, overestimated its capabilities in managing the market, and chose to believe that it was capable of controlling and managing the risks to a reasonable limit. The government failed to realize that this round of market frenzy, triggered by high-leverage financing, would likely lead to greater dangers or even an equity-market crisis when “deleveraging” measures were implemented. Although the government took a series of measures to rescue the

market shortly after the tumble began, these measures produced very limited effects. Only when a full-scale crisis happened, did the government finally have to intervene with a heavy hand.

Rescuing the market should be part of government’s responsibilities. In any country, the government should be the final credit guarantor for the financial market, a kind of quasi-public product. At a time of crisis, the government is always obligated to guarantee market stability. After the financial crisis in 2008 in the United States, the U.S. regulatory departments swiftly and resolutely adopted measures to limit tremendous risks of the stock market to the minimum levels, resolutely prevented possible spillover and contagion, and made financial stability a priority. When the Chinese stock market continued to tumble and a crisis evolved, the Chinese government also had the responsibility to rescue and stabilize the market, so as to guarantee market stability and rebuild confidence. In the face of a crisis, it was therefore justified for the Chinese government to take measures to shore up and stabilize the market.

But the methods and degree of government rescue and intervention should be appropriate, otherwise they would be subject to



Shanghai Composite Index (2014/09 – 2015/07)

The surging trend in the Chinese stock market will continue in the second half of the year.

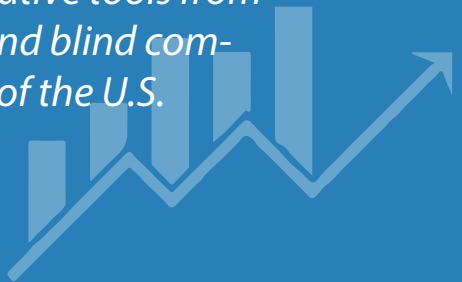


28 June - July Chinese government began to launch measures to rescue the market.

suspensions and questioning from the market. Judging from the current circumstances, the Chinese government's market rescue measures are unprecedented, extensive and resolute, and the main purpose has been to stabilize the market and restore confidence. The government has realized that both the massive stocks rally

and slump in the past year, to a great extent, were associated with the government's policies towards the stock market, the government's understanding about the nature of the financial market, the blind introduction of various financial derivative tools from mature and developed markets, and a simple and blind

The government has realized that both the massive stocks rally and slump in the past year, to a great extent, were associated with the government's policies towards the stock market, the government's understanding about the nature of the financial market, the blind introduction of various financial derivative tools from mature and developed markets, and a simple and blind comparison of the Chinese financial market to that of the U.S.



comparison of the Chinese financial market to that of the U.S. After the restoration of stability, therefore, the Chinese government will probably have to seriously reflect, redefine, and re-position the stock market. These reflective measures are likely to serve as new driving forces for reforming China's stock market. Otherwise, after this round of government rescue measures, it will give rise to a speculation that the market-oriented reforms would be abandoned and the government will frequently intervene and meddle in the stock market in the future. Such a speculation will produce negative impacts on the reform and opening of the stock market. Therefore, it is widely believed that the government will likely deepen reforms so as to reassure the market players and dispel doubts and uncertainties. It is certain that the market-oriented

reforms of the Chinese financial markets will continue and will never backtrack.

Despite this unprecedented slump in the stock market, the Chinese government's strategy in developing the equity market was not changed, and the government will continue to foster a healthy development of the stock market by applying market-oriented reform policies. Therefore, the surging trend in the Chinese stock market will continue in the second half of the year. From the point of view of the government, as long as the economy is still in the process of struggling to return to the road of healthy and sustainable path, the government will continue to drive up the stock market to aid the real economy; otherwise, the economy will likely slow down further.

Gains and Losses for U.S. in South China Sea

China-U.S. competition and rivalry in the South China Sea is structural, strategic, and irreconcilable. Preventing conflicts from damaging bilateral ties is a practical imperative for decision-makers in both countries.

Wu Shicun

President, China

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Sea Studies



U.S. South China Sea policies have undergone several rounds of profound changes since the end of the 1990s, evolving from “staying neutral” to “limited intervention”, and then “active intervention.” This is because, on one hand, with Chinese comprehensive national strength continuously rising and its relative capabilities growing at sea, Chinese policies regarding the South China Sea have become increasingly clear, and a maritime order in the South China Sea dominated by China is beginning to take shape. While pressing ahead with its pivot to the Asia-Pacific, the U.S. is gradually enhancing its preventive containment of China. On the other hand, the U.S. is reducing its policy of “neutrality” into a nominal existence, getting involved more and more deeply in maritime disputes in the South China Sea, and China-U.S. rivalry in the area is unprecedentedly tense. In retrospect, adjustments and evolution of Washington’s South China Sea policies in recent years can be summed up as three gains and three worries.

The first gain is, by supporting the Philippines quest to submit its maritime dispute with China to the International Tribunal for The Law of The Sea, it has subjected China to direct challenge and pressure from



international multilateral mechanisms. In January 2013, with the open support of the U.S., the Philippines unilaterally proposed the compulsory arbitration procedure against China, against both China's will and the commitment Manila had made in bilateral and multilateral agreements to solving the South China Sea dispute through friendly consultations and negotiations.

The second gain is, the U.S. has adamantly supported the Philippines in "safeguarding" the Ren'ai Reef, providing moral and practical support for the latter's attempt to permanently control it. This is because maintaining the China-Philippines territorial dispute in the South China Sea is not only consistent with U.S. interests, but also facilitates its rebalancing to the periphery of the South China Sea and supports its military deployments against China.

The third gain is, taking advantage of the dispute over oil rig 981, it on one

hand supported Vietnam to create new troubles for China on the Xisha Islands issue, and on the other hand actually lifted its lethal weapons embargo against Vietnam. The China-Vietnam dispute in the South China Sea has provided opportunities for the U.S. to contain China.

Besides harvesting the three gains on the South China Sea issue, the U.S. also has absorbed three unexpected worries.

First, it is worried that China will dominate rule-making in the South China Sea. Since the 1990s, China and the Association of Southeastern Asian Nations have reached consensus on launching consultations about a code of conduct in the South China Sea. In 2002, the two parties signed the Declaration on the Conduct of Parties in the South China Sea (DOC); in 2011, they signed the Guidelines for the Implementation of the DOC; in 2013, the two sides reached a new consensus on accelerating

The U.S. should understand and take into consideration Chinese concerns and interests in the South China Sea, honor its pledge of “neutrality” on the issue, restrain its close-in surveillance and reconnaissance flights against China, and prove with actions its claim that it has no intention to contain China with the South China Sea issue.

consultations about the proposed Code of Conduct in the South China Sea; in 2014, China put forward the dual-track approach that “disputes over the South China Sea be resolved through consultation and negotiation between disputing parties, peace and stability of the South China Sea be jointly preserved by China and the ASEAN.” It is thus evident that China may firmly dominate future rule-making regarding the South China Sea.

Second, it is worried that China may obtain overwhelming sea power in the South China Sea.

With global geopolitical gaming centered around the oceans getting increasingly fierce, the U.S. pressing ahead with its strategic pivot to the Asia-Pacific, and exploitation of maritime resources by coastal nations extending from offshore to the high seas, disputes in the South China Sea have evolved from those between claimant countries over sovereignty and maritime jurisdiction over islands and reefs to fierce gaming in such areas as geopolitical competition, natural resources exploitation, and waterway

control among claimant nations and stake-holding parties. China-U.S. competition in the South China Sea has thus upgraded from the previous concerns about freedom of navigation to those regarding dispute-resolution mechanisms, rules on navigation and over-flight in the South China Sea, and the legal status of the nine-dash-line in the South China Sea.

Third, the international community worries that China may declare an Air Defense Identification Zone in the South China Sea.

Since China declared its East China Sea Air Defense Identification Zone in November 2013, the U.S. and the international community have either worried or predicted that it will soon announce an ADIZ for the South China Sea. China has repeatedly stated there is no need for such a zone for the time being. Though such action is within Chinese sovereignty, whether or not it will declare a new ADIZ will depend on its evaluation of security conditions in the South China Sea. China’s ongoing construction activities on isles and reefs in the Nansha area have again

struck American nerves. In a certain sense, it is more concerned about the possibility of the consequent declaration of the feared ADIZ than about the speed or scale of such construction projects.

The South China Sea is a natural line of defense for Chinese national security, an important strategic waterway, and a strategic must-have for it to become a maritime power. For the U.S., controlling the South China Sea and maintaining its presence there is indispensable for its dominance in the Asia-Pacific based on its bilateral alliances formulated in the post-war era. In this sense, China-U.S. competition and rivalry in the South China Sea is structural, strategic, and irreconcilable.

Given the implementation of the U.S. pivot to the Asia-Pacific and adjustments in its South China Sea policies, the South China Sea issue is no longer solely disputes between China and several other claimant nations about sovereignty over islands and reefs and maritime jurisdiction. It has become a very complicated one with China-U.S. conflicts assuming center stage, and those between China and other claimants in the background. Meanwhile, the South China Sea will be an important and unavoidable issue in China-U.S. relations. Therefore, managing China-U.S. disagreements over the South China Sea and preventing conflicts there from damaging bilateral ties is a practical imperative for decision-makers in both countries.

The U.S. should understand and take into consideration Chinese concerns and interests in the South China Sea, honor its pledge of “neutrality” on the issue, restrain its close-in surveillance and reconnaissance flights against China, and prove with actions its claim that it has no intention to contain China with the South China Sea issue. China should respect U.S. freedom of navigation and over-flight in the South China Sea based on international law, try its best to avoid unilaterally declaring the anticipated South China Sea ADIZ that may undermine political mutual trust and security cooperation, truly speed up consultations on the code of conduct so as to deal with the absence of security and crisis control mechanisms in the South China Sea, prioritize civilian functions in construction activities on the isles and reefs there, and be prudent about military facilities that go beyond defense purposes. From the perspective of mechanism building, the two parties can consider setting up a single or one-and-half track “China-U.S. working group for consultations on maritime issues” under their Strategic and Economic Dialogue. When conditions are ripe, they can also consider hotlines between naval commanders.

Thinking Beyond Conflict

As China assumes a bigger role in regional and global affairs, managing differences becomes key to a new model of Sino-U.S. relations. President Xi's upcoming visit is another opportunity for Americans to understand that China's actions are not targeted at the U.S. and its allies.



Chinese Vice Premier Liu Yandong (R) shakes hands with U.S. Vice President Joseph Biden during the joint opening session of the seventh annual Strategic and Economic Dialogue, and Consultation on People-to-People Exchange June 23, 2015 at the State Department in Washington, DC. (Photo by Alex Wong)

In February 2012, Xi Jinping, then vice-president of China, made a visit to the United States. During the trip, he called for “a new model of major-country relations befitting the 21st century” between China and the US. Three months later, then Chinese President Hu Jintao said in his speech to the opening session of the fourth round of China-US Strategic and Economic Dialogue (S&ED) that “no matter how the international landscape or our domestic situations may evolve, China and the US must remain committed to enhancing our partnership and strive to build a new model of major-country relations that reassures the international community as well as our own publics.” Fast forward to June 2013: Xi Jinping, the recently elected President of China, held a retreat with US President Barack Obama at Sunnylands in California. During the summit, Xi laid out, in considerable detail, China's proposal to build a new model of major-country



Zhou Wenzhong
Secretary-General of
Boao Forum for Asia

relations with the US, featuring no conflict or confrontation, mutual respect and win-win cooperation, to which Obama responded positively.

In my view, this vision of a new model of China-US relations is important for three reasons.

First, it outlines a new possibility of relations between a rising power and an established power.

After China overtook Japan as the second largest economy in 2010, US officials and pundits began to discuss the implications of China overtaking the US one day as the world's largest economy. Some predict that this would happen as early as 2020 and no later than 2030. Trained in historical fatalism and the realist theory of international politics, American analysts are inclined to think that a rising China will inevitably challenge US interests and a collision between Beijing and Washington is all but certain. According to this argument, the US should start to prepare itself for such an eventuality. Mindful of this narrative, China offered to construct a new model of relations with the US. If successful, this attempt can help both sides to avert "the tragedy of great-power politics", avoid the "Thucydides' trap" and prove historical fatalism wrong.

Second, it champions an inclusive approach to China-US interactions in the Asia-Pacific region.

Early in his first term, President Obama announced a "pivot" to Asia. By increasing strategic, political,

economic and security investments in the region, Washington seeks to contain the rapidly growing strength and influence of Beijing. This strategy has heightened differences and tensions, and created a more competitive environment in the region. It raises the specter of Sino-American conflict, which would be destructive to the bilateral relationship, and might jeopardize peace and stability in the Asia-Pacific region. To stave off this dire scenario, China has championed a more inclusive approach. Chinese leaders argue that the Pacific Ocean is big enough for the two nations. China and the US should strive to avoid conflict and confrontation, show mutual respect and pursue win-win cooperation. By addressing sources of competition and friction, the two countries build a more positive relationship in the region.

Third, it reflects China's commitment to peaceful development and win-win cooperation as it rises to major-country status.

Under its new leadership, China has pioneered ground-breaking theories and practices in its diplomacy. Whether or not China can build a constructive relationship with the US will be the touchstone of this new approach. Conversely, the vision of a new model of major-country relations can enrich China's innovations in diplomatic theory and practice. Make no mistake: the vision is not aimed at challenging American supremacy in the world, seeking parity with Washington, or forming a G2 with the

US. On the contrary, it is to maximize positive interactions and constructive cooperation between the world's largest developing and developed countries. A more immediate goal is to dispel strategic distrust between the two sides and the often negative predictions about China-US relations, and persuade the world that this vital relationship is a positive, amicable, cooperative, constructive and predictable one.

Since 2013, some tangible progress has been made toward realizing this vision.

First of all, Chinese and US leaders are pursuing constructive dialogue with unprecedented depth and width.

The Sunnylands summit between President Xi and President Obama in June 2013 created a new model of engagement between our leaders. Without fussing over whether it was a state or working visit, the two presidents spent more than eight hours in face-to-face dialogue. They discussed a broad array of issues: from domestic developments and governance experience to economic and financial issues facing China and the US, from traditional bilateral issues to nontraditional regional and global challenges such as North Korea's nuclear program, climate change and cyber-security. While helping to drive China-US cooperation around concrete issues, the meeting did not shy away from certain long-standing disagreements. The Sunnylands summit will be remembered as an unprecedented investment in China-US relations for its novel format, length and depth of

discussion, and range of topics.

Then in November 2014, President Obama came to Beijing to attend the APEC Economic Leaders' Meeting, after which he paid a state visit to China. All eyes were on his meeting with President Xi. As it turned out, the two presidents spent ten hours together over two half-days. They met informally at the Zhongnanhai leadership compound for an evening walk, a restricted meeting, a private dinner and a tête-à-tête over tea, where they shared domestic developments and priorities. The next morning, they met again in formal talks to discuss bilateral and international issues at the Great Hall of the People.

Both sides characterized the conversations as constructive, candid, sincere, in-depth and productive. Obama said that they gave him "the most comprehensive, in-depth understanding of the history of the Chinese Communist Party and its idea of governance and a better understanding of why Chinese people cherish national unity and stability." Through these talks, the two leaders had an opportunity to reaffirm their shared desire to work toward a new model of relations, increase mutual understanding, address misperceptions and reduce mistrust. With Obama passing the halfway point of his presidency and contemplating his diplomatic legacy, the meeting drove home to him the importance of building a more positive relationship with China in his last two years in office. He sounded a positive note at a joint press conference with Xi, saying, "The

truth is that we have made important progress today for the benefit of both of our nations and for the benefit of the world. The truth is that even more progress is possible as we continue to develop this important relationship. I am confident that we will be able to do so.”

In addition to unprecedented presidential “face-time”, China and the US have also reaped “early harvests” over the last two years in important bilateral and multilateral areas.

The two sides have agreed to launch substantive negotiations on a bilateral investment treaty (BIT) based on pre-establishment national treatment and a negative list, a major breakthrough in China-US economic engagement. Meantime, two-way trade and investment continue to soar. Last year saw a record \$555.1 billion of trade and \$120 billion of cumulative investment between China and the US.

For too long, military-to-military ties have lagged behind other areas of the relationship. After the two presidents agreed at Sunnylands to improve and enhance mil-to-mil relations, a number of advances have been made, such as increased interactions at all levels, institutionalized dialogue and consultation, exchanges between young officers, joint trainings and exercises. Last summer, China participated for the first time in the RIMPAC exercise organized by the US, a significant breakthrough as China fielded the second largest fleet (after the US) in the 23-nation exercise. This was followed by

the signing of the mechanism of notification of major military activities and the code of safe conduct for maritime and air encounters by senior defense officials in November 2014. These two confidence-building mechanisms (CBMs) will go a long way toward bolstering strategic trust, managing crisis and preventing risks between China and the US and help to reduce the chances of miscalculation and accidents involving their militaries.

The expansion of bilateral exchanges calls for a more convenient visa regime. Last November, the two presidents agreed to issue five-year, multiple-entry visas to each other’s students and ten-year, multiple-entry visas to each other’s business travelers and tourists. The announcement was hugely popular in both countries and will surely bolster people-to-people exchanges across the Pacific. As a result, the number of Chinese visas issued to US visitors grew by 54% in the three months after the announcement, culminating in 4.3 million two-way visits for 2014.

In the multilateral arena, the two sides have reached bilateral understanding to expand the WTO’s Information Technology Agreement (ITA), which will inject momentum into multilateral discussions in Geneva. The two sides have enjoyed close communication and coordination on the Iranian nuclear issue and have worked together to drive progress in the P5+1 negotiations. They have also stayed in close touch on the Korean nuclear issue to maintain peace and stability on the peninsula and in northeast Asia. In addition,

Both sides must focus on the big picture, discard a confrontational approach and improve internal coordination.

there have also been collaborative efforts to improve the situation in Syria, Afghanistan and South Sudan, and to fight the Ebola epidemic in Africa.

The joint announcement on climate change issued after the Xi-Obama summit last November deserves special mention. With the United Nations Climate Conference scheduled for December in Paris, the world is watching to see whether an agreement can be secured to limit global temperature rise to 2 degrees Celsius from pre-industrial levels. As the world's largest emitters, the positions of China and the US will be crucial. The joint announcement was eye-catching because it contained clear targets: the US intends to achieve an economy-wide target of reducing its emissions by 26%-28% below its 2005 level in 2025, while China intends to increase the share of non-fossil fuels in primary energy consumption to around 20% by 2030 and achieve the peaking of CO2 emissions around 2030. Both sides agreed to push for a global deal at the Paris conference. Meantime, China and the US will enhance practical cooperation, including on advanced coal technologies, nuclear energy, shale gas, renewable energy, carbon capture, utilization and storage (CCUS), hydrofluorocarbons (HFCs), low-carbon cities, and trade in green goods.

These significant steps will bring about a paradigm shift in the global politics of addressing climate change. The New York Times noted that in the past, no country was willing to cut emissions until other countries have done so; with the China-US announcement, countries will be motivated to follow their leadership. This demonstrates the enormous value of China-US cooperation to strengthening global governance.

More can be expected. On Feb 11, President Obama called President Xi to invite him to pay a state visit to the US in conjunction with attending the UN's 70th anniversary events, which Xi readily accepted. The Chinese and US teams are preparing the ground for a successful visit, which will hopefully cement the momentum of high-level engagement, remove mistrust and build consensus for better relations through patient and in-depth dialogue, and deliver more tangible results of cooperation. If so, Xi's September visit will surely drive new progress in building a new model of major-country relations between China and the US.

Let me end with a few thoughts on the implementation of that vision.

Building a new model of China-US

relations will be fraught and complex process full of opportunities and challenges. It is important that both sides adopt new thinking. China's rise is taking place against the backdrop of economic globalization, regional integration and international cooperation in the post-Cold War environment. Committed to peaceful development and win-win cooperation, China has drawn lessons from the past. Beijing has expressed a sincere desire to avoid the strategic mistakes other rising powers have made and find a new path to major-country status. The US rose to global preeminence after the Second World War. It established a global architecture during the Cold War and stood out as the world's sole superpower after the end of the Cold War. But times have changed. The US should stop relying on military and geopolitical methods as the way to maintain its advantageous position. It should stop viewing the rise of China in zero-sum terms and take a fresh look at its relationship with a rising power whose values and social system is fundamentally different from its own. Thus, both sides can give sustained impetus to the vision through new thinking and dynamic action.

To build a new model of China-US relations, the two sides need to respect each other's core interests and major concerns and manage their differences and tensions. As China's economy and interests continue to grow, Beijing will not shirk from upholding its sovereignty, security and development interests and will assume a bigger role in regional

and global affairs. The US must stop thinking that China's actions are targeted at the US and its allies and designed to weaken US supremacy or the regional order. Washington must not seek to counterbalance or even contain Beijing. Hence the importance of managing differences, which is as central to the relationship as augmenting cooperation. To do this, both sides must focus on the big picture, discard a confrontational approach and improve internal coordination.

To build a new model of China-US relations, both sides must approach it from a larger, global context. The course taken by China-US relations will have a big impact on world events. While our world is becoming more multi-polar and globalized, the urgency and challenges of global governance are more prominent. In the current phase of China-US relations, both sides need to closely monitor and analyze global developments, think outside the box, and be prepared for both opportunities and challenges in a fast-changing world. This is the best way to achieve sound and steady growth of China-US relations in the long run.

South China Sea

Is It Worth the Risk of War?

The chattering classes are buzzing about the importance of making China “pay a price” for its aggressive behavior. However, the possibility of miscalculation and misjudgment makes it even more important that all participants step back from confrontation.



Doug Bandow
Senior Fellow, Cato
Institute

The U.S. and China disagree on a long list of issues. That's not particularly serious. After all, America and Europe hold different views on many topics. However, the territorial controversies in the South China Sea (and seas further north) risk swallowing the entire bilateral relationship.

Contrasting Chinese and American perspectives were on display at the recent Shangri-La Dialogue, during which Defense Secretary Ashton Carter challenged Beijing over its island expansion program. China denounced his “absurd” remarks. Privately the possibility of war has emerged as a serious topic in Washington. Both nations should draw back from their increasingly dangerous game of chicken.

Some territorial claims are easy. Often, however, history disdains simplicity. In this case there is a complex mix of control, historical practice, international law, and treaty. In the view of most observers, Beijing's claims are extravagant. Yet they are not unprecedented.

James Knox Polk became U.S. president in 1845. America had annexed Texas after the latter's violent secession from Mexico and claimed a new national boundary set well beyond land populated by secessionists. Washington also took an aggressive posture in dealing with Great Britain about setting the U.S.-Canada border in the Pacific Northwest. America won its claims in the first case through conquest and in the second instance through



Adm. Scott Swift, commander of U.S. Pacific Fleet, observes operations aboard a P-8A Poseidon aircraft on July 18, during a seven-hour surveillance flight over the disputed waters. (Photo by MC2 Tyler R. Fraser)

negotiation. Washington should remember that Great Britain's decision to so accommodate the U.S. yielded long-term peace and future friendship.

As territory most of the islands are worthless rocks. However, they carry with them control over surrounding waters and underlying resources. Perhaps equally important, ownership reflects national ego. Almost as important as exercising sovereignty is denying control to adversaries, some long-hated.

While Washington lays claim to no land, it insists on free transit in surrounding waters. Equally important, with China expanding, many Americans want the U.S. to contain Beijing. One recent study urges Washington to retain military primacy in East Asia and attempt to weaken the PRC. That means backing not only treaty allies but in practice their territorial claims against China.

Indeed, there is increasing commentary among the chattering classes about the importance of making China "pay a price" for its aggressive behavior. The administration is in the curious position of more vigorously advancing claims than the claimants themselves. Washington even has suggested joint patrols with Japanese ships and planes in the South China Sea, where Tokyo has no claims. The U.S. created particular controversy flying over islands claimed by China, courting a corresponding challenge from the latter.

The problem is not asserting American navigational freedoms, but doing so in a way seemingly designed to provoke a response. In 2001 similar military gamesmanship resulted in an aerial collision, which killed a Chinese pilot and brought down an American spy plane, leading to an extended bilateral stand-off.

The territorial controversies in the South China Sea risk swallowing the entire bilateral relationship.

Since then both nations have become even more concerned over credibility and reputation, which means neither will readily back down when challenged. Beijing does not want to yield to seeming efforts at containment. The U.S. worries about being viewed as a paper tiger around the globe.

The result: a real danger of an escalating military confrontation. Rather than working to prevent such an eventuality, however, a number of officials, pundits, and analysts appear to view it as almost inevitable.

I recently attended a gathering, which included retired military, former government officials, current policy analysts and journalists, NGO staffers, and non-political professionals. Much of the discussion concerned the challenge posed by the PRC and recent events in the South China Sea. Without a neoconservative at the table there was broad agreement that Beijing

had tossed down the gauntlet, so to speak, and had to be confronted.

Most sobering was the acknowledgement that an aggressive reaction could trigger a Chinese response in kind and a confrontation such as a ship collision or plane shoot-down. The consensus was that Washington would have to act immediately and firmly by, for instance, sinking a vessel or destroying a runway. The unspoken presumption was that the confrontation would end there, with Beijing duly chastened. But the obvious question is what if the Chinese made a similar calculation and escalated in turn? Some “damn fool thing” in the Asia-Pacific just might trigger war between the two nations.

Washington enjoys military superiority but must disperse its forces around the globe. More important, the PRC views its interests in nearby waters as important if not vital. In contrast,

American domination everywhere, against everyone, is not necessary for America's defense.

American domination everywhere, against everyone, is not necessary for America's defense. Beijing knows that and will risk much more than the U.S. in handling nearby territorial issues.

No amount of scare mongering is likely to change this calculation. If you were to ask Americans to risk a lot to preserve Japan's independence, they might rise to the challenge. Ask them to war against a rising nuclear power to ensure that the Philippines controls Scarborough Reef, and they are likely to view their leaders as dangerous fools.

The possibility of miscalculation and misjudgment makes it even more important that all participants step back from confrontation. China cares deeply about sovereignty; Beijing's adversaries believe the U.S. has their back; Washington would not tolerate an attack on its forces. No one wants to look weak. The fuse to war may be long, but no one should risk lighting it.

All parties should look for creative solutions to the plethora of territorial disputes. Countries could set aside deciding on sovereignty while jointly developing resources. Neighbors could share sovereignty and resources.

Beijing could pledge to maintain navigational freedoms irrespective of the islands' ultimate disposition.

Sovereignty over territory in the western Pacific is important, but not worth war. Yet a dangerous dynamic appears to have taken hold. The PRC believes the islands are Beijing's by right and can be acquired by assertion. The U.S. believes that the territories will end up China's by conquest unless Washington actively blocks Beijing's claims. Instead of sleepwalking into a shooting war while assuming the other party will bend, both America and China should renew their determination to defuse territorial controversies peacefully.

Foundation of China-U.S. Relation Lies in Silent Majority

The desire for peace, mutual respect, and economic cooperation is already winning the hearts and minds of everyday people on both sides of the Pacific. Their voices may seldom make the headlines, but they are a critical foundation of this important relationship.

Wang Dong,
*Associate Professor,
Peking University*



In his recent speech at the Carter Center, the prominent China scholar David Mike Lampton stressed his concerns about the state of U.S.-China relations, stating, “A tipping point in U.S.-China relations is upon us. ... We are witnessing the erosion of some critical underlying supports for predominantly positive U.S.-China ties.” Professor Lampton’s remarks reflect the growing pessimism in China-U.S. relations in the American media and academic community.

Interestingly, recent survey results released by the Chicago Council on Global Affairs on June 2 said 67% of the American public, 87% of Democratic leaders and 78% of Republican leaders think the U.S., when facing a rising China, should undertake “friendly cooperation and engagement” with China, while only 29% of the overall public, 22% of Democratic leaders and 25% of Republican leaders believe the U.S. should actively work to “limit” the growth of China’s power. This says a lot about the perception gap between the U.S. media and think-tanks vis-a-vis the public and decision-makers when it comes to China-U.S. ties. I was left with a similar impression from my recent trip to the United States for the annual dialogue between my institute and the Brookings Institution and

exchanges with officials from the National Security Council, the State Department, the Pentagon and the Treasury.

This suggests how many in the U.S. media and policy circles are focusing excessively on the dramatic aspects of differences or frictions between China and the U.S., i.e., the South China Sea and cyber security, and overlooking the relations' strong social foundation. That being said, the issue of misperception and emotionally guided perspectives does exist between the two sides. One needs to see that despite heightened U.S. strategic suspicion toward China, its overall China policy remains a hedging strategy. On the whole, China and the

U.S. continue to have far more common interests than differences. For China, it is important to see the larger picture and not let any particular event stand in the way of the growth of relations with the U.S. even as we protect our own national interests. It is important for Beijing to have patience, to step up strategic communication to avoid miscalculation and misreading in the China-U.S. signaling game, and to learn how China might guide and shape the choices and behavior of the U.S.

More important, we must not ignore the "silent majority" when observing and analyzing China-U.S. relations. The lower we move our sight down the "tree" of China-U.S.



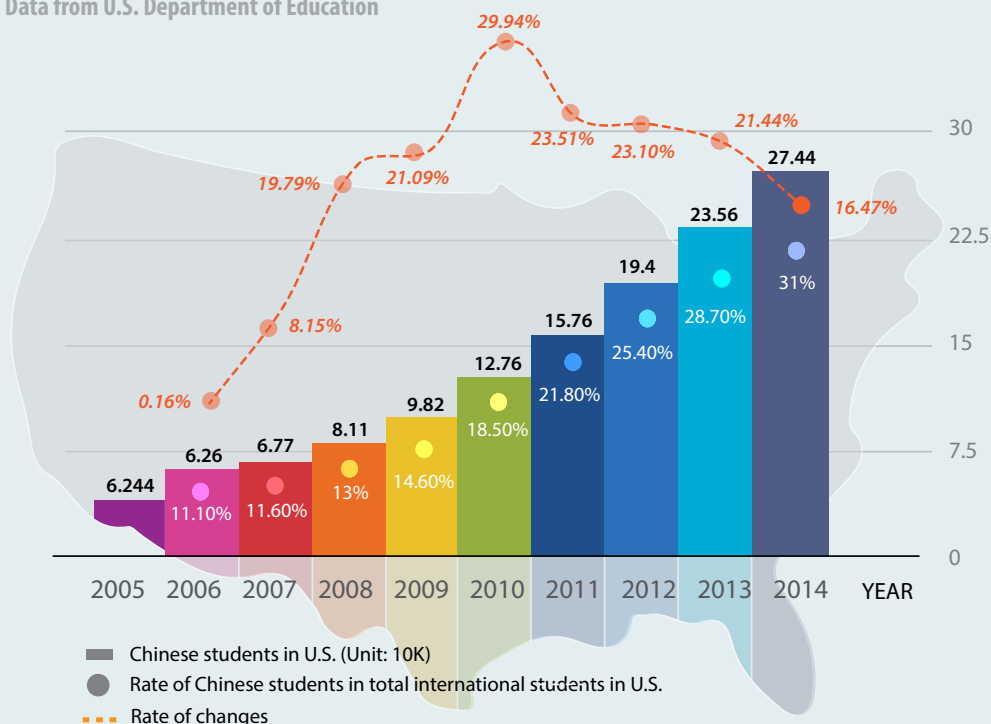
A group of American students with diverse ethnical backgrounds visited Hangzhou Xixi Wetland Museum during their two-week' China visit in August 2014. The program was organized and sponsored by Wanxiang Group and China-US Exchange Foundation.

relations and the more we focus on the sub-national and community levels, the more evidence we shall find that proves how strong public support for bilateral ties is, which actually continues to grow each day. Between the people of China and the United States, exchanges have kept deepening, covering economy, trade, science, technology, education, culture and various parts of the two countries. They are a witness to the increasing interconnectedness and interdependence between China and the U.S. in this globalized age. Just to cite a few statistics. Bilateral trade

has risen above US\$550 billion. The accumulated Chinese investments in the U.S. in the past five years have reached about US\$50 billion and the number may reach US\$200 billion by 2020. Joint collaboration and innovation have reached impressive depths in a wide range of areas including environmental protection, clean energy, agriculture and health, and so on. From 2009 to 2014, over 100,000 American students have studied, visited or lived in China. At the moment, there are more than 270,000 Chinese students in the U.S., accounting for one third of total

The proportion of Chinese students in total international students in U.S. (Unit: 10K)

Data from U.S. Department of Education



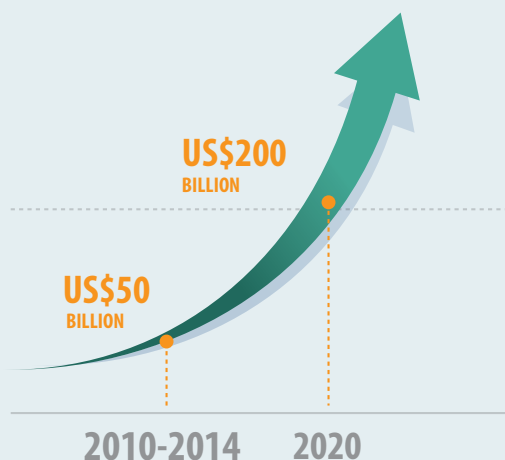
From 2009 to 2014, over **100,000** American students have studied, visited or lived in China.

international students there. So far, 38 provinces/states and 169 cities have established sister relations. Each day, more than 10,000 people travel between the two shores of the Pacific. This year, the number of mutual visits is expected to exceed five million. In a sense, people-to-people exchanges are like a giant net, underpinning a bilateral relationship of enormous significance, and, more essentially, are like the omnipresent air that keeps this relationship alive.

The “silent majority” are actually the frontrunners in practicing and building the new model of major-country relationship between China and the U.S. Just as some American experts are still questioning the idea, the “silent majority” have already cast their “yes” vote through action. Among them, a new model of relationship featuring non-conflict and confrontation, mutual respect

and win-win cooperation is already taking shape. Their voices may seldom make the headlines, but they must never be ignored by us, observers of this important relationship. As the recent Seventh China-U.S. Strategic and Economic Dialogue and the Sixth China-U.S. High-Level Consultation on People-to-People Exchange in Washington D.C., it is most important to see faith and optimism in the future trajectory of China-U.S. relations through the vibrant people-to-people exchanges going on between the hundreds of millions of Chinese and Americans and to listen to what the “silent majority” is saying to all of us.

Accumulated Chinese investments in the U.S



Bilateral Trade US\$550 billion

Bilateral trade has risen above US\$550 billion. The accumulated Chinese investments in the U.S. in the past five years have reached about US\$50 billion and the number may reach US\$200 billion by 2020.

A Dragon Meets a Bear In Central Asia

With the support of Russian resources, China is emerging as a much stronger player in Central Asia. States in the region may exploit this Sino-Russian rapprochement in order to advance their own goals, receiving security and funding from Moscow and Beijing, while not being required to change political regimes.



**Kemel
Toktomushev**

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On May 9, Russia staged the biggest military parade in its history at Red Square, involving more than 16,000 troops and hundreds of the newest armored vehicles, military airplanes and helicopters. The Victory Day Parade marked 70 years since the defeat of Nazi Germany in World War II, during which the Soviet Union suffered the heaviest casualties. Although the victory over Nazi Germany was an allied effort, many Western leaders shunned Moscow's military parade in protest of Russia's alleged involvement in Eastern Ukraine. This rupture between Moscow and the West underlined that the U.S.-Russian "reset" is rather over, whilst the Kremlin is willing to deepen its relations with the non-Western states and is tilting more towards China. The parade in Moscow appeared to confirm this tendency.

Although it is highly unlikely that a new Russian-Chinese bloc will emerge in the Eastern hemisphere,

a Sino-Russian rapprochement is to be expected, and Central Asia is the natural region to observe greater cooperation between Moscow and Beijing. Russia and China are already working together in Central Asia under the auspices of the Shanghai Cooperation Organization (SCO). The SCO was established initially in 1996 as the Shanghai Five to set the framework for strategic cooperation on matters related to security on border regions between Kazakhstan, Kyrgyzstan, Tajikistan, Russia and China. In 2001, the goals of the organization were reformulated to include political, economic, and military cooperation.

The birth of the SCO was immediately regarded by many analysts and policymakers as a potential balancing tool of Russia and China to counter the growing American engagement in Central Asia. Yet, to date, such a result has not materialized. Beijing



remained reluctant to get engaged directly in the security matters of Central Asia, notwithstanding its concerns with Islamic separatism in Xinjiang. In a similar vein, Moscow resisted the Chinese initiatives to turn the SCO into a more development and economic-based platform. In this respect, a Sino-Russian rapprochement may animate the SCO. In fact, Beijing may become the powerhouse of the SCO by guiding the organization in a new direction. The enhanced cooperation between Russia and China may also foster new bilateral and multilateral initiatives.

Nonetheless, points of friction between Russia and China remain. The impact of the Eurasian Economic Union and its tariffs on the level of trade and investment in the region have yet to be seen, since China remains one of the principal economic partners of the Central

Asian states and their main source of development finance. At the moment, official Beijing appears to understand the Kremlin's vision of the role of Russia in the geopolitical system of axes. There is a widely accepted belief in Russia that the country is emerging as the world's greatest power and thus should be treated as an equal partner in the international arena. For now, China is willing to accept these popular discourses and play an informal leadership, or rather co-leadership role in Central Asia.

As a result of such an approach, China is emerging as a much stronger and greater player in the Central Asian region, and perhaps beyond. Beijing acquired not only exclusive access to the Russian resources, but also the Kremlin's political support to be more proactive in the Russian "near abroad." The Silk Road Economic Belt and Asian Infrastructure Investment



Russia China

The enhanced cooperation between Russia and China may also foster new bilateral and multilateral initiatives.

Bank are some of those exemplary initiatives spearheaded by China and endorsed by Russia. Yet, again, it remains unclear to what extent Russia will be willing to encourage Central Asian states to engage in the Chinese-led activities such as the Silk Road Economic Belt projects.

In turn, Central Asian states may exploit this Sino-Russian rapprochement in order to advance their own goals. Russia and China emerge as convenient partners for the Central Asian leaders to cooperate with, since both Moscow and Beijing may act the guarantors of security from external threats and serve as the sources of funding for the Central Asian states. Yet, most importantly, neither Russia nor China is demanding democratic transformations from the Central Asian governments as the prerequisite for such support.

In the meantime, although many Western leaders boycotted the military parade in Moscow on May 9, President of Russia Vladimir Putin still enjoyed the company of important dignitaries to mark the Victory Day. Apart from the usual suspects, China's President Xi Jinping was among those guests to join the Russian president at the 70th anniversary parade. For some period it appeared that, indeed, the parade was not about military might and the balance of power, but about paying tribute to millions of civilians and soldiers who lost their lives in the Second World War.

70 Years After WWII

What Have We Learned?

Events commemorating the 70th anniversary of World War II will give China opportunities to demonstrate its determination to promote peaceful development in the world and strengthen mutual trust with its wartime allies, including the U.S.

It is rather timely to reflect and gain some new insights on the lessons of World War II for today's China-U.S. relations on the occasion of the 70th anniversary of the war's end.

The history of World War II proves that justice will triumph over evil, light over darkness, and progress over reaction. It also teaches us the following:

First, differences in social systems are not the fundamental reasons behind war or conflict; countries of different social systems may seek common ground while reserving the right to difference and jointly deal

with the shared challenges of mankind so long as they follow historical trends and the people's will. During World War II, even though there were conflicts of interests and policy differences among China, the U.S., UK, France and the Soviet Union, they were examples of countries with different social systems able to coexist peacefully, cooperate closely and fight enemies together. Seventy years have gone by. Mankind today is still confronted with common enemies – new ones that threaten war, nuclear proliferation, terrorism, environmental pollution, climate change, poverty and diseases. Though countries have their



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China's official logo for commemorating the 70th anniversary of the end of the Chinese People's War of Resistance Against Japanese Aggression and the World War II



own interests and priorities, they should and can develop appropriate cooperative measures in dealing with these common threats.

Second, change in the character of a state does not necessarily lead to a different view of history.

Even though the drastic changes in the former Soviet Union shocked the whole world, and debate still exists over the path of development in transitioning Russia, the various political forces in Russia do not differ on safeguarding the achievements of World War II, or upholding the relevant international agreements such as the Potsdam Proclamation and Cairo Declaration. In other words, they still have the basic patriotic sentiment, national pride, and a sense of historical justice. The Japanese authorities are exactly the other way round. In the evolving political ecology in Japan, revisionist appraisals of World War II have become more prominent. The rightists go all out to distort

history and cover up crimes against the opinion of the world. Such acts are naturally condemned by the international community.

Third, in the past 70 years, both mankind and the times have been evolving, with peace and development gradually becoming the main theme. To recognize this reality is essential. Even with such a significant event as the Ukraine crisis and tense U.S.-Russia relations, President Obama has said on more than one occasion that the world would not return to the Cold War. In this connection, what China or the U.S. considers first is no longer, “Who is our enemy?” but rather, “Who are our partners?” The proposition to create a new model of major-power relations is thus consistent with the historical trend. Competition between cooperation partners is only natural: Competition does not mean confrontation; there are rules to follow.



Fourth, China and the U.S. both have clear-cut core interests:

sovereignty and security. There is no specific factor leading to conflict between them. Since the adoption of its reform and opening-up policy, China has always respected the special status and global influence of the U.S. and objectively accepted the international order dominated by the U.S. even though China stands for changing unreasonable aspects of the old order, such as unilateralism. For example, on the question of the Diaoyu Islands, what the U.S. needs to do is rather simple, i.e., review the Potsdam Proclamation and confirm the existence of dispute between China and Japan, rather than quoting its Security Treaty with Japan. With that, China and Japan may discuss a solution in the spirit of shelving disputes and engaging in joint development. Partiality for Japan is nothing less than giving a tacit agreement to the legality of the December 7, 1941 attack on Pearl Harbor planned by war criminals enshrined and worshipped at the Yasukuni Shrine.

Fifth, various reasons exist behind the distortions of World War II history in today's world.

There is the inertia of a Cold War mentality that seriously obstructs people in some countries from making an objective appraisal. There are schemes to serve special political purposes. There are also echoing voices either shaped by

To open up the future, we must remember history; and to safeguard peace, we must not forget about the war.

ignorance or misled by distorted advocacy. However, there is no lack of people with vision in the world. When West German Chancellor Willy Brandt knelt down at the monument to Polish victims, his nation stood up. Former German president Roman Herzog once said to the effect that a nation will not exist forever without a thorough understanding of its own history. Visiting German Chancellor Angela Merkel stressed in Tokyo that facing up to history is a precondition for post-war reconciliation. Even in Japan, there are people safeguarding the truth of World War II history.

Sixth, as the old Chinese saying goes, “past experience, if not forgotten, is a guide for the future.” Events commemorating the 70th anniversary of victory in World War II will be opportunities for China to demonstrate its determination to safeguard peace and promote development in the world, unswervingly pursue peaceful development and strengthen mutual trust and mutually beneficial cooperation

with World War II allies including the US. As President Xi pointed out, “to open up the future, we must remember history; and to safeguard peace, we must not forget about the war.”

China Postures, America Signals

Leaders in the U.S. and China are not willing to budge from actions they consider key to protecting vital national interests: The U.S. has interest in the shipping lanes and its regional allies, while China is unshakable in its desire to safeguard regional sovereignty. But both understand that military confrontation is in neither nation's interest, and that reality should guide both sides toward peaceful strategies to resolve the tensions.

Both China and the United States understand that a military confrontation between them over sovereignty issues relating to the South China Sea is not in either's interests. Both have enough domestic issues, especially China, and international issues elsewhere, especially the United States, to realize that military hostility with a primary economic partner is not a good idea. This realization was evident in the polite rhetoric at recent talks between Chinese Foreign Minister Wang Yi and U.S. Secretary of State John Kerry, where the U.S. pushed for diplomatic resolutions to the South China Sea disputes. Equally

evident, though, was that neither is willing to budge from what it considers actions key to protecting vital national interests.

While the United States has not officially taken a position on the disputes and does not have a proverbial “dog in the fight” over territorial claims, its interests come peripherally through commitments to allies and interests in regional stability, and directly in maintaining freedom of navigation of key shipping routes in the disputed areas. Over \$5 trillion worth of trade moves through disputed Sea Lanes of Commerce (SLOC)

Satellite image shows the Yongshu reef (also named 'Fiery Cross Reef') of the Nansha Islands after a land reclamation project in south China. The land reclamation project of China's construction on some stationed islands and reefs of the Nansha Islands will be completed as planned soon. (Xinhua Photo)



Joan Johnson-Freese

Professor, U.S. Naval War College

every year. If China controlled these SLOCs, countries might be required to seek China's permission to transit. If China interfered with access to those trade routes and countries had to transit goods another way, there could be significant negative ramifications to global economies. Additionally, not only would SLOC control garner China considerable commercial power, it would potentially allow China to keep U.S. naval forces at bay. The United States therefore considers both the potential commercial and military consequences of extended Chinese maritime claims untenable.

However, Wang also made the Chinese position clear at the May 2015 meeting in Beijing, stating: "The determination of the Chinese side to safeguard our

own sovereignty and territorial integrity is as firm as a rock, and it is unshakable." For China, the idea of territorial integrity is linked to rising Chinese nationalism and regaining the stature it lost during the century of humiliation endured after Western imperialism and Japanese intervention from 1839-1949.

Many countries have made historical and legal claims to the disputed areas. China is by far the largest claimant within what is called the nine-dash line, running south and east from its most southern province of Hainan, indicating the multiple, overlapping territorial claims. But, perhaps not surprisingly, each country's legal claim denies the claim of the others. And so China has increasingly reverted to the simple legal adage that

Both have enough domestic issues, especially China, and international issues elsewhere, especially the United States, to realize that military hostility with a primary economic partner is not a good idea.

possession is nine-tenths of the law and is staking its claim by possession.

Since neither party wants a military confrontation but neither is willing to back down from increasingly protective stances, the risk of a military confrontation appears to stem primarily from miscalculation, or escalation after an accident or mishap. Given increasing Chinese bravado in reclamation efforts, that's a real risk. China postures for possession and control, and the U.S. signals its rejection of Chinese claims. Neither wants a military confrontation so they dance around each other like scorpions in a bottle.

China and six other countries – Brunei, Indonesia, Vietnam, the Philippines, Malaysia and Singapore – are involved in some or all of the various disputes, which have been percolating in some cases for centuries. Beyond nationalism and geostrategic benefits of sovereignty claims are claims over resources in the disputed areas. Estimates for area oil and natural gas reserves vary, but for countries with booming energy demands like China even the lowest estimates, particularly for natural gas, would provide it a significant supply boost. The South China Sea is also a

rich fishing ground. Approximately 10% of fish caught globally are caught in the South China Sea, making it a multi-billion industry and a source of livelihood for many people in the region.

While other countries involved in the dispute have engaged in upgrading their South China Sea outposts as well, Chinese land reclamation efforts have been by far the most extensive. China is building manmade islands near Fiery Cross Reef and Subi Reef, both potentially capable of accommodating an airstrip. If an airstrip is needed, that likely means that China intends a sustained military presence on the real estate.

If Chinese actions in 2013 regarding a disputed island with Japan are any indication, China could declare an Air Defense Identification Zone (ADIZ) around those islands to restrict air traffic. While the Chinese Foreign Ministry specifically stated in 2014 it was not considering an ADIZ in the South China Sea, that could change if an airstrip is established somewhere. In the 2013 case of China's self-proclaimed ADIZ, the United States flew B-52's into the area to demonstrate its objection

and non-recognition of China's claim. Similarly, the Wall Street Journal recently reported that the U.S. plans to send air and sea patrols near these artificial islands, again signaling U.S. rejection of Chinese sovereignty claims.

These kind of scenarios are, however, inherently dangerous.

In 2001, a Chinese F-8 fighter jet bumped a U.S. EP-3 signals intelligence aircraft flying 70 miles off the Chinese province of Hainan. That mid-air collision resulted in the death of the Chinese pilot, and the U.S. aircraft and its crew being forced to land on Hainan Island, and an overall tense situation between the U.S. and China, particularly until the U.S. crew was returned to the United States. The determination of the two countries to resolve the situation without escalation indicates recognition of the importance of a stable U.S.-China relationship. But testing that resolve is precarious.

There is a very real danger that a similar maritime or air incident could take place in the South

China Sea. Chinese military vessels have already harassed U.S. naval surveillance ships Impeccable and Victorious in June 2009. Expanded Chinese submarine capabilities also increase the risk of an incident. In 2009 a Chinese submarine collided with the towed sonar array of a U.S. destroyer. While the United States military did not believe the collision intentional and referred to it as an "inadvertent encounter", it demonstrates the increased potential for mishaps.

Because intentions can sometimes be difficult to discern, miscalculation can occur, prompting a response that leads to escalation that nobody wants, but can be difficult to dial back.

Beyond potential direct U.S.-China confrontation, the U.S. could also be pulled into a dispute through an ally, specifically the Philippines. The Philippines has announced its intentions to extend surveying and potentially natural-gas test drilling on Reed Bank. That could trigger a Chinese response leading to a military confrontation with

Hopefully actors on both sides will keep that in mind as they proceed to protect their interests, remembering that if one scorpion stings the other, both die.

the Philippines. Since the U.S. and the Philippines have had a Mutual Defense Treaty since 1951, the treaty could obligate the U.S. to become involved.

Given the intransigence of both sides' positions, there is a growing fear of an inevitable conflict. Once something is declared inevitable, it usually is. Therefore vigorous efforts must be undertaken to avoid that scenario.

China and the U.S. signed a Military Maritime Consultative Agreement (MMCA) in 1998 toward developing "rules of the road" similar to those regarding potential Incidents at Sea rules established between the U.S. and Soviet Union during the height of the Cold War. Unfortunately there has been little progress toward that goal and the MMCA has been fairly ineffective. Nevertheless, establishing confidence-building measures is a goal worthy of continued diplomatic efforts.

The United States could also support regional actors such as the Philippines in their efforts to protect

their territorial claims. That would mean assisting the Philippines with capabilities toward deterring China, and so runs the risk of aggravating China. Consequently, any such assistance would need to be coupled with both diplomatic efforts toward China, and tempering inclinations toward bold moves against Beijing by the recipient country.

Finally, plans for crisis management must be in place in case an incident occurs, toward avoiding escalation. Perhaps the most positive aspect of this entire situation is that a military confrontation between the U.S. and China is recognized on both sides as not in either's interests. Hopefully actors on both sides will keep that in mind as they proceed to protect their interests, remembering that if one scorpion stings the other, both die.

Beyond the AIIB Signing Ceremony

The Asian Infrastructure Investment Bank (AIIB) will help finance billions in infrastructure projects around Asia, and also challenge the existing financial institutions. Curtis S. Chin suggests ways how the new institution could be efficient, environmentally stringent, and respectful of local rights.



Curtis S. Chin
Former U.S.
Ambassador to Asian
Development Bank

China knows signing ceremonies. This was clearly the case amidst the pomp and circumstance surrounding the recent Great Hall of the People signing ceremony for a new China-led version of the World Bank.

Representatives from some 50 founding members of the new Asian Infrastructure Investment Bank were present, including representatives from Europe and South Asia as well as Australia. But the show was clearly China's.

As one era ends, another begins. Or so, China would have it.

This was most decidedly evident as China

championed a new kind of international financial institution that it may well hope marks the dawn of an Asia-led economic order – if not perhaps a return to an older order, with the Middle Kingdom at its core.

Distinct and different from the World Bank and the International Monetary Fund, which were established under Western leadership as part of a post-World War II financial architecture envisioned at Bretton Woods, New Hampshire, the new China-led version of an Asian development bank has quickly taken shape without either Washington or Tokyo's support. Both nations were notably absent



Chinese President Xi Jinping (Front C) poses for a group photo with the delegates attending the signing ceremony for the Articles of Agreement of the Asian Infrastructure Investment Bank (AIIB) at the Great Hall of the People in Beijing on June 29, 2015. (Xinhua Photo)

from the recent celebrations in Beijing given their governments' decision to refrain from joining the AIIB, even as almost every major economy, including European and Asian allies, did so.

Ostensibly to help fill an annual infrastructure financing shortfall in Asia of some US\$800 billion, this new lender could also contribute a multilateral veneer and funds to realize Beijing's vision of a "new Silk Road" and "new maritime Silk Road", better connecting China to markets and resources in and outside of Asia. Loans may well go to fund ports, railways, bridges, airports and roads across the region as well as to replace aging infrastructure.

This follows the announcement last year of the establishment of a New Development Bank, or so-called

BRICS bank, by founding members – Brazil, Russia, India, China and South Africa. This bank, like the AIIB, will be headquartered in China.

Each of these new multilateral lenders are direct challenges to existing institutions that China and other nations argue have been too slow to evolve as Europe and the United States' share of global GDP has declined. The AIIB is also a pointed response and potentially potent competitor to Japan and the Asian Development Bank, a Philippines-based multilateral lender focused on poverty reduction. Since its 1966 founding, the ADB has always been led by a Japanese president, with strong U.S. support.

At an initial approved capital base of US\$100 billion, the AIIB

at establishment will be nearly two-thirds the size of the decades-old ADB. China will provide some 30 percent of the new bank's initial capital.

The debate may well continue over whether or not the establishment of the AIIB is a reflection of failed U.S. diplomacy and, most cynically, a Chinese wolf in multilateral sheep's clothing, or simply an institution whose time has come given China's economic rise.

As I have argued in the Wall Street Journal and elsewhere, there are several key points all signatories to the AIIB Charter should be on the lookout for, if they are to work from the inside to establish an institution that is less corrupt and wasteful, and more green and respectful of rights, than it might otherwise have been.

Personnel is power

During my own time serving as U.S. Ambassador to and member of the Board of Directors of the Asian Development Bank for three-and-a-half years under Presidents George W. Bush and Barack Obama, I saw how management and staff of this Japan-led institution were able to undercut or "slow walk" initiatives that the United States and European shareholders had long advocated for. This included the advancement of qualified, senior women, and also the

hiring and promotion of personnel based on merit, not nationality. Strikingly, the head of the ADB's then budget and personnel management systems department, one of the most important senior roles at the bank, was typically a secondee from the Japanese government. To this day, spots in senior management – at the vice-president level – are informally reserved for specific nationalities, including the United States. An informal quota also exists for staff by nationality level, based on shareholding.

As AIIB's personnel policies are written, shareholders will want to understand how the AIIB will learn from, follow and as appropriate improve upon what Japan, Europe and the United States have wrought elsewhere. During my time at the ADB, a new standing committee of the board was ultimately created to provide greater oversight of the institution's human resources after a protracted negotiation with Japan and given persistent concerns about less-than-best practices.

The degree to which the AIIB will find budget for experts in areas ranging from environmental impact and resettlement – typically major issues on large-scale infrastructure projects – to world-class human resources and an office for an ombudsman will speak immensely to the new bank's priorities.

Metrics matter

What gets measured does indeed get managed. China has made clear that a “lean, clean and green” AIIB will not be subject to what it and other borrowers have viewed as overly bureaucratic systems for approval and evaluation at the ADB and World Bank. Shareholders will want to focus on what rules and procedures will and will not be adopted from the established multilateral lenders.

Critical will be the system that will be put in place to evaluate the AIIB’s impact. Metrics such as how many, how large and how quickly disbursed are the new institution’s loans must be complemented by a stringent assessment system of the results of such lending. A truly independent evaluations department that reports not to bank management but to the AIIB Board – even a non-resident board – will be vital, as will be a process to hold borrowers and the AIIB accountable should there be non-compliance with the new institution’s standards, however strong or weak they might be.

Accountability mechanisms will need to be strong and effective. At the ADB, there have been instances where borrowers, including China, have undercut or ignored

the work of that institution’s Compliance Review Panel. In one case in the city of Fuzhou, the government of China declined to give permission for ADB staff to investigate an allegation of non-compliance with bank standards. As the panel’s chair made clear in a public report from my time on the bank’s board, “Our view of ADB compliance in the Fuzhou case concluded that we could not safely draw any conclusions or make recommendations after permission for a site visit was refused by the PRC.” Simply stated, China’s control of freedom of movement worked to its advantage in quashing an investigation. Shareholders will want to fight for access and data for effective measurement and evaluation systems.

Third, don’t be fooled by sweet promises. The Wall Street Journal reported that a Chinese promise that it would not have veto power at the AIIB had helped sway some European nations to join. Yet, the lesson of the ADB is simple: Money matters, and the shareholders that contribute the most have the most influence, regardless of any actual, explicit veto power. At times derided as a rubber stamp board akin to China’s National People’s Congress, the ADB board works by consensus, with there being little chance that anything that comes

to the board will not be approved. There, Japan maintains significant control over the ADB agenda despite having only about 16 percent of the bank's shares.

This is likely to be no different at the AIIB, but there China as the dominant, if not majority, shareholder will call the shots. Shareholders will want to pay close attention to ensuring a means to influence policies and shape project lending proposals early on, well prior to what is likely to be eventual rubber-stamp board approval.



Jin Liqun is tasked as the Secretary-General of the Multilateral Interim Secretariat of Asian Infrastructure Investment Bank.

Transparency starts at the top

Transparency starts at the top, and that includes preventing corruption and avoiding conflicts of interest. My former ADB colleague, Jin Liqun, now tasked as the Secretary-General of AIIB's interim secretariat, was often an eloquent advocate for the role of the private sector and strong public-private-partnerships in development. This is likely to continue at the AIIB.

Whether the AIIB, however, will be used as a means by China to strengthen its own state-owned-enterprises and other Chinese entities via "China-friendly" procurement rules at the expense of other nations will need to be scrutinized. The AIIB also might show the World Bank and the ADB how real transparency works, and have its senior management subject to financial disclosure rules. As China's President Xi Jinping continues his much vaunted fight on corruption, AIIB can go a step further and make clear that board, management, and staff will not directly benefit from decisions they make at the new institution. Strong restrictions should also be put in place to limit a revolving door of future former AIIB staff becoming high-paid consultants to the organization.

Safeguards matter

At the ADB, there has been a general commitment that no individual should be made worse off by bank-funded projects. People are compensated if affected, though there is no guarantee that such individuals will be made better off. It is a high and difficult goal for any multilateral lender, even with the best board oversight and management intent. That is one reason for safeguards and periodic policy reviews at the new AIIB.

As recent as early this March, the World Bank identified serious shortcomings in implementation of its resettlement policies and said it would improve oversight and management of its practices to better protect people and businesses affected by projects it funds.

Nathans Sheets, the U.S. Treasury Under Secretary for International Affairs, has called for support of the World Bank and ADB's "high quality, time-tested standards". China has made clear that those standards are up for debate at the AIIB. (Indeed, the existing multilateral lenders are not necessarily the best poster children for good governance.) As did the late Lee Kuan Yew during his iron-fisted rule in guiding Singapore's success, China is now advancing an "Asian way" in this newest of

multilateral lenders.

For all the founding members of the AIIB, their challenge is now to move beyond the signing ceremony and ensure that the "AIIB way" is a balanced one: building infrastructure and growing economies while also respecting the environment as well as individuals and their businesses and communities.

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