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INTERNATIONAL PEACE

Transcript

MANAGING STRATEGIC FRICTION ON CHINA'S PERIPHERY

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Carnegie International Nuclear Policy
Conference 2015

March 24, 2015

(Transcript not checked against delivery)

TOBY DALTON

Welcome back for the second day. I hope you had a good time at the reception last night. Before I turn it over to Michael Swaine to introduce the next panel I wanted to remind everybody that if you have not done so already please try app. If you don't know your password, the app desk can help you. If you don't know the email that you registered with, the app desk can help you. If you need an iPad the app desk can help you. In other words please go to the app help desk if you need help. We've I think had good results with the app and really want to continue to use it and make everybody practice, so that when we do the session on prognostication this afternoon we will have a good sample. So with that I will turn it over to Michael Swaine to get things rolling this morning.

MICHAEL SWAINE

Thank you Toby, thank you very much. Good morning. Thank you all very much for coming. My name is Michael Swaine. I am a senior associate at the Asia program in the Carnegie Endowment. I work primarily Asia and China related national security issues. And I will be moderating our discussion this morning. And as you have seen in your program, the topic of this session this morning is Managing Strategic Frictions of China's Periphery. This is a vital topic. It is not per say a nuclear topic but it is certainly related to nuclear issues, China and the United States being major nuclear powers themselves. As we know China's emergence as a global power and one that is beginning to project not just economic but also military influence especially in the region in the Asia specific poses serious potential and actual security challenges to many states on its periphery and these challenges create dilemmas for the United States which enjoys alliance relations with many of the countries in the Western Pacific and along China's maritime periphery in particular.

The United States is an Allie and a partner of many of these countries and it has acted as security guarantor in the Asia specific area in the maritime theatre since the end of the Second World War so the question here is, how should the United States and its allies interpret China's emerging capabilities in the Asia specific region? Both military and otherwise and its policies towards other countries in the region. How should the United States and these other States respond to Beijing's rise. Is the US re-balance a good response and a good strategy to deal in part with China's emergence as a major regional power? Which sources of tensions could potentially escalate to confrontation and are most in need of active management?

These are the kinds of questions that we want to address in this brief period that we have this morning and to do that we have three superbly suited individuals to engage in a discussion based on their practical experience and based on their knowledge in particular of Asia and of the US - China relationship. To my right in the middle is Admiral Dennis Blair, he is chairman of the board and CEO of the Sasakawa Peace Foundation USA. Then he is an expert on Asia specific policy and he serves on the Energy Security Leadership Council, the Aspin Homeland Security Council and the boards of Freedom House and the National Bureau of Asia Research and the National Committee on US - China relations. He was formally director of National Intelligence of the United States. He has also served as President and Chief Executive Officer of the Institute for Defense Analysis prior to his retirement from the USA Navy in 2012, Admiral Blair served as commander and chief of the USA specific command, which is when I met him actually.

And to my immediate right is Mr. Kevin Rudd her served as an Australia's 26th Prime Minister. He led Australia's response during the global financial crises. He helped found the G20 when he was in office. He is currently a senior fellow with Harvard's University's John F. Kennedy School. He is undertaking a major research project of the US and China which is of great interest to me.

He is also a distinguished fellow at Chatham House and a distinguished Statesman with the Centre for Strategic and International studies. He is also President of the Asia Society Policy Institute. And as I think many people also know he is quite proficient in Mandarin Chinese.

The third member of our discussion group is Admiral Stapleton Roy on my far right. As you can see he is not General Zhu Chenghu.

J. STAPLETON ROY

Nor is he an admiral.

MICHAEL SWAINE

Nor is he an admiral!

J. STAPLETON ROY

I am an ambassador, Michael.

MICHAEL SWAINE

I will get to that. General Zhu was unable to join us unfortunately and surprisingly for himself as well as us, he was unable to receive approval from his National Defense University to travel to the United States at this time. So Ambassador Roy has very graciously consented to sit in for General Zhu and channel the Chinese view on certain of these issues. Many of you know Ambassador Roy; he is a distinguished scholar and founding director of the Kissinger Institute in China and the US at the Woodrow Wilson Center here. He was born in China, spent much of his youth there. He is also a distinguished former Foreign Service officer. He retired after 45 years in the US Foreign Service with the rank of Korea Ambassador, the highest in the service. His ambassadorial assignments included Singapore, China and Indonesia. On retirement he joined the Kissinger associates here at the Woodrow Wilson Center, a strategic consulting firm and then joined the Woodrow Wilson International Centre for Scholars to head the newly created Kissinger Institute.

He is also a trustee. We are very privileged to have him as a trustee of the Carnegie Endowment for International Peace. Now I would just like to say a word about the format. We have only here less than an hour and fifteen minutes now. We are going to use about 40 minutes or so for a discussion among the three of these gentlemen with myself moderating on this topic. After that we are going to take questions from the audience for approximately 30 minutes. So without any further ado I would like to start this discussion with the three gentlemen.

First I want to ask a question to each of them and hear their response. I'll begin with Kevin. I'd like him to give us sense of what he sees as strategic challengers post to the Asia specific by China's growing regional military capabilities and its dispute with its neighbors, but particularly to look at how this has implications for the political diplomatic and economic dimensions of the issue. Kevin?

KEVIN RUDD

Sounds like the history of the Western novel in five minutes, but we will give it a go. I think number one and I will dovetail here a bit with Stape, I think, in the absence of Zhu Chenghu and try outlining how I think the questions you've just spoken of as seen in Beijing. And therefore how the rest of us respond to what I think is an emerging Chinese strategic view. Number one, a point I'd lead with is conference and gathering, is an observation with which I think is generally

accepted now but less so in a year or two ago. When we look at Xi Jinping, we are not looking at any Chinese leader alike we've had for the last 20 years or so.

This is not just a Chinese leader who is significantly powerful. He is at least the most powerful since Deng. And I think it is fair to say is emerging as a political leader as powerful as Deng. And the reason that I say that is it is very important therefore to understand that Chinese policy both foreign and security policy is at present not static but dynamic and many of us who are familiar with following the Chinese policy debates over many decades now are accustomed to Chinese shifts very much occurring over an extended period of time and watching slow evolution. That is not the case and as far as sharing things, personality or policy predilections are concerned. Secondly, it is to understand therefore what his priorities are. And to be very blunt his number 1, 2 and 3 priority is to retain the central authority of Chinese communist party which he knows full well has been deep challengers of legitimacy because of endemic corruption and also more recent concerns about the party's performance on a range of domestic questions including the ability to continue to generate high levels of economic growth. And its flip side also, which is to manage environmental pollution in a way which simply doesn't cause massive public reaction. And this by virtue of party opinion poll research they now know there is a huge pervasive daily topic of conversation. Not just in Beijing but around the country.

So when he looks there for continued legitimacy and the position of the Chinese communist party to which he is personally dedicated. Not just as a convenience instrument but as a vehicle of ideology. He knows that there are these challengers to legitimacy and therefore a huge slice of his energy goes in this direction now. The second priority is this massive task of re-gearing the Chinese economy from its old growth model to its new growth model. He was seen at a public debate to which there is no question marks about the substantiality of Chinese economic growth levels. There are multiple contributing factors for that. But again if you were to go to the standing committee of the Politburo and sit around it. There is only seven of them and could fit comfortably on this stage, then frankly the sustaining reasonable levels of economic growth by which we mean growth levels north of six. During a time of deep transformation and structural adjustment as they seek to re-engineer China's economic model from the past to the one that they have devised for the future is a formidable task and that occupies a huge slice of their time as well.

Which brings me to probably the third priority and that is to do that they wish to maximize strategic stability from their perspective, because they see this as "a period of strategic opportunity", that is the official term in the Chinese security policy lexicon and economic policy lexicon. And therefore is one in which China is to further consolidate its economic power. And for reasons such as that, that whatever has happened in China and Japan relations in the last two years has by reason of strategic decisionmaking in Beijing been deescalated. I think folks in Beijing saw this as getting too close to the why during the events of 2013 and 2014 and as a result you will now see a whole range of external manifestations of that decision, not least of which is the trilateral with the foreign ministers in Seoul in the last week and more to come on that score.

And just to then flip down through the rest of the region briefly, the South China Sea is more of an open question. They do not see the security policy tripwire as being acute there as they have seen it around Senkaku Diaoyudao. And it is a consequence I think you will still see to continue the assertion of China's territorial claims, but always with this caveat fall short of a hot security crisis of one form or another.

My final point in terms of the security policies sort of radar screen. Looked at it from China's point of view and not entering the question of Chinese strategic nuclear forces. At this stage of our conversation is that if you flip around the dial what the Chinese also see is a merging set of strategic challenges and opportunities with their unresolved land border with India. President

Obama had a highly successful visit to India in January. Prime Minister Modi heads off to Beijing in May. And there will be an open question as to what China now does in response to what is seen as a successful diplomatic initiative on the part of the United States. And if I was making a bold projection, which I am sure will be easily disproven with the passage of time, do not rule out the possibility of a significant move in relation to the resolution of the land border. And the reason deeply in the geopolitics of it is when Xi Jinping looks at the history of how China's strategic environment has been consolidated and made better over the last quarter of a century or more – he is a deep student of his own country's history and his party's history – he looks with great admiration at what Deng did with the Russian border or the then-Soviet border back in 1989 and concludes from that with the resolution of that border China security circumstances fundamentally changed. If it was possible to find a landing point with Delhi, I wouldn't rule that out as a possibility

Which brings me to conclude on the Russia question. This is more than I think simply a temporary relationship of tactical strategic convince. I think it would be complacent in Washington to conclude that this will not develop into something further. What further I do not know and I cannot predict it at this stage. But if you were to put down on one side of the page the things where common strategic perceptions and interests line up against those on the other side of the page where there are continued deep frictions I would not necessarily say that the latter continues to outweigh the former. In fact, I see the commonalities for reasons of domestic concerns about color revolutions through to external concerns about the position of the United States as increasingly aligned if we get onto the commonalities of energy security and energy supply coming out of Russia itself.

So to sum up party consolation first, get the economy right, maintain strategic stability, deescalate with Japan, and continue to assert policy interests in South East Asia and the rest as discussed. But the final point is this; there is however I think a new level of global activism in Chinese foreign policy and the students of Chinese foreign policy. If you want I think the best doctrinal statement of what it is about is Xi Jinping's statement to the Foreign Policy Work Conference of the Chinese party and state apparatuses at the end of November last year. Which is the best encapsulation, I think, of the new activism which underpins the foreign policy association of China's interests. But I think the economy first, the growing economy in the region of Chinese economic influence, politics following the economy, foreign policy following politics and in time from China's perspective the security policy interests follow accordingly. I'll leave it there.

MICHAEL SWAINE

Thank you Kevin. Before responding and dealing with some of the points that Kevin has made I would like to ask Denny if he would basically address the same question. What sort of strategic challenges do you think are emerging in the region as a result of China's growth? Focusing in particular on your understanding of the military security dimensions of the issue.

DENNIS BLAIR

Thanks Michael. I think it is worth remembering that these territorial disputes in East Asia with the exception of Taiwan are not really classic irredentist issues. They don't involve lost homelands, large populations. They don't even involve high economic stakes, relatively modest hydro carbon resources around the islands and the East of South China seas. Rather they are matters of national pride. They are indicators of national prestige and there are issues of political importance within all the countries that are involved. Now most of these involved islands with few or no inhabitants. And they have been managed three ways over time in East Asia. The first way is treaty agreement: 1979, 1990 agreements between Malaysia and Thailand, for example. It is a series of agreements between Singapore and Malaysia over the years. In

2014 a fisheries agreement between Taiwan and Japan. So some of these are solved by classic compromise and diplomatic negotiation.

The second way they have been managed over time is a tacit agreement that there will be a diplomatic solution that military forces are simply not going to be employed. That complaining is about the highest level of aggression that will be seen from either side. Certainly the Kuril Island and northern territories are in that category between Japan and Russia. I would say that the same is true of the Dokdo Takeshima dispute between Korea and Japan.

The third way in which these disputes have been handled have been by military stand offs. Military preparations strong enough that the country that has physical position of the island has a good chance of being able to repel military aggression by the other country that claims that resulting in a lack of incentive or nothing really happening militarily. This has certainly been true of Taiwan for a long time and I would say it is now true for the Senkaku Diaoyudao dispute between China and Japan. It is also works for half-islands and Korea peninsula where the standoff is going on since the 1950s.

So those are sort of the three ways in which these territorial disputes have been managed and that brings us to the South China Sea in which none of these three ways has really been decided upon yet or worked out by the participates. There are tremendous differences on how the current round of disputes in the South China Sea happened after the 2002 agreement to handle them diplomatically. Things turned worse in recent years. If there is questions about who started it there is certainly no question about who is making a game now. China is responsible for about 80% of the aggressive actions that are being taken in that region these days. It is not using military means it is rather using administrative declarations, civil organizations such as coast guard and fishery enforcement vessels. Even commercial means, oil drilling ships, dredges. The military forces are used very sparingly and in the background, but rather this is being worked out in the grey zone as the Japanese plays it.

Now China has been making a game in this area and South China Sea. The American response has been quite tentative and week and I think it doesn't recognize the important American interest in the region. Should China achieve the full range of its territorial ambitions in the South China Sea then America, in fact all seafaring nations' access to the region would be severely restricted and controlled by China much to the disadvantage of other countries.

So what do we do about this? I would propose that we return to some of the classical ways of handling island disputes. But take a jump step, I would propose that an international conference be convened with a claimant nations supported by other seafaring nations like the United States, Japan, Australia and others. China should be invited. And the objective is to work out a rough international solution of claims in the South China Sea and that this conference be locked behind doors and not let out until they do it. Again China would not participate but I think the other countries based upon general precedents and standards could come up with a set of territorial seas, economic zones, and joint development areas which would roughly fair to the claims of all concerned. And then I think that the claimant nations themselves should act as if the results of that conference were in fact there territorial seas or exclusive economic zones and the rest of us should recognize the legitimacy of that conference and support the actions that are in accordance with it and oppose those which are not. I think this would return the classical ways of handling disputes like this to the South China Sea where they are currently dominated by these grey zone interactions on individual islands, administrative claims, appeals to the UN convention on the law of the sea.

And it would get us back on a track in which we could put this important area in the category of the other territorial disputes which I would say have been very well managed within the region.

MICHAEL SWAINE

Thank you. Now turning to Ambassador Roy I would like to ask the same question looking at the region, what do you see as the major strategic challenges emerging and in particular addressing the question of your interpretation of how the China might look at this. And this of course relates to what Kevin has said to a great degree.

J. STAPELTON ROY

Thanks Michael. From an American perspective to deal with these strategic challenges it is important that we also understand how China views the issue and I am sure that General Zhu would be delighted if I made a stab at giving you a sense of how China looks at the strategic picture in East Asia and the world. First, the world is changing. The center of gravity is shifting from west to east in favor the developing countries with China in the lead of those developing countries. The global system needs to adjust to reflect these changes. China now has the second largest GDP in the world or the third largest if you treat the EU as an aggregate economy.

Even with a slower growth rate China will soon surpass the GDPs of the US and the EU. Deng Xiaoping's admonition that the country should keep a low profile and concentrate on economic development was suitable for the first three decades of China's reform and openness policies. But that time has now passed. China now needs the active foreign policy of a major nation co mentioned with the countries growing wealth and power. China's interests are best served by buying into the existing global world order but at the same time it must change that existing world order to suit the changed world conditions and China's own interests.

Nevertheless, China's vast population means that national rejuvenation in China will inevitably make China the strongest country in the world with the largest economy. This is not a vigorous ambition it is simply a natural development given the nature of Chinese population. China faces numerous challenges. It has land border with 14 countries and potential security threats from major off-shore countries such as the United States and Japan. Four of its neighbors already have nuclear weapons aside from the United States. The United States has passed its peak but remains economically and militarily very powerful. China needs a peaceful environment and decent relations with the United States in order to meet its long-term goal of achieving the GDP of a middle income European country by 2049, the 100th anniversary of the establishment of the PRC. But at the same time, it must resolutely uphold its sovereignty and territorial integrity.

But the United States is blocking China at every turn. It seeks to maintain its naval and air superiority over China thus denying China the ability to defend its own territory. It has been interfering in the Taiwan issue for 65 years and continues to sell arms to the island in violation of its undertakings in the August 17, 1982 joint communiqué. Despite its insincere rhetoric it opposes China's growing international role and influence. The United States seeks to insight and embolden its Asian allies and to confront China while maintaining its own contacts with China. As a result, strategic competition between China and the United States is increasing. The United States first paid lip service to but is now resisting China's proposal for a new type of major nation relationship that could limit such competition based on the principals of no conflict, no confrontation, mutual respect and win-win cooperation.

China believes that the changed circumstances in Asia require the establishment of new security and cooperation architecture in Asia and the Asia Pacific. While Asia should remain open to other countries, Asian countries should take the lead in running the affairs of Asia. China's recent proposal for an Asia infrastructure development investment bank and the building of a Silk Road economic belt and a 21 century maritime silk road demonstrate that China seeks to promote the economic integration of Asian countries and deep in regional cooperation. The United States should work with China rather than resisting change and seeking the whole of China down. So you see that China's perspective on the region is somewhat different to ours. We

talk about China's aggression in the South China Sea, from China's stand point it has been sailing through this islands for centuries. It was mapping them and naming them at a time when all of the other claimants were colonies of European countries or the United States.

Defending your own territory and your sovereign claims is not aggression by any definition. So Americans distort the way that China is looking at the issue from China's perspective. Now I have been giving you a Chinese perspective. I have myself an American perspective. So I would not present the issue the way that I have just presented it to you but I think it is important to understand how China looks at the issue because it is not an irrational approach. It reflects a way that if you were Chinese you might look at the issue as well. And as the Chinese adage goes, Admiral Blair I am sure is aware of it, if you want to win 100 hundred battles you need to understand the other side and you need to understand yourself. So I was attempting to give you a sense of how the other side looks at these issues. Thank you.

MICHAEL SWAINE

Thank you Stape. I think you channel General Zhu quite well.

KEVIN RUDD

It underlines the point as why we need senior Chinese at forums like this. I would just like to say to our Chinese friends that it is really important to have China's voice at gatherings like this. And hopefully that will change in the future.

MICHAEL SWAINE

I would like to talk up the point that you touched on but we haven't really addressed in any detail. And that is the United States and US policy in addressing these issues. Kevin has spoken about different aspects of US policy in the region, relations with India, but I'm interested to understand a little bit more about how you look at the US position in the region today? How you think the United States should adjust their policies, if it should in the near to medium-term to deal with this dynamic situation? Denny has mentioned that he believes the US response in the South China Sea is tentative and weak. So I would like to get a better understanding of how you characterize the US position today and its policies and where you think they might go as briefly as possible? Kevin could you comment on that?

KEVIN RUDD

Yes sure, the last thing people welcome is former prime ministers landing in their country and telling them how to run it, so I will just be a little circumspect in what I say. My friend Gareth Evans over there will be less circumspect later on – good to see you here, Gareth. One point about America's perception in the region – and I don't think it is well enough understood here in DC – it is not a political point, or a foreign policy point, it is an economic point: China is the number one economic game in Asia. That actually is a transition that has been occurring over the last decade. It is now a reality. Therefore when the region looks at the question of China and the United States understand the game has shifted.

I just needed to say that very bluntly and very loudly. It is an objective fact. But here is a simple number which is a global number of how many countries in the world have China as their largest trading partner? 123. How many have the US as their largest trading partner? 64. If you were to go through Asia I think you would probably find China ahead of the United States in every single economic relationship, ever single trading relationship as of now.

On the investment front, understand this as well. That game has now changing. China is now the world's second largest destination for foreign direct investment. Well that has been the case on and off for quite some time. China is now the world's third largest source of foreign direct investment and rapidly changing. And it is not just private firms at it, if you look four trillion dollars in China's foreign exchange reserves and the fact that these will not permanently remain in US treasurer notes that they will also be looking for other forms of constructive investment from their perspective in maintaining the value of their reserves and then they are actively through sovereign well funds and other mechanisms looking at how to deploy an extraordinary amount of capital, even if it is just a proportion of what I've just described. So I believe the investment game is changing as well.

Let me go into a third element: the renminbi. There is an assumption in the US that the US dollar is permanently unchallengeable as the reserve currency of the world. I don't think that that is the view in China. There is an internal debate about that and certainly led by very sober individuals including Zhou Xiaochuan who is the governor of the People's Bank of China, who looked at these things in terms of global long-term macroeconomic stability. But they're a ways off from any immediate liberalization of the capital account. But if you look at the immediate term as to what China has now done with our 24 different bilateral currency swap arrangements around the world and the use increasing the renminbi as a currency for trade transactions. The renminbi now counts for 15% of the total volume of trade transactions around the world, in other words, not intermediate through the US dollar. Now where does that go to all the time in terms of the currency and capital? Open question.

But here is my point, the economic nature of the game is changing in a very fundamental way and therefore this is a big reality in the minds of most governments that I visit in the region. Mind you I haven't visited mine most recently but that is because I came second in the last elections. So a point about the framework for the relationship: Xi Jinping, I think building on the Stape's very good exposition before, is a highly rational individual. Given what both Stape and I have said about the framework which he brings to bear on China's strategic challenges and opportunities in the region and the enormous array of domestic challenges he currently confronts, there is I think an opportunity to develop what I would describe as a broad common strategic narrative between China and the United States which is capable of accommodating differences which cannot be resolved in the foreseeable future, maximizing cooperative endeavor with the objective long-term of using the political and diplomatic capital from the second of those arms to try and, shall I say, build strategic trust step by step.

It is not a Pollyanna-ish of the world. I mean in terms of South China Sea, everything that we have been discussing here is a real hard edged national security sovereign interest question at play. We can't just sort of brush that away in some sort of kumbayah moment. It is just not going to happen. But what I think is and it is certainly in the strategic mind of somebody like Xi Jinping, who self-describes by the way as a grand strategist, it is a very important consideration, is how in fact we craft a strategic framework between the United States and China for the long-term which they can make sense of internally but which also has utility in terms of managing irreconcilable differences now, building on what is quite an emerging array of common strategic, economic and other interests, and then trust building overtime.

The framework that I've been working on for the Harvard Kennedy School for the last year is nothing terribly flash but it is basically constructive realism for a common purpose. Realism about the hard stuff, constructive about the things you can do together with the view to a common purpose being evolved by step by step building strategic trust overtime. It is not perfect but I think one of the deficiencies at present is that we internally, by which I mean the United States here, have a quiet internal narrative about what we think China is up to. They, as General Zhu Chenghu/Stapleton Roy said just before, have a well-developed internal narrative about what they think the United States is up to. I don't see any common narrative at present.

frankly. And it is useful to have one if simply to maximize the prospects of strategic stability for the shorter term. Frankly, I think is a mechanism for transforming this relationship over time.

J. STAPELTON ROY

Yes I would just add onto that Kevin, it is true that China's economic prowess has made a big difference within the region but it's a limited region. No country that I know of or that I've talked to with a couple of exceptions wants China at this stage to be the leader the general economic system in East Asia. The only respect they pay to it is economic prowess. So they sort of balance off the figures that you cited with the sort of East Asia that they would like to live in, because on top of China's economic prowess and mercantilist, often oppressive way certainly of treating their own people and often of treating other countries. Australia itself is in this dilemma that its largest partner being China and its long-term security being the United States.

KEVIN RUDD

We have never seen this as a dilemma by the way; we just walk and chew gum at the same time. But there are countries a lot smaller than us in the region, all I'm saying is money speaks and I'm just trying to make a very aggregate point here about how things are shifting. And where it lands I am not sure but if you are looking at it from a classic old Soviet point of view: the correlation of forces. I haven't heard that term since I was in short pants. This is shifting in a negative direction from a US perspective and we need to be simply mindful in crafting strategic frameworks for the future.

MICHAEL SWAINE

I think that is true, but I don't think we should extrapolate the last 10 years into the future. As you know and as you said, China is having to go through a tremendous wrenching change of its model. The old "assemble products to be sold to the United States and other countries and invest in infrastructure" model is dead and the third planning was a very dramatic case of that. So I think that the future will not be like the past economically. Japan is transforming with urbanomics, China is having to transform, the United States must make an economic transformation. And the question is who can do that successfully so that the future projections of economic growth become settled in the minds of the countries themselves and those who are observing. And I am not necessarily sure that I would bet on China.

KEVIN RUDD

Can we hold on that one for one second? Just one point on the economy. It is an open question how the Chinese economy will land. And my friend at Harvard, Larry Summers, quite a brilliant paper he has put out last year on the dangerous of extrapolation. But we have been warned of the danger of extrapolation with China for the last 35 years and they have continued to extrapolate quite successfully. Now the growth rate is coming down. There is a whole bunch of reasons why we are not going to see 10%, 8% growth in the future. Question is how much, how sustainable, and will they be able to navigate through? All I am saying observing the region in 2015, I may be the bearer of bad tidings here but this is what is happening on the ground and in terms of regional economic architecture questions. Whether it is on the trade questions or the finance front. Whether it is a debate about the Asian infrastructure bank or whether it is a debate about frankly the future about TTP or FTAAP.

Underneath all of that is this massive thing happening and it's called Chinese trade investment activity. And even if growth comes down from eight to six – and six is the accepted internal, not official, but internal benchmark for what is necessary for social stability, it used to be eight or

ten – and that is still a powerful economical phenomenon unfolding across a whole of small polities.

DENNIS BLAIR

I think the perception is obviously there, that China's economy – many Americans now polled believe that China's economy is stronger than that of the United States. I think in the region there is perception of that and perceptions are important of course. You can't see long range on this. But I think that is an issue that has to be dealt with and Stape I would like to ask you as you listen to this conversation and you hear –

I mean on the one hand there is a strong argument to be made that China's economic influence is certainly growing in the region whereas the United States is still looked at as the primary security guarantor. So there is a potential disjuncture there. In terms of levels of influence, types of influence. How do you think the United States is positioned to deal with this issue over the near to medium term and even beyond that?

J. STAPELTON ROY

In contrast to some other geographic regions of the world, I actually think our policy framework for East Asia is pretty good. We are not trying to hold down China. We have over 500 billion dollars in bilateral trade with China. That is not characteristic of a country that you are trying to hold down. I think our problem is that the way the economy, the US economy which is inherently very strong, cannot generate the public funds necessary to have a balanced approach in East Asia. We talk about the rebalance. The rebalance is universally perceived in East Asia as a military rebalance because within a constrained government budgetary picture the military is better funded than the other departments of the government. The military will tell you that they are badly restrained themselves, in part because of sequestration. So I am making a distinction between the strength of our economy and the strength of our public funding for the necessary business of government, which includes the foreign affairs component. If you look at our six geographic regions in the State Department, the East Asia Pacific region ranks fifth in terms of the development funding available to it. Our biggest project in a sense is the Lower Mekong Initiative and we put several hundred million dollars into that. Japan with a smaller GDP than the United States puts more into it.

In other words, our rebalance in East Asia is largely a military rebalance and it is not intended to be. It is intended, and the East Asians tell us that they want us, to be more involved in the region where China's economy is so much a driver of growth that China's neighbors while benefiting from that growth are concerned about being overwhelmed by China's growing economic wealth.

MICHAEL SWAINE

So what would you like to see the United States do that that it is not doing to address some of these problems?

J. STAPELTON ROY

I think that we need to be better at adjusting to the necessary process of change, not appear to be fighting against it. To be a status quo power that with the world changing around us we want to maintain the post-World War II institutions and not make the changes. Our problem, again, is a domestic one. We can't make the changes because Congress won't approve the necessary changes. How do we address that question? Well I think our political candidates have to start talking about that. They talk about other issues. They don't talk about how the United States can remain a highly competitive country in a competitive world where China is in danger of eating

our lunch. And I think that is the number one challenge to our strategic ... [overtalking] it's a domestic challenge.

MICHAEL SWAINE

It is an important domestic issue.

KEVIN RUDD

Now our Chinese friends are deeply respectful of the power of the United States. I mean all of us who have been dealing with this relationship for a long time know that. I mean, Admiral, you would know that directly. And when you speak to our Chinese interlocutors, and I speak at National Defense University and Chinese Academy Military Science quite frequently, they are deeply respectful of Uncle Sam's military. These are deep strategic realists and when they look out to mid-century they still see the United States as this formidable and, in all probability, dominant strategic force in most categories of its kits, equipment, and capabilities. And if I was looking at this from an American point of view on the economy question, and frankly the demography and economy question, there are huge grounds for American optimism. Number one your population is growing and it is young. If you take this broader entity called NAFTA into a future lens and look at it by mid-century you are looking at an entity of an integrated economy of 600 million people. That is big.

Demography is working in China in the reverse direction. China's population will peak round about 2026 by the time we get to mid-century down to 1.2 and worst case scenario planning down to about a billion or just under. Assuming that the American economy continues to fire based on its enormous strengths in terms of innovation and the rest. Then frankly what I find in China when I talk about a fashionable thesis in Beijing, and I think quite a dangerous one in recent years, is that the US has been in a reversible structural decline. Is that there is now a deep reappraisal of that. Partly through your economic recovery but I think partly also because of the deep students of American history who are alive in Chinese think tanks and the official community.

So what I would say is frankly in the aggregate there is a hugely positive position for the United States to be in. So given China's perception, I think and Xi Jinping's perception of continued US power, frankly notwithstanding what I have just said about the economy and how US economic powers are seen within Asia, there is an opportunity frankly for these two elephants in the living room to work out as I said before a common strategic narrative which is not one which concedes fundamental US and allied interests, but one which does find a way through. And I think that simply requires diplomatic imagination.

DENNIS BLAIR

Michael, we have to mention this connection to the Trans-Pacific Partnership.

MICHAEL SWAINE

Sure.

ADMIRAL DENNIS BLAIR

Because how the United States will be received in East Asia heavily depends on whether or not we are successful in pushing through that agreement to final conclusion.

MICHAEL SWAINE

And that again is a domestic issue isn't it?

DENNIS BLAIR

It is a domestic issue but at the same time it does represent a very important non-military component in our re-balancing strategy in East Asia. And if it succeeds it actually is something that could be very beneficial to China because if China – to push through the domestic economic reforms China needs to remain competitive in a highly competitive globalized economy. It needs the type of high end trade provisions that are reflected in the Trans-Pacific Partnership. And there are people in China who recognize this and that is why they are showing interest in this. But if we fail on the TPP then we are going to have a double whammy to us where the military will remain the sole major component of our re-balancing strategy, and that is a dangerous situation.

MICHAEL SWAINE

We are running out of time. We are already into the Q & A but I do want to get some very brief commentary from Denny in particular. Get your view on what Kevin said a minute ago about US power in the western pacific, particular as a military nation. How do you look at the United States? Is it well positioned for the future in the western pacific? What do you see as the primary challenge to the past position of the United States as what has been the predominant maritime power in that part of the world?

DENNIS BLAIR

I think from a military position we are fine. Any Chinese military attempt to change the status quo of any these territories that are under dispute by force is an extremely high risk measure by China, would be defeated with big consequences domestically within China for having taken a chance and then failed. So I think the military balance has been and can continue to be for as far as the eye can see something that is not a temptation or a cause of friction. And then I agree completely with both Prime Minister Rudd and Ambassador Roy that the big game then has to do with economic diplomatic business commercial ties and you know let the best country win. And that is just fine but it ought to be done on a basis – I think if we are in this balance view this expectation that China either had surpassed, as some polls show in the United States, or will surpass by “X” date the United States, sort of has given a competitive, all we have to do and push the United States flavor in China. And if that re-balances, wait a minute we both kind of going to be there for a long time, let's work together, which I think is a necessary political backdrop to do these things.

MICHAEL SWAINE

Just very briefly, because part of the description of this whole panel has been how do we move forward in the future. one issue that has been central to the problems in the US China relationship that many people sight is the whole question of sincerity or trust. Now, people argue as to whether or not that really is that important; national interests are more important. But at some level a greater degree of confidence in an ability to reach an understanding of some type in the future will require a certain amount of confidence that the other side in this case the US China relationship is going to follow through on any kind of agreement. What single thing do you think could best improve the relationship, the US-China relationship in terms of building trust as we look forward? As briefly as possible.

KEVIN RUDD

Okay, what President Obama did last October I think is good. Have been calling for it for years myself but frankly these two agreements on the avoidance and management of the incidents in the area and incidents at sea is a very large step forward to, frankly, the possibility of conflict by accident. And the extension of those protocols, as I now see early reporting to suggest that they are, to China's engagements with the other, shall I say, other active militaries in the wider region, most particularly between China and Japan.

Final point is this, you cannot declare tomorrow in the People's Daily that as of this Saturday we are going to have strategic trust with the United States. I mean this is a country with two-and-a-half thousand years of deep strategic thinking based in Sun Tzu's Bingfa and six other military classics that basically says never trust the other bastard, okay? Okay and by the way when I read Von Clausewitz and the rest, quite frankly, there is a Western cannon which says exactly the same. So guess what? Both traditions are pretty pessimistic about human nature on this question. Therefore, my realist response to that, with a little tinge of liberal internationalism to one side, is how do you build strategic trust incrementally over time step by step? And I would simply take one matter at a time and a virtue of the outcome with the president's visit last November is that you got the first of those steps. I can outline about six or seven others that should be taken but all within a frame work of what I describe as constructive realism for a common purpose.

MICHAEL SWAINE

Denny?

DENNIS BLAIR

I think strategic trust is highly overrated.

KEVIN RUDD

I thought you would say that.

DENNIS BLAIR

I don't think you need it. I don't think you're going to get it between the United States and China. I agree completely with Prime Minister Rudd that you just work it out an agreement at a time based on realistic expectations and enforceable and verifiable things that you are doing and you move forward.

MICHAEL SWAINE

Stape?

J. STAPELTON ROY

I am a little bit more optimistic than Admiral Blair in terms of how you deal with it.

DENNIS BLAIR

That's not hard.

J. STAPELTON ROY

Because as a diplomat I put the burden on the military side. The real problem that is driving the growing and strategic mistrust between China and the United States is the fact that China is

building up its military based on the premise that China needs the capabilities to defend itself. And that is beginning to impinge on our ability to maintain the credibility of our alliances in East Asia, which are necessary to remain credible if China's rise is going to be a peaceful one. So the question is, is there some way in the future to enable two powerful militaries to co-exist in the western pacific in ways that don't constantly drive an arms race and a strategic rivalry? So you have to deal with the military component.

But in my judgment it is impossible to deal with it as a purely military question. So you have to deal with it as an issue of grand strategy bringing the political and economic component into it. Why is the political important? Because when we had our breakthrough to China in 1971 and '72, all of a sudden China's assets which had been part of the hostile forces that raid against us became positive assets in our competition with the Soviet Union. In other words, the very same assets changed because of the change in the nature of the political relationship.

So to build trust you have to deal with the military component but you can't solve the problem within the military component alone if you aren't building a political relationship in which you don't see each other as having the intention of aggressing and infringing on the vital interests of the other side.

MICHAEL SWAINE

Great, thank you very much. I am very sorry we have eaten into the Q & A but I thought that this was an interesting and valuable enough discussion to have us do so. I am not quite sure on how we proceed in terms of – I think I will select the people. Please be brief, as brief as possible. Identify yourself, we are talking less than one minute and we need questions probably addressed to anybody on the dais. Thank you. Yes sir.

GARETH EVANS

From Gareth Evans from Australia. At the risk of being un-circumspect as my compatriot painted me, let me just ask American colleagues, don't we need a mindset change in relation to China? Not just about the imminence of Chinese economic primacy which has been the concentration so far, but also the reality that America's strategic superiority is simply not going to be indefinitely sustainable. How long will it be before we hear any American leader saying at a presidential election campaign what I heard Bill Clinton say at a private function 15 years ago, just after he left the presidency? Namely, America has two choices in the way in which we exercise our huge economic and military power. Choice number one, seek to use it to remain top dog on the global block in perpetuity. Choice number two is to use that enormous economic and military power to create a world in which we will be comfortable living when we are no longer top dog on the global block. My experience is that that kind of language is just not usable language in the American political scene. But if it was used it seems to be it would be enormously helpful in creating the kind of environment we all want to see for the long haul with China. Will the American colleagues please come in?

DENNIS BLAIR

You know it is interesting, I was the commander in chief for the Pacific Command at the zenith of American power when we were the hyperpower and I got to tell you, it didn't feel very hyperpower-ish. You've got problems, you've got things you've got to work. You've got to find your friends. You've got to try to – I mean it's – maybe the PR side of it has to use words like you were talking about but the practical business of exercising your military economic and diplomatic activities in a region is pretty day-to-day deal with lots of country stuff. So maybe it is a case of presentation but I think the United States is not the way it was in 1990 and it is not the way it was in 2000. It is adjusting to the fact that our relative power is diminishing even as

our absolute power is probably increasing and that is happening by the force of events. So whether we actually ever put a political tag on it, you politicians know that that is not exactly a winning formula: we're number two, but we're tied for number two. But the reality of how you work is pretty cooperative and not very imperial in my experience.

MICHAEL SWAINE

Thank you. I want to try to get in as many questions as possible. Yes sir.

TONG ZHAO

Tong Zhao from Carnegie Global Tsinghua Center. Just recently the commander of US 7th fleet, Vice Admiral Thomas proposed this new initiative of joint multinational sea patrols lead by other nations and to be supported by the US 7th fleet in South China Sea which was obviously not well received in Beijing because it obviously excludes China from this proposed joint original endeavor. So I was wondering as the most recent example of I guess US re-balance to Asia, how do you think the US should manage its signal-sending to China that can't avoid a Chinese misunderstanding of US strategic intentions. Thank you.

MICHAEL SWAINE

I think that is a question both for Denny and Stape as well.

DENNIS BLAIR

Well I mean China was invited and participated in the room in the Pacific exercises in Hawaii last year. The largest naval exercises. I would think that Chinese participation in exercises in the South China Sea that involved a lot of seafaring nations both on the South China Sea and elsewhere would be a good idea. I think it matters as to what it is you are exercising when you are there. This ought to be concentrated on missions that you are liable to do together, whether it be response to the many disasters in the region, peacekeeping exercises working against piracy the way we are in the Gulf of Aden patrolling the seas so that they are used for lawful purposes and not used for unlawful purposes, and I think that all of that is to the good no matter where you do it: Guam, South China Sea, East China Sea or in Hawaii.

J. STAPELTON ROY

I will just briefly add, the US approach in the South China Sea essentially rests on freedom of navigation, rule of law and non-use of force. Our secretaries of defense have specifically outlined this type of approach. Rule of law ought to be really pushed by the United States as the core of our approach. Because it will ensure freedom of navigation and China is not opposed to rule of law. You can find statements on their side in which they wish to have a rule of law based approach to the South China Sea. The trouble is there is some domestic disputes in China over whether or not that is appropriate if China has more expansive claims. If you take this approach you can have various military patrols in the area which are compatible with the commitment of all of the countries in the Declaration on the Conduct of parties in the South China Sea that they all signed in 2001 to not use force, to resolve problems through peaceful means.

If that is the case, naval forces can operate in the region without threatening anybody else but they can also serve as the deterrent to countries that might want to use force to settle these problems. So there is a framework within which one can deal with this, but it involves things such as negotiating a code of conduct in the South China Sea which all of the countries including China are committed to but they haven't yet brought to fruition.

MICHAEL SWAINE

Thanks Stapelton. Will?

WILL NORRIS

Will Norris from the Carnegie Endowment. Being that this is a conference on nuclear weapons I want to inject a little bit of nuclear thinking into this particular panel. I wanted to hear your thoughts on what I think is a very low probability to event but significant nonetheless were it to occur. If you can tell us your reflections a little bit about where the most likely points of conventional conflict between the United States and China lie over the next decade or 15 years? And then within those conventional conflicts, what you see is the most likely potential pathways to a nuclear escalation?

DENNIS BLAIR

I think the chances of nuclear exchange between the United States and China are somewhere between nil and zero. I just don't see the ideological reasons which underlay a large part of the Cold War, the theoretical considerations on both sides or the geopolitical issues in the region. I am getting to the level that neither country is going to risk the destruction of a retaliatory strike in order to solve. It is just incomprehensible. I would say that some of the same rationale thankfully is leading over into the cyber level where the chance of damage on a wide scale, civil attacks using cyber are equally destructive and I would hope that it would also go into the space regime as well, where there could be a lot of damage to everybody if war escalated to that.

And as I said, on the particular issues that are between us, we've sort of worked out military standoffs that make the initiation of conventional war not worth it for either side. So I don't think we're going to get into a war with China, much less a nuclear war.

KEVIN RUDD

I think there's a huge wisdom in what the admiral has just said. The Chinese nuclear doctrine on No First Use is so deeply entrenched within the political and military establishment in China that it's almost biological, so that's the first point. But can I just say that a very smart way to entrench that for the future, given that I'm in Washington, is please get the Senate to ratify the Comprehensive Test Ban Treaty. Just please. Please.

J. STAPLETON ROY

Could we throw the Law of the Sea Convention in also?

KEVIN RUDD

And before we go onto that state, I bit my tongue when the Americans said the Chinese were doing well in observing elements of international maritime laws, can you please get the Senate to ratify UNCLOS, and when you're at it, when you're at it get the Senate also to think about China's quota at the IMF. Because if you're worried about the emergence of an Asian infrastructure investment bank, this is in part a Chinese geopolitical reaction to the door being slammed in China's face over expanded mandates or expanded quotas both at the Bank and the Fund. And so please, just fix that.

MICHAEL SWAINE

Done.

KEVIN RUDD

And as an American ally, I'm sick and tired of going to Capitol Hill and Americans say, "Well Kevin, you know that's just not going to happen." Well, you might have been able to say that once, but the rest of us, as your allies and friends in the region are saying, "Guys, it can't just be that way for reasons of American domestic politics." These are big questions affecting all of us.

MICHAEL SWAINE

Yep, yep. Amen.

J. STAPLETON ROY

Michael, let me just throw in one point.

MICHAEL SWAINE

Very briefly.

J. STAPLETON ROY

We did not get into direct conflict with the Soviet Union during the Cold War, in part because neither side knew how to manage escalation. The same constraints will apply to us and China in terms of direct conflict. The danger is proxy conflicts, where they back a party that is attacking someone else and we support the other side. Proxy wars took place throughout the Cold War and there is a danger of proxy wars taking place in East Asia

MICHAEL SWAINE

My apologies to both groups of people in the wings. With the lights here, I was not as aware as I should be. Sir, over there, and then I'll go over here, but we're fast running out of time so you'll have to be very brief, please.

ZAFAR JASPAL

My name is Zafar Jaspal and I am from Pakistan's Quaid-i-Azam University. My question is straight to Dennis Blair. [unclear] you have talked about the rebalancing and we have heard these kinds of things. In this changing world, is the United States going to rely on its allies in this region? Especially when many of the United States strategic partnerships in the Asia have a big economic interest with China, like 80 plus billion – I am talking with reference to India – and when President Obama was visiting India they didn't show the Agni-V. In such a situation, how do you understand your allies' potential to multiply your potential in order to balance?

DENNIS BLAIR

I think we've been working with our allies and partners pretty skillfully in East Asia over the years and I expect that to continue. And from the allies' and partners' point of view themselves, I think Prime Minister Rudd's idea that they can walk and chew gum at the same time is a pretty good one, so I think we can do it.

MICHAEL SWAINE

I'm afraid this is the last question, over here please.

MUHAMMAD UMAR

Okay, just, kind of, from the Chinese perspective you know, when you see ...

MICHAEL SWAINE

Can you identify yourself please?

MUHAMMAD UMAR

Oh, sorry. My name is Muhammad Umar, National Defence University Islamabad. From the Chinese perspective, when you see defense deals taking place with India, the largest Chinese neighbor, and maritime deals taking place, isn't that seen as a challenge by the Chinese to their growing regional influence? And secondly, Prime Minister referred to the Chinese-Russian alliance as a strategic alliance, do we see that –

KEVIN RUDD

I didn't use the word alliance.

MICHAEL SWAINE

No, he didn't say alliance.

MUHAMMAD UMAR

Oh, sorry, well, if the disputes continue between China and Russia with Japan, the territorial disputes, do we see that expanding, that alliance? Or do we see an alliance taking place?

MICHAEL SWAINE

Well these are big questions for which we have zero time, so can anybody make a very brief comment on either of those two questions? If not, we're going to have to have this off to the side.

DENNIS BLAIR

I think the point to be made is that there is a new dynamic, I think Asia and the world in general is much more networked than it is the old hub and spoke – and to this extent, Gareth, I think it's true that the United States doesn't sit like the spider in the center of the web and just send signals out, it's a much more complex relationship involve cross relationships which in many cases are as important as the relationship with the United States. So I think that the United States is going to have to get into the game of there being many power centers, many different, more subtle ways of operating than just sitting in Washington, making a policy, and then telling each of our allies or partners what it is.

MICHAEL SWAINE

Thank you. Thank you.

KEVIN RUDD

This year's September summit between President Obama and President Xi Jinping is highly significant. It's the third in terms of summits since this new Chinese president has been in, it's the first official visit – make the most of it. Because in the Chinese system, I go back to my very first comments here today, this leader has, I won't say unprecedented but near-unprecedented political authority, and if new strategic frameworks are possible in areas where you could build

some strategic trust step by step, as Deng Xiaopeng used to say [unclear, speaking Chinese] cross the river by feeling the way stone by stone, and this is the opportunity to do it.

MICHAEL SWAINE

Great, well on that positive note, we have to conclude the session. Please join me in thanking the panelists.