Managing itself disruptive giant

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Australians were certainly tested. The New Guinea campaign is an amazing tale of Australian heroism, resolve, and just plain grit, from the turning points of Milne Bay and the Kokoda Track in 1942 to the Japanese surrender to Generals Blamey and Sturdee in September 1945.

The events of World War II prompt a reevaluation about the present. For most of the past 70 years, Americans and Australians, having learned bitter lessons about the breakdown of world order, have tried to create global and regional security frameworks – and strong networks of economic ties – to preclude such a danger from ever arising again.

Not surprisingly, as years pass, the beneficiaries of those labours might take for granted that security and those economic opportunities.

Today, our global security, political, and economic system is suffering from rising levels of stress.

The century-old Middle East order has shuttered. The old states created by Sykes-Picot in 1916 have fragmented into tribes and sects, which are in the midst of a brutal struggle for power and survival, exacerbated and exploited by neighbours seeking local hegemony. Almost every Middle Eastern country is now a battle-ground or a battlefield.

The European Union has been convulsed by loss of control of its borders, a tepid recovery from the Great Recession, and a stressed monetary union. Political movements are fracturing the old centre parties. The tragedies of the Middle East spilled over to Europe, and terrorists from within and without haunt European societies. If Britain votes to exit, the EU will turn inward for years as it is buffeted by the shock waves.

Russia has violated a fundamental norm of the post-Cold War security order by more than its own territory from neighbours. Tempted to restore parts of its empire, a Russian strongman is bolting a weak and uncertain Europe. Even as Russia boasts of their revived assertiveness, they look anxiously to the south and east for movements that threaten Russia’s future.

The optimism of the Asia-Pacific has been shaded by uncertainties about China’s economy and by President Xi’s shift from Deng Xiaoping’s credo of “bide strong, ride time.” The unpredictable Communist Kingdom of North Korea threatens with nuclear weapons and missiles. A two-year flow of Islamist terrorists between east Asia and the Middle East feeds internal dangers in south-east Asia.

The US is in the midst of an unpredictable elections year. Leaders of both parties have treated the US-led security-economic-political order with disdain and ignorance. Would-be strategists in the US are struggling to reestablish America’s sense of direction.

Leadership Dealing with a rising and more assertive China will require the US and its allies to show resolve, identify mutual interests and manage differences, says former World Bank president and US Trade Negotiator Robert Zoellick in a keynote speech he was due to deliver to the Crawford Australian Leadership Forum at the Australian National University on Sunday before being kept away by injury.

The Australian Financial Review has this exclusive edited version of his remarks.

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developed economies such as the US and Australia. Chinese nationalists will be tempted to press for "indigenous innovations" that keeps foreigners out. But technological protectionism will cut China off from global innovation and markets, a reversal of Deng Xiaoping's development strategy.

When Japan pursued a domestic strategy for its telecom development, the results were poor. Let's pull these economic strands together.

In the near-term, I expect China will face a bumpy deceleration, not a hard landing.

But as Ravil Memon, the perceptive head of Singapore's Monetary Authority, has pointed out, China's debt — at about 250 per cent of GDP — poses a growing risk unless China can reverse its returns from fastening spending, and employment. That debt figure is up 800 per cent from 2008, with 70 per cent of the increase from corporations, especially state-owned enterprises. Local government debt also surged with infra projects to keep growth numbers high.

My diagnosis seems to have been confirmed by comments in The People's Daily out early in a column by a so-called "authoritative person" who also warned about China's reliance on debt-fueled growth.

At some point — perhaps over the next two to three years — if China's reforms are unable to restore confidence in growth based on a new, structural model, Chinese capital will seek to exit in disruptive quantities.

China had a taste of these trends over the past year, and the party did not like the implications for its successful stewardship.

In sum, opening up China's capital account, with a slowing economy, a debt overhang, and a financial system that is only partially developed is a very tricky business. The economic track record of China's leaders is impressive, and China's skilled technocrats understand the problems.

But President Xi and his colleagues will face staggering political economy decisions in the near future.

In the back of their minds is the reelection that the Soviet Union's 13th Five Year Plan was its last. Xi's top priority will be to get to number 14.

Of course, President Xi's modernisation plans for China extend beyond the economy. He has shaken up the leadership of the military, too, in part through his anti-corruption drive.

Xi has changed China's military command structure. He is forging joint capabilities among the services, with a greater emphasis on roles of the Navy and Air Force to develop "project power.

These military changes

likely to continue to grow. The US challenge has been to shape Chinese calculations of its interests as it expands influence.

Dr Silove also draws out a critical but often underestimated aspect of the US strategy — indeed, a key element of the whole post-War World II system — which is the fundamental role of US allies and partners. The "rebalancing" of powers in the Asia-Pacific in the face of China's rise and increasing assertiveness depends not just on US capabilities, but on that of US allies and partners as well.

Dr Silove describes the US shift away from the "hub-and-spokes model of asymmetric bilateral alliances that had characterised the security architecture of the region to... a federated network model in which the United States would lead a web of more powerful allies and partners with stronger links to one another."

These ideas are probably familiar in Canberra. Australia has recognised that allies and partners in the region are increasing their expeditionary capabilities and interoperability. Australia has been a leader in forging closer relations with Japan, India, South Korea, and ASEAN countries.

I hope Dr Silove's strategic insight might also reassure Australians that there is a sensible US response to China's rise other than accommodation through weakening concessions on the one hand, or inevitable confrontation on the other.

This strategy recognises that balancing and engaging China should be systemic.

The idea is to shape China's behaviour. The United States, its allies, and partners need to demonstrate resolve in the face of Chinese assertiveness while also identifying mutual interests and managing differences.

The frictions between China and the United States can, however, make cooperation harder. As Professor Wang Jisi of Peking University, the informed 'Dean' of China's scholars of America, has explained, it is increasingly difficult for those in the two countries who are knowledgeable about each other to clearly explain to their domestic audiences that the other side does not necessarily harbour 'evil strategic intentions' — and that "cooperation benefits both sides".

The US, Australia, and other partners need to suggest positive agendas with China, even while remaining clear and firm on Chinese actions that threaten security stability.

China's economic reform challenges offer a good place to start.

Our economic dialogue should explore how foreign firms — if given fair access — can help China develop its service sector, meet social needs, and expand consumption.

The Fifth Five Year Plan priorities environmental and health services, which should offer win-win opportunities for China and foreign partners.

If China pursues its technology, innovation, and workforce development goals, it has a good chance of shaping an open market model, with that should be opportunities for stronger FIP protections, cross-border investment, and education services. Education is Australia's largest service sector export and four-fifths overall iron ore, coal, and natural gas. The US now hosts over 300,000 Chinese students, more than from any other country.

Expanding cross-investment could be enhanced by adoption of the principles incorporated into international investment treaties, such as bilateral investment treaties or free trade agreements. Austra-

lia's FTA with China includes some investor protections, although considerably below the standards in the Trans-Pacific Partnership or TPP. The US negotiations with China for a high quality Bilateral Investment Treaty are supportive of China's restructur-

ing aims, and China's willingness to open up sectors for foreign investment will be an indicator of the country's commitment to rules.

China may also be interested in disciplin-

ing its State-Owned Enterprises with the rules in the TPP or suggested by the OECD's research.

Instead of the IMF adding China's RMB to the Special Drawing Right, or SDR, straight away, the IMF should have worked with China's financial market reformers to target liberalising goals as steps to including the RMB in the SDR basket. President Xi would have recommended an SDR Council to con-

vene with the International Banks and the masters of principal SDR currencies to consider market conditions and monetary policy interdependencies for China toward greater financial and economic cooperation as it proceeded with reforms. Such a group would be more useful than the G-7 or G-20.

The US also anticipate possible oppor-

tunities created by President Xi's "One Belt, One Road" plan. China's investments across Central Asia — including infrastructure for transport, energy, and water — could turn out to be a useful, corrupt boondoggle to export China's excess capacity — or an opportunity for development, expanded global supply, new service centres, and improved security. China also shares an interest in containing the violence and chaos in the Middle East.

Western firms such as Caterpillar and Siemens have averted such risks through China's "One Belt, One Road" initiative. New strands of exchange will be blocked by Chinese efforts to control the South China Sea.

Even the contentious South China Sea may be susceptible to reseamonnent. China's actions have mobilised opposition. The broad assertions of control within China's nine-dash line would make the sea look like a Chinese lake, which neither the US nor many other maritime countries will accept. At some point, China will need a rationale and opportunity to redefine its position in a way that does not involve territorial sovereignty, including lowering maritime power, China may find itself more interested in the US position on free-dams and freedom of navigation in their exclusive economic zones. The US, in turn, should be careful to state its systemic interest in the stability of the South China Sea, including the peaceful settlement of disputes, without tak-

ing aim to restrict the sovereignty of indi-

vidual islands.

South Korea, the United States, and China also have a joint interest in the South Korea missile launches, which are an affront to the US, Chinese, and North Korean scenarios, including the security of nuclear facilities in the event of North Korea's collapse.

Since Nixon and Kissinger re-established US ties with China more than 40 years ago, the US experience has been that the effective management of China's diplomacy is complex. Someone needs to look across the range of activities of China with an eye toward coherence and larger goals, involving both the US and its allies. That person has been at times the Asia Pacific Security Advisor, the Secretary of State, or even Secretary of the Treas-

ure.

Today, unfortunately, no one is handling the US-China portfolio at the top reaches of the US presidency.

Therefore, the next US President needs to recognize this need and to fill it. Another way to war closer Austra-

lian friends to convey that message to our president.

The Sino-American relationship is cer-

tainly not the only challenge we face in maintaining stability across the old world order. But if we do not handle that responsibly, our voice, the world, and all of us, will pay a high price.

Robert Zoellick is a former US trade representative, and former president of the World Bank.