

# ISAS Brief

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## President Obama's First Asian Visit

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### Abstract

This is the first of two briefs on the United States' evolving relations with East Asia – with the region as well as the countries in the area. The first provides the context in which United States President Barack Obama will undertake his first official visit to the region. The second will examine what the American president accomplishes during the visit and what its long-term consequences will be for the relations between these two important parts of the global economy. It should be noted that in preparing for the visit, President Obama consulted with Lee Kuan Yew, Singapore's veteran leader, who impressed upon him the importance Washington must give to economics, in particular to trade, in basing its relations with the region. The Obama visit comes at a time when China is leading the world out of what has come to be described as the "Great Recession". Its fast developing economy is intertwined in several different ways that call for good working relations between Beijing and Washington. These need to be based not on *ad hoc* exchanges between the two leadership groups but on solid and durable institutional arrangements. What we are seeing is the evolution of G2 at the apex of a new world order.

### Background

"Ever since taking office, President Obama has signaled that the United States wants to improve relations with the powerhouse nations of East Asia, and he'll put his personal imprint on that when he travels to the region for the first time next week", wrote John Pomfret for *The Washington Post* on the eve of the American president's departure for the region<sup>2</sup>. The approach the new American president has adopted is different from that of his immediate predecessor, George W. Bush. This is in two respects, although there is continuity in one area. President Bush occupied himself and his country with the Middle East and West Asia by waging wars in Afghanistan and Iraq. There was little time left for engaging his country with East Asia. Second, when he did turn to East Asia it was again in the context of pursuing his country's security interests. After having identified North Korea as one of the

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<sup>2</sup> John Pomfret, "U.S. is reaching out to East Asia's powerful nations" *The Washington Post*, 7 November 2009, p. A6.

three countries that constituted the axis of evil – the other two were Iran and Saddam Hussein’s Iraq – he devoted considerable time to pressuring North Korea to abandon its quest for nuclear weapons. China helped by becoming a part of the six-country arrangement for negotiating with North Korea. That said, its principal interest was in developing its economy within a global framework that was not disruptive. However, economics, a subject that was of little interest to the former United States (US) president, was not the basis for his administration’s dealing with the countries of the region.

The only part of the Bush legacy that has entered the policy framework being pursued by the Obama administration is the importance being attached by Washington to emerging China.<sup>3</sup> In fact, in developing a new international framework for formulating economic policies, Washington was pursuing a two-tier approach. It was working with China in what many analysts, including myself, had called the G2 along with effectively replacing the G8 with the G20. The G20 was made up of all the advanced countries that constituted the G8 along with a dozen large emerging markets. Four of the countries included in the G20 are from Asia, namely, China, India, Australia and South Korea.

The United States under President Obama sent a clear signal to Asia that the region will receive its attention on a priority basis. Secretary of State Hillary Rodham Clinton’s first overseas visit was not to Europe, the traditional starting point for most of her predecessors. Instead, it was to Asia where she attended the meeting of regional leaders that had been skipped by previous Secretaries. While there, she signed a treaty with the 10-member Association for Southeast Asian Nations, or ASEAN. However, as discussed below, for the United States signing a treaty with a foreign power is only the beginning of a complex process.

The methodical President Obama prepared himself well for his maiden voyage to the region as president. Among the several people consulted was Lee Kuan Yew of Singapore, who visited the American leader in the White House. After the visit, Mr Lee said that he told the American president, “if you do not hold your ground in the Pacific, you cannot be a world leader”. But working closely with East Asia and with the countries on the two sides of the Pacific meant placing emphasis on economics. “The business of Asia is business,” says Evan A. Feigenbaum, a former senior State Department official currently at the Council of Foreign Relations. “What you’ve got is an Asian challenge to Obama in the economics area that his predecessors didn’t face. Whatever good things the administration is doing – and they are doing good things – there is no substitute for economic management”.<sup>4</sup> In that area, the United States does not have a good record.

### **Basing Relations on Economics**

The most important issue in economics is trade. Here, the American record is poor. Its leaders have not brought to bear the kind of pressure the American political system needs to move initiatives forward through Congress. It took a lot of arm twisting by President Bill Clinton to get the North America Free Trade Area, the NAFTA, approved by the US Congress. The

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<sup>3</sup> In an earlier work for ISAS, I had suggested that China is rising for the second time, this time by not putting that much emphasis on external trade and the development of the private sector. Instead, China based its recovery from what was now called the “Great Recession” by focusing also on the development of internal markets, and by bringing the state back as a major player in economic managements. See Shahid Javed Burki, “The Rise of China: How It Will Impact the World”, ISAS Insights, No. 80, 6 August 2009.

<sup>4</sup> John Pomfret, “U.S is reaching out to East Asia’s powerful nations”, *Op. Cit.*

president got the approval with a margin of only one vote. President Obama is currently preoccupied with getting Congress to approve his agenda. His agenda includes such difficult subjects as the reform of the health and financial systems and accepting targets for the United States concerning carbon emission. Given this policy load he has not been able to turn his attention to the treaties his country has signed with the East Asians. The United States and South Korea, for example, signed a free trade agreement in June 2007 but the Senate has as yet to ratify it. On the other hand, South Korea's parliament ratified a free trade agreement with India on 6 November 2009. Even when the United States took the lead in developing a framework for multi-regional cooperation, it failed to take advantage of its own work. A good example of this is the trade treaty with ASEAN. While the treaty languishes for approval in the Senate, it has been used as a model by other countries and regions that have recognised the importance of working closely with Asia. Earlier this year South Korea signed a free trade deal with the European Union (EU) that, ironically, was modelled on the one worked out with Washington.

Washington will need to turn its attention to trade relations with East Asia for the simple reason that this is now the fastest growing region in the world. It is also the case that the East Asians are reshaping the global trading system. Broadly speaking, there are now three parts to the emerging global structure. The smaller East Asian nations on China's periphery have become major suppliers of parts and components to the Chinese industry. China is now concentrating on using these inputs to manufacture finished products that range from iPods to airplanes. It is no longer dependent on the export of such simple items as toys and garments. The final products it produces find their way into the markets of the United States and Europe. The question then is – how to regulate this three-way trade? The hope that this will be done in the context of a multilateral treaty negotiated under the auspices of the World Trade Organization (WTO) has not been realised. The Doha round of talks that began in 2001 is now stalled. It has turned out that the matters that were to be resolved within the framework of one treaty could not be done because of the complexity of the trade-offs that were involved. Instead, the world is moving towards concluding bilateral treaties between countries, between regional arrangements such as the EU and ASEAN, and between regions and countries such as between South Korea and the EU. The US cannot afford to ignore this development no matter how great its weight is in the global economy and the world trading system. It has a cumbersome treaty-approval system that needs to be improved for it to remain involved in the evolving global trading system. This matter will be taken up in the talks that President Obama will have with the East Asian leaders in particular with those of China.

### **Working with China**

The most important part of the Obama visit to East Asia will be the three-day stay in China. In Beijing, he will spend a significant amount of time with Hu Jintao, his Chinese counterpart. The two have met before including on a one-to-one basis, of which their first meeting was in London in April on the sidelines of the G20 meeting. In August, President Obama hosted a large delegation from Beijing that met with an equally large number of officials from the United States. These consultations clearly signalled to the world that the two countries were prepared to work together to handle global economic issues within a framework that could be labelled the G2.

The Hu-Obama meeting will be held at a time when some strains exist in the relationship between the two countries. These have arisen largely on the account of a variety of disputes

concerning trade. It has not pleased Beijing that Washington, under President Obama, has used the blunt instrument of counter-veiling duties allowed under China's agreement with the WTO to pacify some of the influential lobbies that the new administration wishes to keep on its side. These lobbies are threatened by the increasing competition coming from China. The Chinese leadership was not pleased with the fact that only days before the Obama visit Washington has slapped anti-dumping duties on US\$2.6 billion of Chinese steel pipe imports. The US Department of Commerce imposed tariffs of up to 99 per cent on some Chinese imports while filing a formal complaint as required by international law with the WTO. Last month, the Obama administration levied 35 per cent tariffs on vehicle tires made in China and imported into America. These actions, as usually happens in trade disputes, led to counter-actions by Beijing. It opened investigations into US exports of poultry on the grounds of safety, and car and car parts because of the state aid these industries have received. The reference was to the bailout of General Motors and Chrysler by Washington. There was irony in this since the Chinese government's support of its state-owned companies has long been a bone of contention with its major trading partners. But Beijing did not stop at the adoption of these counter-measures. It issued a stinging rebuke to Washington – "China resolutely opposes such protectionist practices and will take steps to protect the interests of our domestic industries", said the country's commerce ministry. "The US should give objective consideration to the fact that the fundamental problem of the US industries in question is the fall of demand brought about by the financial crisis."<sup>5</sup>

The economies of China and the US have become intertwined in several unexpected ways. Take for instance the setting of interest rates in the US, a responsibility that lies with the Federal Reserve System, the US central bank. The Fed sets short-term interest rates which then influence the long-term rates which, in turn, have an impact on the levels of investment. However, this link has been severed. Since 2001, the Fed has moved short-term rates from 1 per cent to more than 5 per cent and then back to zero. And yet the rate on the 10-year Treasury note has stayed mostly within a relatively narrow range between 3.5 percent and 4.5 per cent. The lack of volatility in the long-term rates was almost entirely because of Chinese purchases of the US Treasury bills. The Chinese now have close to US\$900 billion in investments in the US long-term instruments. It has been suggested that "it's time to form a joint central bank. This won't happen overnight, but in some ways the process has already begun".<sup>6</sup> There are other areas where fresh thinking is required to set the relations between the two countries based on the recognition of reality. One of them is the US concern with international property rights. "Successful American businesses operating in China, however, have learned that trying to protect intellectual property wastes time and energy, and they're better off reinvesting in research and developing new products. Chinese firms excel at copying but not yet creating. As a result, smart firms have recognized that the lasting solution is innovation, not courts and lawyers."<sup>7</sup>

It is in the area of climate change that the two countries need to work together. This subject will figure prominently in the Hu-Obama discussions. Some of the commentary concerning this subject has missed the links that exist between China and the United States in the area of global warming. It is pointed out that China will soon overtake the United States as the largest emitter of carbon into the atmosphere and therefore, has to adopt an aggressive carbon-emission target matching those the United States is working on. A clear path forward

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<sup>5</sup> Quoted in Geoff Dyer, "China attacks US in fresh trade spat", *Financial Times*, 7 November 2009, p. 2.

<sup>6</sup> Zachary Karabell, "For China trip, lose the old baggage", *The Washington Post, Outlook*, 8 November 2009, p. B3.

<sup>7</sup> Ibid.

would “involve regular meetings and annual targets that might be set by some combination of the [US] Environmental Agency and China’s Ministry of Environmental Protection. Given that a significant portion of China’s emissions result from American companies manufacturing goods there, and given that the cost of US energy consumption is shaped by China’s hunger for the resources, the two nations must coordinate policy and action, including emission targets that adjust over time – with China bearing a larger share of the burden as it becomes ever more energy intensive.”<sup>8</sup>

## Conclusion

There is an important conclusion to be drawn from the preceding analysis of the circumstances that will determine the success or failure of the first visit to East Asia by President Barack Obama. Relations between these two parts of the global economy should be based on institutional arrangements rather than on *ad hoc* dialogue between the leaderships of the various countries. This is particularly the case with relations between Beijing and Washington. If institutions were to develop, it will not happen overnight but will evolve over time. There are a number of areas that will need to be tackled within institutional frameworks. These include monetary policy, trade policy and management of climate change.

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<sup>8</sup> Ibid.