

The challenge of Chimerica



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For more than a decade both the United States and China have focused on economic win-wins, managing down their lurking geopolitical rivalries and keeping a lid on potentially incendiary political disagreements and military tensions.

Their presidents, Hu Jintao and Barack Obama, have already signalled their strong intentions to keep on this path. The problem for both, and for the world, is that after the global financial crisis it will become increasingly difficult to do so.

The leaders know their "trade for T-bills" ties were a major contributing factor to the global financial crisis. China was happy to provide a bottomless pit of cheap American credit by buying up dollars and Treasury bills so long as Chinese goods continued to sail off American shelves. The US was willing to live with a massive trade deficit with China and an apparently undervalued Chinese currency so long as the low interest rates made possible by China's hunger for dollars kept the US economy humming.

The historian Niall Ferguson calls this co-dependent arrangement "Chimerica".

Undoing what everyone now agrees is a most unhealthy co-dependence between the world's top two economies will be hard. It will demand nothing less than a recoding of the economic DNA of China and the US.

Americans are born with the consumption gene, and borrow, not earn, their way to the American dream of home and business ownership.

Chinese, on the other hand, have the thrift ethos drummed into them from birth. Their Government has continued to pour money into investment in infrastructure and industry for export to drive growth and raise living standards. But the Chinese Government has not built the kind of social safety net and retail financial system that would lead its citizens to

save less, consume more and build a vibrant and sustainable domestic market-led model of economic develop-

ment. Whether they like it or not, China and the US will be stuck with Chimerica for a long time.

The idea of a G2 has been hotly debated in recent months. In January Zbigniew Brzezinski raised the idea in a Beijing celebration of the 30th anniversary of formal US-China diplomatic ties, in which he had played a leading role.

The British Foreign Secretary, David Miliband, warned his European colleagues that they would have to work hard if they wanted to turn the nascent G2 into a G3 including them. Others say the whole idea is fanciful, given the fundamental differences that divide China and the US.

No senior government official from either the US or China is ever likely to call their relationship G2. But putting together all we know about the economics of the crisis, it is hard to avoid the conclusion that the world is moving towards a de facto G2, almost by default, as the other major economies are being hit even harder by the crisis and with longer-lasting effects.

For close to three decades Australia has successfully pursued twin objectives of building powerful economic links with China while strengthening its security alliance with the US. Like both his Liberal and Labor predecessors, the Prime Minister, Kevin Rudd, wants to continue this essential balancing act.

The challenge for Australia is that the US and China will be different countries and their relationship will be different after the global financial crisis.

How should Australia act in this environment? The 2009 defence white paper makes the case for an upgraded, modernised and expanded Australian defence capability to insure against fallout from military conflict among the major powers of the Asia-Pacific – an unlikely outcome, but one defence planners have to consider with all seriousness and resolve.

Though the white paper talks also of India, Japan and Russia, it is widely viewed that the paper's primary concern is China's nascent rivalry with a slowing weakening but still dominant US.

The focus of the white paper is 2030, knowing that the progress of major military build-ups is measured in decades rather than years.

There is no indication that the US under Obama will scale back its far-reaching global ambitions. Nonetheless, the country will grow ever more cash-strapped and psychologically exhausted from foreign entanglements, with its military stretched close to breaking point,

Obama will give US allies what they said they wanted but did not get under George Bush: more involvement in setting shared strategic objectives. But he will also demand that these allies take on more responsibility in furthering these objectives.

The cost of doing what it takes to stay on America's A-list of trusted allies is likely to grow over the next decade, and Australia may well be better placed and more willing to pay them than some of the US's other traditional alliance partners.

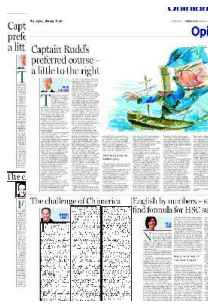
Managing these two bilateral relationships will be even more important to Australia's national interests after the financial crisis than before it. Australia will want to involve itself in US-China relations in ways that help smooth the frictions between the two great powers without getting in the way.

The best diplomatic track for Australia to work collectively with the US and China seems to be in supporting the shooting-star ascent of the G20 from an obscure meeting of finance ministers into what might well become the most important institution of global economic governance in the coming decade.

The G20 agenda will focus on issues of vital importance to Australia: financial regulation, resisting protectionism, furthering free trade, reconciling the climate change agenda with global economic integration.

And, as the challenges facing the US-China relationship grow increasingly complex, Australia is well positioned to help them work through their differences within that forum.

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