

**The American Chamber of Commerce in Hong Kong
Chamber-wide Breakfast**

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U.S. Economic Engagement in Asia

Thank you for your introduction and thank you for inviting me today. It is a great pleasure for me to speak to the members of the American Chamber of Commerce in Hong Kong, which represents some of the most influential U.S. businesses and investors in Asia.

I have come to Asia for the third time this year to help further economic ties between this region and the United States, and in particular to participate in a noteworthy IPR and telecom conference for our officers in U.S. Embassies in Asia and South Asia. I also have had the pleasure to meet with business and governmental leaders and will do the same in Guangzhou later this week.

Today I would like to focus on U.S. global economic engagement strategy, with a particular emphasis on U.S.-China and U.S.-Hong Kong relations. The U.S.-China relationship is not only important to the U.S. and to China, but to the entire region and the world. The world economy grew by almost 5% over the past year, its fastest pace in two decades. The twin engines of America and China together accounted for almost half of that global growth. This is evidence that if we manage our relationship well, the world as a whole benefits.

Before I get into this broad theme, let me just say a few words about the conference. As part of a worldwide effort, the State Department's Bureau of Economic and Business Affairs, working with the U.S. Consulate General in Hong Kong, organized a conference on the vital issues of intellectual property and telecommunications. Over 40 State Department officers stationed in Asia-Pacific and South Asia attended the two-day conference. It featured speakers from industry and the U.S. and Hong Kong governments; and covered topics such as digital piracy and Internet development and its impact on foreign policy. We had a panel just focusing on China and its regional impact in both the intellectual property and telecom arenas. As you know, the Pearl River Delta and the rest of China face massive piracy and counterfeiting problems.

Although Chinese government officials have started to crack down on this problem, it is a long, slow, uphill battle. We encourage them to take a page from Hong Kong's experience of the past several years, during which Hong Kong made the transition to being a model of effective enforcement against optical disc pirates and counterfeiters. At the same time, Asia sets the global pace in the development and adoption of exciting new communications technologies, including wireless broadband and Internet telephony. I am very encouraged by the enthusiasm of our officers to tackle these problems, and I

hope the business community will continue to work vigorously with us in this critical area.

The four pillars of America's economic policy

Our country faces major foreign policy challenges: war, proliferation of weapons of mass destruction, terrorism, and how to respond to genocide and famine; yet economic issues and policies are always close to the top of the agenda of diplomats and government leaders. As Secretary of State Colin Powell has commented, "Visiting leaders and foreign ministers sometimes want to talk about security, sometimes they want to talk about some diplomatic problem; but all the time they want to talk about trade... about debt relief... about investment."

I want to address the international economic policy goals of the United States, goals that reflect our core national interests and remain stable over time. I will try to frame my remarks concerning those national interests in the context of our relations with China and Hong Kong. There are four pillars -- broad economic policy priorities -- that support and bolster the economic aspects of U.S. foreign policy:

- First, we try to assure our economic security;
- Second, we promote global growth to help ensure economic health at home and abroad;
- Third, we promote sustainable development. We do our best to ensure that poor nations participate fully in the rising tide of prosperity;
- Fourth, we advance global prosperity by expanding international trade and investment.

In applying these four pillars to our relationship with China, we have come to understand that we must vigilantly manage this vitally important bilateral relationship, which means staying engaged in all areas – political and economic, bilateral and multilateral – so that problems in one area do not block progress in another. And let me assure you that we are fully engaged in managing that relationship. The United States is a vibrant democracy with a tradition of open debate, and occasionally that debate touches upon our relationship with China, often the economic element. But the fundamental U.S. policy interest lies in responsible conduct of U.S.-China relations, and those interests will not change in the coming years. Dialogue with China involving our most senior leadership has been nearly continuous in the past years and has yielded gains for both sides. This pattern will continue in the years ahead.

Economic security

We pursue economic security by marshalling and coordinating resources across the U.S. government. Our goal is to make the U.S. and world economies more resilient in the face of economic shocks and – especially these days – safer from the risks of terrorism. We have four main tasks: First, cutting off financing for terrorists; second, bolstering the stability of key allies; third, developing and maintaining diversified and reliable supplies of energy; and fourth, facilitating safe and secure international transportation of people and goods.

Economic diplomacy is key in the fight to prevent terrorists from obtaining money and resources. International cooperation is an indispensable weapon in this battle, and the President and the Secretary of State have made it a front-burner issue for U.S. diplomacy worldwide. American diplomats play a leading role in developing and sustaining a global coalition to identify and disrupt terrorist financing networks in every region of the world using a variety of tools and collaborating internationally through the Paris-based Financial Action Task Force (FATF). Since September 11, 2001, we have ordered the freezing of the U.S. assets of almost 400 individuals and entities linked to terrorism and frozen approximately USD 142 million in assets located around the globe, including in the United States.

Hong Kong has been a crucial ally in this effort. In particular, Hong Kong has been a strong partner in the multinational FATF. Initially as president of FATF in 2001, Hong Kong guided the organization to adopt stringent anti-terrorism measures in the wake of September 11. Hong Kong was instrumental in the organization's adoption of eight Special Recommendations that all members should implement in the fight against terrorism and terrorism financing. Hong Kong was also active in building global awareness of and support for FATF's work among non-members. We continue to work closely with Hong Kong, as a regional financial center, on these important issues of terrorist financing; we also want to strengthen our cooperation with Chinese officials in this key area.

To help countries threatened by both terrorism and economic and financial instability, we work actively with other governments, the international financial institutions and the private sector to prevent financial crises and to more effectively resolve debt and foreign exchange crises when they occur. The United States is providing direct assistance to countries around the world that have joined us in the war on terrorism, including Turkey, Jordan, Afghanistan, Pakistan, Indonesia and the Philippines. The State Department is pleased to play a key role in fulfilling the President's commitments to assist reconstruction in Iraq. Along with our colleagues at the Treasury Department, we are working with Iraq's other creditors to craft a solution this year to reduce Iraq's external debt to a level that ensures sustainability, and we are confident that the so-called "Paris Club" of creditors will produce such an outcome this year. We have spoken with the Chinese on the issue of reducing Iraq's debt on a number of occasions and are encouraged by their assurances of willingness to join others to forgive official debt, and we would like to see China's state-owned companies do the same. Bilaterally, China pledged USD 25 million in development assistance at the Madrid Iraq Reconstruction Conference but has not disbursed those funds yet – China's willingness to cooperate is laudable, but follow-through on this vital issue is essential. We also have worked to lift UN sanctions on Iraq, rebuild its oil industry and transfer frozen Iraqi assets back to the people of Iraq.

Reliable energy supplies remain a vital economic interest for the United States and for our friends and allies. World economic growth and prosperity will require new sources of oil and gas, as well as the more efficient use of other traditional sources of energy, like coal, with less impact on the environment. We will have to make greater use of nuclear and renewable sources of energy to the fullest extent possible and increase our efforts to develop new energy technologies, such as hydrogen, where China is playing an important role in the International Partnership for the Hydrogen Economy.

Rising oil prices are the result of strong growth in the global economy and oil demand; concerns over supply stability from major suppliers; and a very slim margin of spare capacity. We have fine-tuned our approaches to cushioning the world economy from sudden disruptions in the oil market with our partners in the International Energy Agency, and the U.S. increased our own insurance policy against a severe supply disruption by filling the Strategic Petroleum Reserve to 670 million barrels, on its way to reaching full capacity of 700 million barrels next year. China has already begun building its own strategic oil reserve, and we continue a dialogue on this important issue. During the last week of October, Chinese officials participated, for the first time, in an IEA oil supply disruption response simulation to foster coordination. Among our wide range of cooperation activities with China on the energy front, we discuss energy security issues with the National Development and Reform Commission (NDRC) as part of a broader State Department-NDRC dialogue on economic issues.

The United States is a world leader in transportation security. We have worked successfully with foreign governments and international organizations to ensure the safety of passengers and cargo. For example, the United States took the lead, with support from the G-8 group and APEC (Asia Pacific Economic Cooperation) members, to adopt transportation security initiatives that are models for successful international economic cooperation. To protect our ports and seaways, we have expanded the Container Security Initiative (CSI), launched in February 2002. The CSI, which we have implemented with our partners at 32 foreign ports handling U.S.-bound cargo, uses automated information, advanced detection technology and highly-trained inspectors to pre-screen and target high-risk containers for inspection before they reach U.S. ports. All containers – 100% -- identified as posing a terrorist risk are inspected using X-ray scans and radiation detection equipment. Hong Kong, which has been an operational CSI port since March 2003, in fact serves as a model of how we would like to see other CSI operations work. The port of Shanghai in China will be operational soon. The U.S. Coast Guard had a successful recent visit to Hong Kong to share best practices under the International Ship and Port Facility Security Code.

Global growth

Our second pillar, growth, is essential for the health of the global economy. Clearly, the U.S. economy remains an engine for growth, and rapidly China is joining us as a major locomotive for worldwide growth. We hope recoveries in Europe and Japan will soon augment global growth prospects. The IMF forecasts world growth of 5% in 2004, slowing to 4.3% in 2005. The countries most able to benefit from this growth will be those that pursue open, transparent trade, as well as monetary and investment policies that seek to reduce structural impediments to growth. Experience shows that protectionism is a "lose-lose" proposition that hurts producers and consumers, and the U.S., the largest economy in the world and its largest global trader, is eager to see China continue to make real strides in integrating itself into the global economy.

We have been encouraging China, our third largest trade partner, to press ahead with its ambitious program of economic reform. This audience does not need to hear from me that China's WTO commitments are producing sweeping changes in its economy, and our central economic engagement strategy is to encourage China to adopt

its WTO commitments fully and on time. This strategy is producing real results and increased market access for U.S. goods and services -- while trade numbers do not tell the whole story, U.S. exports to China have increased dramatically since China joined the WTO. They are nearly 90 percent higher than they were in 2001, making China one of the fastest growing major export markets in recent U.S. history. U.S. financial and insurance companies have been able to move into new areas as a result of WTO openings and we also hope to see smooth implementation of China's commitments in distribution rights, coming before the end of this year. China could benefit from a wave of exports of U.S. equipment and expertise into China's growing logistics and distribution sectors. As you know, however, problems remain, most significantly regarding the extraordinarily high piracy and counterfeiting rates in China. We are devoting extensive resources and political energy to obtaining improvements in China's protection of intellectual property, and indeed in April, as part of the Joint Commission on Commerce and Trade, Vice Premier Wu Yi committed to a detailed action plan on IPR. We are working to ensure that China follows through on these and its WTO commitments, but this is not an easy road.

Another key U.S. goal is to help move towards a flexible, market-based exchange rate in a reasonable timeframe, a goal recently publicly reaffirmed by Premier Wen Jiabao. Both the IMF and the U.S. believe this reform would help sustain China's impressive growth record and promote China's full integration into the global financial and trading system. It is an important step for China as the country emerges as a major economic power. China would enjoy sizable benefits from a more free-floating arrangement. If the yuan should strengthen, the stronger currency would reduce the costs of imports for Chinese consumers and manufacturers. This could be important, especially now in a time of very high oil costs. In addition, a more market-based system for valuing the currency would permit Chinese authorities to exercise a greater range of options in using monetary policy to secure the country's prosperity, while providing a means of adjustment when a change in the value of the currency is required by economic events. Chinese authorities agree that a more flexible arrangement is the preferable option for China. The issue is, when will the country take the next step? We noted with interest the recent move by China's central bank to boost interest rates 25 basis points.

Development

The third of our four pillars is development. Expanding the circle of prosperity is critical to our own national security and well being. Poverty, weak institutions, and corruption can turn nations of great potential into breeding grounds for terrorists. The United States provides more assistance to developing countries than any other country in the world, and we are firmly committed to partnership with developing countries to increase opportunities for all of us. We are proud to have made real this year President Bush's groundbreaking Millennium Challenge Account (MCA) initiative that supports poverty reduction by focusing our assistance efforts on those countries committed to governing justly, investing in people and encouraging economic freedom. MCA funding is in addition to our official developmental assistance. When the program is fully funded in 2006 at USD 5 billion, it will represent a 50% increase over 2003 development assistance figures. 16 countries have been selected as eligible to apply for MCA assistance.

Nonetheless, we recognize that private-sector resources play the most important role in encouraging prosperity in countries around the world, dwarfing more traditional forms of developmental assistance. We have noted Chinese firms have been active and increasingly significant investors around the world, especially in Africa, creating new jobs and export opportunities. In 2003, trade between China and Africa hit a new record high of USD 18.6 billion, an increase of nearly 50% over the previous year. Estimates for 2004 suggest a further increase of perhaps 50% over 2003. Chinese investment in Africa is about USD 1.5 billion and growing.

Trade and investment

Our fourth pillar is building a strong and dynamic international economic system based on free trade and investment -- the fastest and surest way to move from poverty to prosperity. The President said, "Open trade fuels the engines of economic growth that create new jobs and new income. It applies the power of markets to the needs of the poor. It spurs the process of economic and legal reform. It helps dismantle protectionist bureaucracies that stifle incentive and invite corruption. And open trade reinforces the habits of liberty that sustain democracy over the long term."

Trade is now woven into the fabric of the U.S. economy as never before. Total trade is now equivalent to more than a quarter of U.S. output, up from 10% in 1970 -- the largest such increase of any developed economy over this period. Trade has also been a vital component of U.S. job creation: for every job in the U.S. threatened by imports, there are growing numbers of highly-paid, high-skill jobs created by exports. Exports supported seven million American workers a decade ago; that number is now 20 million. In 2003 alone, U.S. exports to China rose by almost 30%. Over the next decade, the U.S. is projected to create an average of three million new services jobs a year, compared to roughly 200,000 jobs that will go overseas.

Hong Kong knows this story well. As manufacturing employment moved across the border to China in the 1980s and 1990s, Hong Kong's services-sector jobs expanded rapidly. Hong Kong's economy is now over 87% service-based. In addition, Hong Kong firms in the Pearl River Delta have expanded operations to provide employment not only to the supporting services-sector workers in Hong Kong, but also to over 10 million workers in China.

Trade negotiations

Strengthening the world trading system is key to America's broader objectives. Fighting terrorism, reducing poverty, improving prosperity -- all of these issues are linked to expanding world trade and the prosperity for people it brings. The last two major trade negotiations -- NAFTA and the Uruguay Round -- benefited the average American family of four by up to \$2,000 each year through lower tariffs and higher incomes; and also brought commensurate gains for our trade partners globally.

In the WTO, the United States has stepped forward with bold and sweeping market-opening proposals to liberalize trade in both agricultural and non-agricultural goods. We are also pressing forward on liberalization of financial services, aviation, telecommunications, agricultural biotechnology and government procurement. The

President is committed to wrapping up successfully the World Trade Organization's Doha agenda, and the United States has taken the lead in re-energizing these negotiations. This effort received an encouraging boost at the end of July when parties in Geneva reached agreement on a framework for further negotiations on removing barriers to trade -- especially agricultural, goods and services trade -- with special consideration given to the needs of developing countries. Hong Kong deserves special praise for its leadership role in fostering consensus on key issues and for hosting the ministerial meeting in 2005. China, although a member of the "G-20" group last year that contributed to the foundering of the Cancun talks, has been helpful in encouraging other developing countries to think about how to compromise on thorny issues.

Along with our WTO efforts, we are pursuing a dual track towards trade liberalization through an aggressive approach to negotiating bilateral free trade agreements, or FTAs. We have concluded trade agreements with Morocco, Bahrain, Singapore Australia, and the Central American countries and Dominican Republic that set new high standards for protection of intellectual property rights, open markets for services, ensure government transparency, and provide effective labor and environmental enforcement, as well as mutual access for services, government procurement, e-commerce and investment. We are also negotiating FTAs with Thailand, Panama, the South African Customs Union and the Andean group of Colombia, Peru and Ecuador.

We have followed with great interest the progression of FTAs among Asian countries, such as China's FTA negotiations with Australia, New Zealand, Thailand and ASEAN, along with South Korea's new link with Chile. These efforts to pursue trade liberalization are in general a positive and welcome development and compliment the policy of "competitive liberalization" that the United States has been pursuing for the past four years. The CEPA (Closer Economic Partnership Arrangement) between Hong Kong and China is also something we pay close attention to as U.S. and other firms take advantage of liberal regulations to expand upon Hong Kong's traditional role as a gateway to investment in the mainland. CEPA is an example of how FTAs can, as we wait for more thorough liberalization under the Doha round, provide broad gains for everyone.

Investment

Openness to private investment is also key to building a modern economy. Investment into China continues to grow, despite the decline in global foreign direct investment (FDI) felt virtually everywhere else since 2000. China was the number one destination in the world for FDI inflow in 2003, at USD 53 billion. Foreign-invested companies now produce 55% of China's exports, but China's domestic market is increasingly a target for foreign enterprises. A majority of American-invested firms are in China to serve local clients and develop positions in the growing domestic market. Experts expect to see this domestic-focused investment grow as China opens its internal distribution sector in December, as it committed to do when joining the WTO.

That does not mean China's investment climate is ideal. According to a recent member survey by the American Chamber of Commerce, most firms place high priority on their investment programs in China. Nonetheless, China's regulatory environment is

regarded as one of the top challenges to doing business there. China has made great progress on its WTO commitments, but there is still significant work to be done to:

- Make the regulatory process more transparent;
- Improve IPR protection, especially applying criminal penalties to IPR offenders;
- Base technical standards on internationally-accepted technical standards.

We have discussed these issues candidly with Chinese policy makers, and they understand the importance of continuing to attract high-quality direct investment. We look forward to continued reform to improve China's investment climate.

Labor rights

Finally, free trade is not only about business. A world that trades freely will grow in prosperity, in security and in freedom. With China's integration in the global trading system comes new international scrutiny of the conditions of China's workers, and we are pleased that China has publicly committed to reforms intended to improve working conditions, fight poverty and unemployment, and improve workers' legal protections. U.S. industry and government should strive to positively influence these efforts, and I am pleased to recognize that AmCham Hong Kong has been a leader in the area of corporate social responsibility. Your pioneering development of a CSR code of conduct has been used as a model by other AmChams in the region and is one of the cornerstones of the U.S. government's overall labor rights strategy with China.

Annually since 1998, the State Department has been pleased to present the Award for Corporate Excellence (ACE) to those companies who employ exemplary business practices and demonstrate the deep commitment to community that reflects the American spirit. American companies demonstrate that spirit around the world each and every day; American investors overseas are America's corporate ambassadors.

A key ACE criterion regarding exemplary employment practices includes "observance and promotion of the ILO-recognized fundamental worker rights, including the right to organize and to engage in collective bargaining, non-discrimination in employment and occupation, and the absence of child labor and forced or compulsory labor." This is a cornerstone to our labor rights strategy worldwide, and certainly in China. We are working with U.S. corporations invested there to adopt codes of social responsibility that reflect this principle and have a full agenda with the government of China on labor rights issues.

Conclusion

We face the challenge of building a more stable, prosperous, and safer world. We do so in the face of unprecedented opportunities, as well as serious threats. We who execute our economic policy do so mindful that the economic landscape will have an enormous long-term effect on global security and prosperity.

Thank you again for inviting me today. I'm pleased to take a few minutes to answer your questions.

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