

**The National Bureau of Asian Research**

**Mr. Robert D. Hormats**

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**Ms. Meredith Miller:** Thank you very much.

We are thrilled to have had two senior administration officials on this year's Engaging Asia program to speak to the critical and intertwined dimensions of economic and security policy in Asia.

And we're very fortunate that Robert Hormats, Undersecretary for Economic, Energy, and Agricultural Affairs at the Department of State has joined us to complete the picture with his insights into the future of US leadership in Asia on the economic and trade policy fronts.

Secretary Hormats' career has spanned the academic, policy, and corporate arenas. As a public servant, he served at the State Department, at USTR, and at the National Security Council. He had an accomplished career in the private sector, and left his position as Vice Chairman of Goldman Sachs International to reenter public service in 2009 in his current position at the State Department.

From the early days of his career, Secretary Hormats has worked to integrate China into the international community. He played an important role in the Nixon administration in opening diplomatic relations with China. And, in his current position, he participates in the strategic and economic

dialog with China, and has also led efforts to engage more closely with Asia's other rising power, India, on a wide array of economic issues.

More broadly, he's led active US government efforts on a wide range of issues critical to maintaining our economic strength, including indigenous innovation issues, intellectual property rights, and the US chairmanship of APEC next year, to name only a few.

His accomplishments as an author and in the academic arena are no less impressive. And I commend to you his full biography, which is in the program.

And without further ado, I will turn the floor over to Secretary Hormats. Thank you again for joining us, sir. It's a real pleasure to have you here.

**Mr. Robert Hormats:** First of all, thank you very much, Meredith, for your very kind introduction. It's a pleasure to be here, also to follow Michèle Flournoy, who is a colleague of mine and a very thoughtful person about many of these issues.

I'm also a big fan of NBR, so I was particularly happy to come and participate because I know the quality of work NBR does and the quality of people it brings together. And of course, also the issue of our economic relationship with Asia is extremely important, and I will go into several dimensions of that in a few moments.

I understand this morning there was also a panel discussion about ways we can avoid the pitfalls that affect our bilateral relationship with Asia. So, what I'd like to do is talk about the opportunities for economic growth that result from developing further our relations with Asia and strengthening our ties in the broader Pacific Rim.

There are a lot of dimensions to this, as Meredith has indicated. And putting them together in some strategic context is one of the things we try to do in the State Department. I'll talk a little about the various dimensions, but also, importantly, how they fit together.

It's interesting to note when you go back in history, and I do--as Meredith's pointed out, I've written a fair amount about history going back to the various aspects of American international economic policy, including a book on how we paid for our wars. So, I've tried to look at the context of our international economic relations both in the current set of circumstances and from a historical point of view.

And one of the interesting quotes that I find fascinating and very prescient is if you go back to 1900, over a hundred years ago, the Secretary of State at the time, John Hay, declared the following. "The Mediterranean is the ocean of the past, the Atlantic is the ocean of the present, and the Pacific is the ocean of the future."

Well, how right that was. And I think it's useful to realize that there were people in those days that had a sense of vision about where things

were going and about where our strategic interests were at the time and would be in the future.

A hundred years later, his vision is shared by the current Secretary of State, Secretary Clinton, who is focusing a great deal of time on developing opportunities for trade and for economic relations and for broader sets of relations in the Pacific Basin.

Secretary Clinton said it very well last July when she was in Thailand. She said, "The United States is back in Asia." The message was heard loud and clear, and she led the US delegation to the ASEAN Post-Ministerial Conference and the ASEAN Regional Forum in Phuket.

Let me make sure I focus on a few of these issues that are particularly important to us. The State Department, when we look at these issues, we recognize the importance of Asia both in strategic terms and in terms of our country's own economic future. And I think that in our own national interest, we have to demonstrate that the United States is active, is engaged, and is playing a constructive partnership role in the region.

And the reason for this should be no surprise to Americans today. The Asia Pacific region is clearly the most economically dynamic in the world today. The members of APEC account for 54 percent of world GDP, 44 percent of global trade, 40 percent of the world's population, something in the order of 2.7 billion consumers.

But, I think it's more than that. And when you look at it, and if you look at it from an historical point of view, when historians look back a hundred years from now over the fundamental events of our time, they'll focus, certainly, when they look at the last century or century and a half, they'll focus on World War I, the post-World War I period of Depression, World War II, the Cold War, a whole range of things like that.

But, one of the things that I think is going to stand out when they look at this period is the rise of the large emerging economies, the fact that a group of countries that were considered for decades and decades, really centuries, as poor developing countries are now anything but that. They are the rising powers in the global system.

China is one in particular as well as India, and I've just returned from a trip to China and India. Brazil is playing a very substantial role, South Korea, many of these countries, so that you're taking a whole group of countries that were really on the periphery of the global system, and now they have become critical players in the global system.

And there are two elements of this picture that are worth looking at. One of them is the move from the G8, or G7 depending on how you look at it, to the role of the G20. It's quite clear that in no major policy area of the world is it possible to resolve problems today in a serious and meaningful way without engaging the large emerging economies.

And the G20 is the most vivid institutional example of that. But, there's another example, and that is, again, if you look in the sweep of history, throughout the sweep of history, capital has flowed, more or less, in one direction, from the industrialized to the developing countries.

What's changed? What's changed is obvious, and that is that now we have a large number of emerging economies who are major suppliers of capital to the industrialized economies, the United States being a particularly important example of that where we're getting money from China, which is a big supplier of capital to the United States, but also from a number of countries in the Middle East and many other emerging economies as well with large financial surpluses.

So, not only are these countries playing a powerful role in trade, they're playing a very powerful role in international finance. Beyond that, they're playing a very powerful role in the development of new technologies.

I spent some time in China, as I mentioned. I go there virtually two or three times a year. I started going in the early '70s when I was working as Henry Kissinger's economic advisor as a very young staff member on the NSC.

And the change in China, it's not just been that they're growing more rapidly and they have these spectacular new buildings and great infrastructure. They're very innovative. They're coming up with their own ideas.

Among countries in terms of patents, they're number three or number four. They're playing a very active innovative role. India is booming. The technology sector of India is booming. So, these countries are powerful players really across the board.

And I think in the way we look at the sweep of history, that big change, that sweeping change, is something historians are going to remark on a hundred years from now, two hundred years from now when they write about this period.

And I think that, if you look at it in a shorter term context, one of the things that's very important is that the rebound of growth in Asia has been vital to the global recovery. And that's just another example of the role they play. It used to be the industrialized countries, particularly during the Asian financial crisis of 1997/'98, it was the industrialized countries that led the world out of the downturn.

Now that's not the case. The industrialized countries have very weak economic growth, by and large. It's the Asian countries in particular that are leading the world out of this downturn, not that we can totally rely on them, because we have to do what we need to do at home.

But, they're certainly very helpful as drivers of economic growth. They're not going to resolve all of our problems for us. But, they can certainly help to boost growth and boost economic activity here.

The Asian Development Bank, for instance, predicts that East Asian emerging economies will grow at 8 percent this year. In addition, the IMF forecasts that the region's economies will grow faster than the world average through at least 2014. Those are powerful numbers.

The United States also can't afford to sit on the sidelines while this is all going on. And that's why we've been working to strengthen our engagement with the economies of the region. And our strategy for cooperation is premised on a framework that is based on four major and very simple elements.

One is openness, allowing for participation from emerging economies and for other countries in a more open international economic system as opposed to one characterized by trade barriers of various sorts.

Related to that is that we want to make sure that trade is freer and freer over a period of time, and that investment is as well. And I'll talk a little about both of these, but I think the key point is we know there is not free trade in the perfect pristine sense. We know that governments do play an active role in the trading system. But, the goal is, over a period of time with respect to trade and with respect to investment, to reduce those barriers to the extent possible, and to do so within a rules based trading system.

And I think this is very important. It's important to underscore. If you look back to the period of the 1920s and early 1930s, what did you



have? You had a free for all. You had no international rules on trade to speak of, no international rules on monetary policy or finance. It was beggar thy neighbor.

What's been very interesting about the system that we have today is that we've gone through the worst financial crisis since the Great Depression and there has been a minimal amount of protectionism in trade or investment. This is not to say it's been perfect. There has certainly been some, but compared to that earlier period, there has been very little.

And that's because you have a system that has been, over a period of time, moving toward a great degree of trade freedom, a greater degree of freedom in investment, and, more importantly or just as importantly, very strong rules to which countries adhere, for the most part. And they adhere because it's in their common interest to do so, not to violate them because, if one country violates them, that can rebound to its disadvantage.

The third key element is transparency, including easy and relatively clear rules for doing business. So, it's not just that the rules are there, it's that we want to make sure that countries and the system itself is transparent enough so that you can look at country after country and determine, "Are they adhering to the rules?"

And one element of this was in the G20 where the World Bank and the IMF and the WTO were asked to monitor the performance of countries in the way they adhere to their commitment not to impose new trade restrictions.

And the last point is one that's sort of a broad rubric, but it's very important when you think about it. And that is it's very important for us to be able to demonstrate to the American people that the rules of the trading system are fair, that there's a level playing field.

And I can't emphasize this enough. There is a great degree of skepticism among Americans today about whether the trading system is stacked against them. People look at free trade agreements that we've signed. They say, you know, "Are they in America's interest? Have they been disadvantageous? Is the system working against the United States?"

The only way we can generate support in this country for international trade agreements is to demonstrate that the system is fair and balanced, and that the rules are being adhered to by everyone, particularly the large emerging economies that are so important to the system. Are they playing by the rules? Are they developing rules of their own? This is going to be a critical element here.

And at a time when tariffs have gone down significantly throughout the region, it's important to take on a number of other tasks to demonstrate that the system is working well. And that means in particular promoting regulatory cooperation and taking various steps at the border to facilitate trade.

So, it's not so much trade barriers that are impeding trade today. In many cases, it's things that happen within systems. It's regulatory changes.

It's thing like, in the case of China, policies that are designed to help support indigenous innovation by Chinese companies to the disadvantage of foreign companies. It's a whole variety of things within borders, or sometimes called beyond borders, it means internally beyond borders that do things that impede trade rather than the more traditional barriers that are imposed at the border.

So, as we move to the next generation of discussions, obviously we want to lower borders, the barriers at the border, but we also need to look internally at what's happening in these countries.

And we also recognize that, as a result of the financial crisis, we really can't go back to growth as usual. And so, we're committed to working within the region to forge a 21st century economic agenda that seeks to attain a higher quality of economic growth, not just higher rates of growth, but ways of achieving growth that is more inclusive than in the past.

And this is not simply an American idea. If you look at China and you look at most countries, their goal is not just to achieve a higher rate of growth but to make sure more and more people benefit from that growth, because that's important to social stability. It's also important to their ability to sustain their growth from a political point of view. And the more people they engage in the system, the better it's going to be in terms of their own ability to compete in the global economy.

What I'd like to do now is just touch very briefly on a few of the tools that we're using to accomplish our goals, one of which, I've touched on this, is free trade agreements. The one that is most in the news these days is KORUS, the US Korean Free Trade Agreement, and then also the Transpacific Partnership, the TPP, both of which are now very important elements of American policy. I'll touch a little bit more on those.

The second are regional multilateral organizations, particularly APEC, whose meetings the United States will be hosting in 2011 as well as our partnership with regional groupings like ASEAN. And the third is our robust bilateral relationship, including historic ties with old friends as well as new bonds of cooperation with these emerging economies.

So, let me take just a moment to discuss the roles that each of these can play in strengthening our economic ties in the region.

First are the free trade agreements. The best place to start is with these, because I think we can--when we look at what's going on in the region, many, many countries are very actively pursuing free trade agreements.

If you look at Korea, for instance, the EU has been pursuing free trade agreements with South Korea, and they're right on the edge of finishing up theirs. In the whole region, you're seeing a burst of free trade agreements. And let me just cite the numbers, because I think they're a wakeup call for us.

In the year 2000, just 10 years ago, there were only three FTAs in East Asia. Ten years later, we've seen 45 FTAs in effect among or between APEC economies, and another 84 in various stages of preparation or development.

Now, what does this tell us? This tells us that these agreements, if we do not get more actively involved by doing things like the Korea FTA and TPP and others, we're going to gradually see our market share sliced down further and further as these free trade agreements give other countries preferential access to one another's markets.

And this is happening at a very rapid rate. And it's a wakeup call for us to understand that we need to be more actively engaged. And the Korea agreement--and the KORUS and the TPP are two ways of addressing this.

And we also have to, and I think this is another point that we need to understand, and that is these are elements that are important from a strategic point of view because they demonstrate our engagement in the region. But, they're also important from a domestic jobs point of view because, if you look at what the President said yesterday about a large portion of the world's growth being outside the world's borders, particularly in the emerging economies, one of the ways the United States is able to participate in that growth is to participate in these types of free trade agreements which give our companies a greater degree of presence and greater market benefits in these economies.

And I think this is something that's important to explain to Americans, that trade policy is about job creation in a very substantial way, and that if you do not have trade agreements with some of these large emerging economies, it puts us at a disadvantage from the point of view of exports and it puts us at a disadvantage from the point of view of creating domestic jobs.

It's just a matter of arithmetic. If the growth is in these countries, then we need greater market access to these countries. And the administration is working hard, particularly in the current moment, on the KORUS Agreement.

The USGR, as you doubtless know, has been instructed by President Obama to work with the Koreans to resolve any outstanding issues related to KORUS and is now engaged in extensive consultations with the Congress and with other stakeholders.

This is going to be very important, and the President intends to submit KORUS to Congress for approval in the months following his November meeting with President Lee. The timing, of course, we have to decide depending on how things work out in terms of details. But, certainly the goal is to move ahead on this as promptly as is possible.

We look at this as a win-win situation. For the United States, it will contribute significantly to the administration's export goals, particularly the

National Export Initiative to double American exports over five years and support two million jobs, which is the President's objective.

And the reduction of barriers in Korea, tariffs and tariff rate quotas on goods alone, would add around \$10 billion to annual merchandise exports to Korea.

We're also working to address issues related to agreements with the other two Pacific Rim countries, Columbia and Panama, in order to present them for Congressional consideration at an appropriate time.

We're also making progress in negotiating the Transpacific Partnership Agreement. The talks currently include the United States, Australia, Brunei, Chile, New Zealand, Peru, Singapore, and Vietnam. And other countries are interested in participating as well.

The goal is to grow the TPP into a high standard, broad-based, regional trade agreement, one that can go a long way toward addressing these behind the border issues that I mentioned a moment ago, and improving trade facilitation, supply chain connectivity, a whole range of elements that will enhance opportunity for our companies around the world.

It would also create more opportunities for small and medium sized companies, which is very important because these are big job creators here. It would prioritize labor and environmental protections. It would foster development and would promote new technologies in emerging economic

sectors. So, this is a very important element of our future trade relations with the region.

The second round of TPP negotiations was held in San Francisco in June. It yielded significant progress across a range of issues that are hopefully going to be covered in the agreement.

A lot of work remains to be done. There are teams working as we speak on a third round of negotiations that will take place in Brunei in October. Successful efforts on both bilateral FTAs like KORUS and the TPP will create new and meaningful market access for US exports and also help to ensure that our businesses remain competitive in the Asia-Pacific region.

The second area is the regional multilateral discussions focused largely on APEC, which I mentioned a moment ago. We know that regional economic integration is about more than just FTAs, although the FTAs are clearly very important and an important priority.

It's about developing multilateral economic institutions that could play a critical role in addressing economic challenges and removing barriers to trade and investment. Groups like APEC and ASEAN provide collaboration forums for dealing with these types of economic issues.

Let me focus for a moment on APEC, because it is one that we're working very actively on. And I should say also that we're trying to bring back and we will be bringing back a number of APEC ambassadors, American



ambassadors to APEC countries, to have a trip around the United States. That will begin early next year.

But, we're trying to help Americans to understand the benefits of APEC. And those who are not able to go, we're going to have our ambassadors come back and do sort of what's known in the banking world as reverse road shows to discuss these in various cities.

The United States sees APEC as a key forum for regional economic cooperation. APEC initiatives help to create an environment that fosters high quality growth, addresses trade and investment barriers, and ensures norms and standards for a level playing field of the type I mentioned.

We've already witnessed the impact that APEC has had at a global level. It played a key role in realizing that WTO Information Technology Agreement. It has also been front and center in addressing pressing economic challenges such as standards and conformance issues, regulatory cooperation, trade facilitation, small business development, and digital trade.

The preparatory work for APEC has done a lot in these areas to help to define the region as a high standard, broad-based platform for companies to operate with one another by going well beyond what is done in the WTO to these behind the border issues that I mentioned. And all of them, I think when you add them all up, have been quite beneficial.

And that's why there is very strong support among the American business community for APEC. And there is a large business constituency headed by a senior official of Microsoft to make sure that the business community works very closely with APEC and vice versa.

A great example of how APEC informs and influences regional trade initiatives is the TPP that I mentioned. The TPP is one of the most promising models for APEC's long-term vision of a free trade area of the Asia-Pacific region. Now, this is not something that's going to happen right away, but it's certainly a vision that a lot of people have had relating to APEC for a period of time.

We're also working within APEC to set a 21st century agenda for the region that focuses on attaining higher quality economic growth of the type I mentioned. To this end, APEC is working to define a regional approach to growth that is balanced, inclusive, and environmentally sustainable.

And the goal here is balance, which means pursuing macroeconomic policies and structural reforms that will gradually unwind distortions and raise potential outputs. And the inclusive element means, as I touched on earlier, helping all members of society gain better access to economic opportunity.

This is a very important issue for virtually all the countries in the region, to avoid lopsided growth where elites or small groups of people benefit and large numbers of people feel left behind. That's a formula for

social unrest and it also means that people don't get a chance to participate in the productive benefits of economic growth.

And by helping to facilitate the transition to green economies, which is a major focus of APEC, the goal is going to be to foster policies that are focused on low carbon emissions, improving market access for environmental goods and service, and promoting energy efficiency across entire economies. And environmental sustainability is really a key element of a lot of the discussions that go on in APEC.

These contributions to regional economic growth and cooperation underscore why the United States values APEC so highly and why we've agreed to host the APEC meeting in Honolulu in 2011.

ASEAN is also a key element of our engagement in the region. And we're ramping up our engagement with ASEAN through the ASEAN US Enhanced Partnership. We're building US-ASEAN trade and investment ties and promoting trade facilitation. We have dialogues on such issues as trade facilitation, customs standards, and public-private cooperation.

This year, we also established for the first time a US mission to the ASEAN organization. And the mission will actively work with the ASEAN economic community, whose primary goal is to achieve a single market and production base across all ASEAN member states by the year 2015. So, we wanted to have a demonstrated presence in the region so that we could work with the countries of the region.

And finally, the broad area of bilateral dialogues and partnerships. We're developing our bilateral partnerships to underpin the entire integration process. Let me just touch on a few countries.

Japan continues to be one of our most important trading partners with whom we work on a broad range of important issues. As APEC hosts in the year 2010 and 2011, Japan and the United States have been working closely together to coordinate our host country agendas. Japan will be hosting APEC this year. The President is going to go to the APEC summit, and we want to work closely with Japan because we're going to be the hosts next year.

So, this bilateral element of how we coordinate on APEC is important. The hope is that there can be achievements in Japan next year that can build a firm base for our relations--for our hosting the following year.

In Indonesia, we've been working to advance the comprehensive partnership that was launched in 2009. We've signed agreements for cooperation on science and technology, and we're finding new ways to collaborate on energy, on the environment, and climate change issues.

Let me turn now to China, because China is clearly the single most important of the new emerging economies and, therefore, our relationship with China is important. And really, no discussion of the region, or really no discussion of the global economy, can be a serious one without talking about China.

This is a country where we are working very hard to develop a wide range of areas for economic engagement. The most important one, and the one that's been most visible, is the Strategic and Economic Dialogue, the S&ED, which is aimed at engaging China on macroeconomic coordination, on trade policy, on domestic policies, and a host of other bilateral issue.

The US-China Joint Commission on Commerce and Trade is another group. This is going to be meeting soon. It's an example of how we can deal with a very specific set of issues relating to China.

As China continues to grow, we hope it will take a strong interest in and provide strong support for the global economic system. And let me just make a couple of very quick points about this, because one could always have a discussion of China which would last several hours. But, I'll just make two points that I think are very important.

Point one is that our goal is not so much to try to tell China what to do, because we know that that policy doesn't work very well and is really not the spirit of what we're trying to do because they have their own sets of interests and they have a very strong sense of their own national purpose.

But, the broader point is this. They have, as they become more important in the global economy, a very serious stake in making sure the global economy works effectively, the financial system works effectively, the trading system works effectively, the international investment system works effectively.

And in order to do this, they must increasingly take into account, in the way they conduct their domestic policy and the way they conduct their international economic policy, the impact of these policies on the global economy, because increasingly what happens is the global economy will feed back on their own domestic economy.

If they want their companies that are increasingly investing abroad to have level playing fields in the countries in which they invest, there has to be a level playing field for foreign companies in China. If they want the intellectual property of their companies to be respected around the world, they have a strong interest in respecting the intellectual property of foreign companies in China.

This is not to say that they are going to do this right away. But, it does illustrate as they become more global, as their going-out policy becomes more robust, they have an interest in the global rules, in making sure that the global rules are respected, in making sure that they don't do anything internally that undermines international respect or international adherence to those global rules as that affects companies in China.

The second point relates to a specific area that I've been focusing on a great deal, and American companies have been focusing on a great deal, and that is the protection of intellectual property. And let me be very clear about why this is important.

First of all, there are international rules that are very clear about the importance of it. But, second, the United States is not as able as it was, and in many cases can't compete very much, in international markets with respect to low wage products. More and more countries of East Asia are competitive in that area and that arena.

What enables us to compete and what the future growth of our economy depends on are knowledge-based industries, industries that produce innovative products, innovative procedures, innovative ways of doing things. You know, higher and higher value-added production is the key to American growth.

And not just American growth. This applies to Europe and other countries as well. But, focusing on the US, that's where our growth is going to come from.

And it is extremely important therefore, recognizing that intellectual property, patents, copyrights, innovative ideas, creative arts, movies and records things of that sort, these are all part of this more and more innovative knowledge-based economy that is going to drive our future growth.

If countries, individually or collectively, but individually in the case I'm talking about, have policies that are designed to take or force the transfer of intellectual property, in ways that are inconsistent with international rules and obligations, from American companies to their companies which they

use to compete back against American companies, or other companies for that matter, that presents a big threat to our future growth.

And the Chinese have what they call their core interest. We have a core interest. And our core interests, we have several, but one of our core interests is the protection of our intellectual property. That is a core interest for the United States.

It's a core interest of the United States because our growth and our ability to create jobs and our ability to compete depends on giving our companies the incentives to invest human capital, to invest money, to invest talent, to invest ideas in developing new innovative products which they can use to compete in global markets. That's the future of our ability to compete.

And if that intellectual property is somehow taken or there is wholesale counterfeiting or forced transfers as a precondition for doing business in other countries, that weakens our prospects for economic growth. That weakens our prospects for creating jobs. And that is something that we will resist as strongly as we can, because it is a core interest of the United States to have those sectors do well and to continue to do well.

Now, there have been some improvements in China. But, there is still a long way to go in terms of protection of intellectual property. And there is still a long way to go to give assurances that, in order to sell to the government of China, let's say, companies should not be forced to transfer



technology or they should not be forced to participate in policies that are known as indigenous innovation which could be used in ways that are harmful to companies that have intellectual property in the United States and can't compete in China because they are not willing to transfer that intellectual property or that the innovation for their products has not come directly from China.

So, indigenous innovation, protection of intellectual property, these are all very important issues that we're dealing with China. Our goal is not to have a confrontation with the Chinese on these issues, but it is to be very assertive of our interests and to explain to the Chinese that, as their companies become more competitive around the world and they want their investments and their intellectual property to be protected, they need to do the same thing vis-à-vis our companies and our intellectual property.

So, this is a very important area of our relationship that we are focusing on a lot, and we will continue to focus on a lot.

Let me conclude by saying that we see, as I mentioned at the outset, the opportunities for closer cooperation in the Asian Pacific as being critically important to the United States. Not just China, not any one country, but the broad sweep of relations between our two regions is very important.

We want to make good use of APEC, of ASEAN. We want to implement the new FTAs that I've been talking about. We want to broaden the scope of

our bilateral dialogues. And we want to share in the economic opportunity which John Hay predicted more than a century ago.

We do see the Pacific as the ocean of the future. We consider ourselves a Pacific economy, a Pacific country. And we want to develop our relations across the Pacific for the benefit of American companies, but also because, if we're going to have a more effective global trading system, cooperation between the United States and the countries of the Pacific are going to be very important to doing that.

Thank you very much. Happy to take questions or comments or strong dissent.

Yes?

**Ms. Lisa Hopkins:** Hi. I'm Lisa Hopkins. I work at the Army Directed Studies Office. But, my question is just really my personal opinion.

Thank you so much, Mr. Undersecretary, for coming to speak with us today and for all of your remarks. I was wondering if you would allow me to mention a few numbers that are on the other side of the debate.

You said we need to explain to Americans how trade with China is fair. I just wanted to cite some things that are on the other side of that.

The US Steelworkers Union recently submitted a report--.

**Mr. Robert Hormats:** --No, that's--that wasn't what I said.

**Ms. Lisa Hopkins:** I--okay. Go ahead.

**Mr. Robert Hormats:** I said we have to ensure that trade is fair. I'm not--I didn't use the word demonstrate that it is. That's a different matter.

I think there are very substantial areas where the playing field is not level, and we have to make it level. I wasn't trying to suggest that it was level at this point, because it isn't.

**Ms. Lisa Hopkins:** Okay. Thank you.

**Mr. Robert Hormats:** There are areas that require more leveling. Let me put it that way.

**Ms. Lisa Hopkins:** If I can just mentioned a couple of them.

**Mr. Robert Hormats:** Okay.

**Ms. Lisa Hopkins:** So, I'm sure you've already heard about the Steelworkers documenting the WTO violations by China, and also that the American Chamber of Commerce has recently come up with a report about Chinese investment in the US, which is, for them, trying to prove that free trade with China is beneficial. And it mentioned about 1,300 jobs that China created in the US through investment, whereas just one factory that employs migrant workers in China employs somewhere over 300,000 that takes orders from Apple and HP and Microsoft, etc.

And then, you were also talking about the knowledge-based economy and how the future is not about low wage jobs but about innovative and high value added jobs, which is something I'm very concerned about.

And we had a lot of talk about having clean energy jobs for America. But, if you've heard about the company BYD in China that Warren Buffett invested in, they're undercutting other countries such as Japan and South Korea because they don't use sophisticated machines to make their cars. They use 140,000 migrant workers who they pay about 3 percent of what a US worker would get.

And so, I'm just wondering how can we--what can we do, what can the State Department do, to try and make the field more level and, at the same time, to get some of these knowledge-based jobs in the US?

Thanks very much.

**Mr. Robert Hormats:** Thank you. Those are very interesting, important questions.

Let me make a couple points. First of all, I still think the United States can be very competitive in manufacturing. I do not want to be interpreted to mean we cannot be a competitive manufacturing country. We can be. It's just that the manufacturing sector of this country depends more and more on producing innovative products that we sell around the world.

So, if you look--for instance, I was in India just, as I say, a couple days ago. And I went to the--India has built two new airports, one in Delhi and another in Mumbai. The Mumbai airport is in the process of being built.

A great many American companies, manufacturing companies, are selling products for that airport, including all of the carpeting for that airport.

Now, we don't see ourselves as a big textile exporter, but carpeting for the airport in India is being made by American companies.

A lot of the metal that goes into it is specialty metal products being made by American union workers and metal companies that produce special kinds of steel and other things that go into the airport.

And the information technology system, the people movers, all those things, American. Huge number of American products are there, manufactured products. The architecture and some of the planning is done by American companies. Those are service products and we're doing very well in those.

But, we can compete in the manufacturing sector. It's just that it's higher and higher value added products that we're selling. That's the point.

The second point on the jobs is that we want--and China has its own model and there are these companies that employ large numbers of people, as you say, to produce things. But, wages are very low and it's natural that there would be labor-intensive production in China. I mean, that's the way labor--countries with a lot of labor operate.

But, there are things that are changing in China. And one of the things that I found very interesting, and I'll just quote this. When I was in Xiamen just a couple weeks ago, Xi Jinping, who's the Vice President of China and the heir apparent made a set of very interesting statements.

And basically, he said that China--and let me just quote it, because I think it's interesting and I'll reflect on it after I've quoted it. "China is now in a new phase of reform and opening up, and is working to integrate the translation of its external and internal patterns of development in order to gain a new edge in the international economic arena, and to be more competitive in the globalized world economy."

Now, what's going on there? One of the things that's going on in eastern China in particular is that wages are going up, that it's harder and harder for these eastern Chinese companies in the Pearl River and the Yangtze River area deltas to compete in low wage goods because wages are rising there. And this is not to say that they're at American levels yet. Of course they're not.

But, increasingly there are changes in China. And China now, at least with respect to eastern China, is going to increasingly be attempting to compete not just in these low wage areas where you have large numbers of factory workers of the kind you described, but they're going to be moving up the production cycle, the value added chain.

And we need to prepare for that by becoming even more competitive. They're going to be producing airplanes that they're going to want to sell. They can't do it yet, but you know in four, five, six, ten years, they're going to be producing airplanes. Probably small frame airplanes at first, but bigger airplanes over a period of time.

Automobiles, they're beginning to produce automobiles. They're not selling them here yet. But, if you look at the South Korean example, they clearly see what happened in South Korea, that they started with small cars and they moved up to bigger and bigger cars.

They're going to be competing increasingly not just in that sort of traditional textiles, toys, things of that arena, but more broadly in the other sectors. So, we have to be prepared for that.

And what it means is that they won't be as labor intensive as--or the exports won't be as labor intensive as some of the exports are now. They are going to be moving more into higher and higher value added products.

That means that the competition in the United States, it's not going to get any less. It's going to get even more intense and it'll be in areas that are in the higher end.

Now, that's one reason we have to protect our intellectual property from the kinds of concerns that I've raised. But, it also means that the kind of areas in which they are going to be--will be competing will be changing over a period of time. And that's a reality we're going to have to anticipate.

Yes?

**Ms. Ann Lee:** Hi.

**Mr. Robert Hormats:** Hi.

**Ms. Ann Lee:** Thank you so much for your comments. I'm Ann Lee with NYU.

I guess I understand your argument about how we need to protect intellectual property and have that enforced. But, I've also heard international lawyers also discuss that there's been no agreement internationally about what should be considered IP and what's not.

And I've also heard arguments that it could actually hinder innovation if it's too stringent. And they mainly talk about, in the biotech space, where companies patent genes and other, you know, basic discoveries of, you know, what makes up the DNA and so forth. And so, when you have IP on those things, it could actually stop companies from developing the necessary medicines and so forth and other innovations.

And so, I'm just curious what your response to is that.

**Mr. Robert Hormats:** Yes.

Well, —to address the second part first, that gene issue is very complicated--I was on the board of a biotech company. I'm fairly familiar with the issue, and it is a complicated issue about what you can patent, what you cannot patent.

And I leave it at this--there's a very specialized debate going on on that issue which I will stay out of, because while I know something about it, I don't know enough to engage in it. But, you've raised an issue that's an ongoing active debate.

But, I will make two broader points, one of which is that there are generally accepted rules on the protection of intellectual property. These



have been worked out in the WTO over a period of time. And they have been worked out in the OECD.

Now, are there little differences of opinion? Sure. But, there is broad agreement about the nature of the protection of intellectual property and why it's important.

There is also, in the WTO, a government procurement--it's called the Government Procurement Agreement, which specifically says that foreign companies operating in other countries should be treated equally with the companies that are indigenous to that country. There should not be discrimination against those companies, and certainly should not be discrimination against their products if the--and the judgment should be not be made whether the government of a country should be a company's product based on whether the innovation was domestic or the innovation came from the originating country.

So, just making discriminatory judgments on the basis of who owns the intellectual property or where the intellectual property came from is specifically prevented by the Government Procurement Agreement.

So, there are plenty of international agreements and international standards that most countries adhere to. China has not joined the Government Procurement Agreement. We would like to see China join that. And in fact, when they joined the WTO, they committed to joining it but they haven't done it yet. But, there are conversations underway.

And as I say, the goal here is not to have this done in a confrontational way with China. It is to explain to the Chinese that they have a strong interest in doing these things because it benefits their own long-term interest.

Moreover, there are a number of Chinese companies that are just as concerned about the protection of their intellectual property as American companies are concerned about the protection of their intellectual property, because the Chinese are coming up with patents all the time.

And when I was there, the last couple of times I've been there, I've met with Chinese companies, and they're very strongly of the view that they want intellectual property protected because they're putting money and talent and time into developing intellectual property.

And I'll actually tell you a story. This goes back a while ago, but it sort of illustrates the point that we're not--this is not us versus China. That's one of the points I want to make. It is not a confrontational issue.

It is about the United States and many, many, many Chinese who believe that the intellectual property protection is critical to their economic futures just as we believe it's critical to our companies and our national economic future.

And the example I'll give you is sort of a humorous one, but I think it illustrates the broader point. Several years ago, Deng Xiaoping's daughter wrote a book. Her name was Deng Maomao, wrote a book called My Father:

Deng Xiaoping. This was originally in Chinese and then it was printed in English.

And there was a dinner party for her in New York. She was doing her book tour. And the question of intellectual property protection came up. And someone said, you know, intellectual property protection in China really needs to be improved.

And she said, "That is exactly right." She said, "I will tell you a story. I wrote this book and within two weeks, four pirating companies have been selling these books on the streets of Shanghai." Four companies had pirated the book of Deng Xiaoping's daughter.

Now, you know, the IQ level of someone who would do that needs to be questioned. But, then she found out who they were and they were arrested, as you would think would happen. But, good for her.

But, it illustrates the point that there are plenty of Chinese who have exactly the same concerns and are just as passionate about it as we are.

And the notion of, you know, protection of intellectual property stifling innovation, I've heard this argument. But, let me make the counterpoint to this. And that is how do you get the huge amount of upfront capital required to develop new innovative products if you believe that within a short period of time someone is going to counterfeit your product and sell it without having put up the capital or the expertise or the innovative input? How do you create the incentives for innovation if you think that the system

is so weak in protecting intellectual property that you won't get the benefits of the money and the effort you've put in?

Think about it. It just doesn't make any sense. So, I'm a great believer in this, and there's an enormous body of evidence, enormous, that protection of intellectual property is important because it's the basis of creating incentives for increasing innovation. And that's the basis for our future growth.

And, you know, Abraham Lincoln, who was the only American president to have actually filed for and achieved a patent, made the same point 150 years ago. So, I'm not alone.

Yes?

**Mr. Dan Michaeli:** Dan Michaeli from the Council on Foreign Relations. I had a couple of questions, but I'll try to make them brief.

The first is US manufacturing. US manufacturing has actually continuously gone up--.

**Mr. Robert Hormats:** --Right--.

**Mr. Dan Michaeli:** --In recent years. It's just that we're employing fewer people in manufacturing.

**Mr. Robert Hormats:** Right.

**Mr. Dan Michaeli:** So, one sort of question to ask is, if manufacturing isn't where we're going to be creating jobs in the future, how

do we think about our own domestic job goals and how that factors into our export promotion goals?

**Mr. Robert Hormats:** Right.

**Mr. Dan Michaeli:** And then, the second question I wanted to ask is I think you rightly pointed out that there are both internal barriers for trade that are quite serious and external barriers that continue to exist.

As China, Japan, and Korea potentially move towards a free trade agreement, not around the corner but at some point in the future, that certainly puts the US at a disadvantage. At the same time, we're not talking about--we're talking about trying to reduce the internal barriers to trade in China, which will help Japan and Korea in that case. But, we're not talking at all about a free trade agreement with China that would give us access to the Chinese market on par with Japan and Korea.

Very politically sensitive, but I'm wondering are there ways, maybe secular free trade agreements, or are there creative ways of trying to address that issue for US companies?

**Mr. Robert Hormats:** Well, that one is a very complicated issue. I think we're--well, right before I get to that, I'd like us to get the KORUS agreement done first and then we can turn to some of these broader issues.

But, the point generally is that the more of these free trade agreements that we're not engaged in, the greater the risk that our market share will get sliced away, although I don't think a free trade agreement

with China is on the horizon probably in my lifetime, although maybe. I don't know. It depends.

But, you're right. There is a great deal of work being done in the region to strengthen free trade agreements in other countries. China does have one with ASEAN. So, there are these things.

They're not the same as the free trade agreements we have. There are a number of elements that are excluded. But, they still do tend to give these countries specific market advantages that we would not otherwise--we would not have.

The broader point on the first part of your question, manufacturing, it's an issue because you're exactly right. We are still a very strong manufacturing country. It's just that, as you say, a lot of what we manufacture has a lower labor input per unit of output than in the past just because these are higher value things that also use more and more technology and fewer and fewer workers per unit.

On the other hand, what's very interesting is that we still are able--if we can continue, we're developing new manufacturing industries all the time. And even though certain types of companies use fewer workers to produce the same widget, we're producing more and more different kinds of widgets, different kinds of products. So, we can still maintain a relatively strong manufacturing sector.

The other part of the thing is, and I mentioned it a while ago, we are attracting and we need to attract more foreign investment, foreign direct investment. And that can be very helpful in terms of creating new jobs. This is in terms of greenfield investments and in terms of mergers and acquisitions of existing companies.

So, one of the key points for us is to be able to attract more foreign investment from the rest of the world. That can help us. And a lot of that investment, that foreign investment, is in the manufacturing sector. So, that's one of the ways of doing it.

But, the other part is that, increasingly, the service sector is going to be the sector that's going to create more jobs. The healthcare sector is going to create more and more jobs. Education, a lot of teachers are retiring. We need more teachers in the United States.

As the population ages, there's going to be more requirements for people to take care of an aging population. There are a whole range of new companies that are being developed in the services sector, and those will create jobs.

But, I still think we can create manufacturing jobs. It's just they won't be the same as those of the past.

**Ms. Meredith Miller:** Thank you very much.

**Mr. Robert Hormats:** Thank you very much. Sorry we're done.

Thanks.

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