



CHINA STATE VISIT: ASG's 8 ESSENTIAL QUESTIONS

SEPTEMBER 2015

CONTEXT OF PRESIDENT XI'S VISIT

President Xi Jinping is expected to travel to the United States for his first State Visit from September 22nd to 28th, with stops in Seattle, Washington DC, and New York.

The trip comes at a time when anxiety about China's stock market instability, flagging growth, and recent currency devaluation is high and these issues will now be a part of the visit agenda. In addition to hearing from Xi regarding the steps China is taking to arrest these negative developments, President Obama will raise questions about China's recent devaluation and exchange rate reform, and he may urge President Xi to avoid large-scale depreciation of the RMB.

Before these financial market and economic issues were suddenly thrust into the forefront of the visit, U.S.-China relations were already beset by a growing list of challenging political, economic and security issues that has created a worrying rise in tensions over the course of this year.

According to recent media reports, the Obama Administration is considering sanctions against Chinese (and other foreign) enterprises and individuals in response to evidence of cyber theft. Timing for announcement of these potential sanctions is unclear, but it would likely torpedo prospects for a successful visit if sanctions were unveiled in advance of President Xi's visit.

ASG provides the **8 Essential Questions** to consider when judging whether this State Visit is a success:

1. WHAT ISSUES WILL BE AT THE TOP OF OBAMA'S MEETING AGENDA?

For the Administration, the list of U.S. priority issues to discuss with China includes: cyber espionage and China's cybersecurity regulations, market access restrictions, territorial disputes in the East and South China Seas, and human rights. President Obama will also seek answers about what the Chinese government intends to do to restore confidence in its domestic stock market and spur growth. The Chinese

ABOUT ASG

Albright Stonebridge Group (ASG) is a leading global strategic advisory firm that helps our clients succeed by assessing and managing risks, identifying and seizing opportunities, and solving commercial, political, and regulatory challenges in international markets.

Chaired by former U.S. Secretary of State Madeleine K. Albright, White House National Security Advisor Samuel R. Berger, and Secretary of Commerce and Kellogg Company CEO Carlos M. Gutierrez, ASG's worldwide team has worked in more than 100 countries and across all major industries.

ALBRIGHTSTONEBRIDGE.COM

government has staked its credibility on an effort to control Chinese equity markets through administrative and regulatory actions to restrict selling and a massive infusion of financial resources to prop up prices. These heavy-handed measures, however, have not been effective, and have fueled questions and concerns about President Xi's commitment to an economic reform agenda that aims to substantially increase the role of market forces in the financial sector and throughout the Chinese economy.

Against the backdrop of China's rise as a global power, the two countries are struggling to agree on a compelling, strategic rationale governing the relationship. Mutual mistrust is rising, and both sides are preoccupied with domestic priorities. Although some cooperative outcomes will be announced during the visit, including commercial contract signings, the two sides face serious impediments to achieving the kind of progress necessary to put relations on a substantially more positive track. That said, the direct exchanges by the leaders will be very important in preventing further misunderstanding and increased tensions, and both sides are motivated for the visit to showcase where the U.S. and China cooperate, while not shying away from issues on which the two countries fundamentally disagree.

2. WILL OBAMA INSIST THAT CHINA AVOID LARGE-SCALE DEPRECIATION OF THE RMB?

President Obama will likely urge President Xi to avoid using further devaluation of the currency as a stimulus measure. China's recent decisions to devalue its currency and alter its exchange rate mechanism were likely motivated by two primary government objectives: to spur export growth in the midst of a slowdown and to improve the RMB's chance of being included in the IMF's Special Drawing Rights currency basket. The devaluation has raised fears that China could trigger a series of competitive devaluations that would undermine global growth and also has reignited the debate in Washington about the need for a tougher U.S. policy on currency issues. President Xi will likely push the U.S. to hold off on raising interest rates.

3. WILL THE TWO LEADERS MAKE ANY PROGRESS ON CYBER ESPIONAGE AND CYBERSECURITY?

From the U.S. perspective, cyber issues remain among the top-tier of bilateral concerns. There are two distinct policy challenges: (1) cyber-intrusions of U.S. government agencies and companies linked to the Chinese government, and (2) China's introduction of domestic cybersecurity laws and regulations that contain problematic provisions that could serve as discriminatory market access barriers to foreign suppliers of China's IT infrastructure.

- While Chinese officials have continued to dismiss allegations of government involvement in cyber espionage, Chinese State Councilor Yang Jiechi signaled in July that China was open to cooperation on creating international norms for cyberspace. It is unlikely, however, that any meaningful agreements will be reached during the visit on this extremely challenging issue.
- President Obama will likely raise growing U.S. concerns about new Chinese laws and regulations that threaten to restrict market access for foreign IT suppliers. Some progress was made in April, when China agreed to suspend a regulation issued by the China Banking Regulatory Commission (CBRC) that required the use of "secure and controllable" technology in bank IT systems. The U.S. government urged that this suspension be made permanent, but this month the CBRC asked U.S. IT companies for input as it prepared a new draft of the regulation. The USG will seek

commitments that China ensure that the CBRC regulation, and other measures, will not contain discriminatory security requirements.

4. WILL OBAMA PLAY HARDBALL OVER THE SOUTH CHINA SEAS?

Tensions have risen over the past several years between China and the United States over China's more assertive stance toward disputed territories in the East and South China Seas. More recently, China accelerated land reclamation activities in the South China Sea, intended both to strengthen China's territorial claims as well as its force projection capabilities. Defense Secretary Ashton Carter has criticized China's actions and pledged that the U.S. will continue to defend freedom of navigation. In response, the Chinese government has criticized U.S. intervention in the region. In the run-up to President Xi's visit, China has apparently curtailed its reclamation and construction efforts. China has long resisted U.S. efforts to promote regional codes of conduct on territorial disputes, and there has been no indication that a breakthrough in this area should be expected.

5. WHAT ABOUT HUMAN RIGHTS?

Human rights issues in China have long been a source of bilateral contention, but this year the scope of American concerns has broadened. In August, ten leading U.S. senators wrote a letter to President Obama urging him to raise human rights issues with President Xi, expressing alarm at the dramatic rise in detentions under Xi and criticizing China's draft law on managing foreign non-governmental organizations. The draft law, released this spring, has raised fears that many U.S. NGOs, educational, commercial and cultural institutions might be forced to leave China. Another issue that has come into public view in recent weeks is the controversy over allegations that Chinese law enforcement agents have entered the United States without official permission to seek to repatriate Chinese nationals suspected of corruption. For its part, China will press the U.S. for repatriation of Chinese criminal suspects who have fled to the U.S., including the brother of disgraced former top aide to President Hu Jintao.

6. WILL THERE BE A BREAKTHROUGH ON THE BILATERAL INVESTMENT TREATY (BIT)?

The U.S. and China are committed to concluding a BIT, but the negotiations have reached a challenging stage. The United States is pressing China to limit proposed investment restrictions that will be contained in the "negative lists" submitted by each country. At the July Strategic & Economic Dialogue meeting held in Washington, DC, the two sides agreed to exchange improved negative lists in early September. There is substantial Chinese internal resistance to making additional concessions, so it is likely that negotiations will likely be quite protracted, and no major breakthrough should be expected during the visit.

7. WHAT DO THE CHINESE WANT TO ACHIEVE FROM THIS VISIT?

For China, a successful visit will include U.S. acknowledgement of President Xi's stature as a world leader and China as a global power. In addition, China will likely raise its desire to be accorded market economy status in 2016, assurance that the U.S. CFIUS process will not discriminate against Chinese investors, and greater cooperation on repatriation of Chinese criminal suspects.



8. WILL CHINA AND THE U.S. AGREE ON A CLIMATE CHANGE STRATEGY?

Perhaps the best prospect for deepening bilateral cooperation is climate change, a priority issue for both presidents. The two governments will seek to build on their historic agreement during President Obama's visit to Beijing last November, when the two countries each committed to specific emissions reduction targets. The two leaders hope to announce a joint strategy to support an international agreement at the United Nations Climate Conference in Paris in December 2015. In addition to climate change, we anticipate the two sides will announce cooperation on energy, global health and development challenges, Iran, North Korea, and potentially Afghanistan/Pakistan.

Please contact Julie Mason at jmason@albrightstonebridge.com for more information or to interview with a member of ASG's China practice.

