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News Analysis

Balancing Act With Beijing

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BEIJING, Dec. 15 — Treasury Secretary Henry M. Paulson Jr. went to China with a team of heavyweights, including an array of Bush administration cabinet members and the Federal Reserve chairman.

But he is returning home to a more critical audience that is unlikely to be satisfied with the inconclusive results he achieved in opening a new economic dialogue with Beijing.

The problem is that Mr. Paulson faces a growing number of lawmakers — and behind them powerful but divided business constituencies, along with a politically energized labor movement — who are not counseling patience right now, especially after an election where China-bashing was a bipartisan sport.

While no members of Congress were actually in Beijing, they might as well have been sitting at the rows of tables at the Great Hall of the People surrounded by red, gold and green décor and even more ornate rhetoric. The antitrade sentiment in Congress lurked over the meeting, and certainly was felt by the Chinese.

One sign that the American delegation was playing to an audience both here and at home came in the speech delivered by the Fed chairman, Ben S. Bernanke, on Friday to the Chinese Academy of Social Sciences, in which he made a strong case for China to let the value of its currency rise against the dollar.

Mr. Bernanke’s advance text, replete with 22 footnotes, called China’s undervalued currency an “effective subsidy” of exports. In the end, though, he omitted that term, taking a more diplomatic approach, possibly because the term might feed protectionist sentiments on Capitol Hill while ruffling more feathers among the Chinese.

Mr. Paulson, in an interview before leaving here Friday, acknowledged that the Chinese were motivated to act out of fear of retaliation by American lawmakers who charge that inexpensive Chinese goods have cost jobs and forced the country to borrow $700 billion from China to finance its import addiction.

“The way I’ve articulated the situation to the Chinese is to look beyond Congress,” Mr. Paulson said. “Congress is a reflection of the American public, and the American public has a perception that the benefits of trade between our two countries aren’t being shared equally or fairly.”

Mr. Paulson said it was not realistic to expect the dialogue, which he began in September, to produce concrete results this quickly. But, he added, “The American people are rightfully going to demand that we show tangible results along the way.”

Some already are. The United States Business and Industry Council, which represents some 1,500 small- and medium-size manufacturers and generally opposes free trade initiatives, said in a statement that Mr. Paulson and his high-level delegation had engaged in “chit-chat diplomacy.” It called the meetings “yet another meaningless mission to China — one that accomplished nothing while domestic manufacturers and other U.S. businesses continue to be victimized by Beijing’s predatory trade practices.”

Part of the frustration among business groups and lawmakers is that Mr. Paulson, by the mere fact that he was accompanied by several cabinet members and Mr. Bernanke, may have raised expectations that he would bring home more concrete results. Instead, the meeting wound up Friday with an agreement to set up several study groups and other pledges, but only atmospherics to suggest that China might eventually stop undervaluing its currency to promote exports.

Mr. Paulson said the currency issue was a “core concern” and would take time to resolve. But for China it was Congress that was a core concern.

That was obvious from the pointed comments of Wu Yi, the stern vice prime minister and principal interlocutor in these sessions, who many times criticized Americans for not understanding China’s situation as a country that has had to rely on exports to develop and needed time to transform its economy away from that model.

“I think both sides know that it is not good politically for Paulson to go back empty handed,” said Jin Canrong, a professor of international studies at Renmin University in Beijing. “China can also see that Paulson is concerned about the incoming Democrats on this issue. He has very actively delivered this message of concern.”

Another session of the dialogue, also with many cabinet members on both sides, was scheduled for May in Washington, where it is certain that members of Congress will participate in some form, if not directly in the talks.

As for Mr. Bernanke, his lecture was a powerful though perhaps esoteric argument for noneconomists that is likely to be closely studied by Chinese officials.

The Fed chairman explained that, to keep the currency undervalued, China has to buy dollars to prop up their price. Buying dollars means exchanging them for Chinese currency, flooding China with an abundance of renminbi, the domestic currency.

The renminbi glut would normally fuel inflation, he said, so China sells bonds to Chinese owners of renminbi to take them out of circulation in a process known as “sterilization.” Mr. Bernanke told the Chinese that can only work so long.

China’s desperate need to keep its currency low to support its export drive, meanwhile, forces it to keep interest rates artificially low as well. The result is that China’s central bank is unable to use monetary policy to manage its economy.

Artificially low interest rates have another downside: When Chinese bureaucrats make loans for political objectives, mainly to money-losing state enterprises layered with Communist Party bureaucrats, the interest rates they charge cannot reflect the risk involved or the market value of investments, as they do in the West.

It all boiled down to Mr. Bernanke telling the Chinese that they cannot have a sound market economy and also an artificially low currency value. Mr. Paulson, treating Mr. Bernanke as his new best friend, called it a great speech that offered “a whole new dimension” to the American arguments.

Some in the Bush administration think China is going through an internal struggle, and that forces favoring a free-floating currency are taking baby steps to get there, by letting the yuan rise ever so gradually to avoid touching off a panic, in hopes of persuading leaders of the export-driven economy that they can adjust to it over time.

Whether Congress can be convinced of that point of view is now Mr. Paulson’s main challenge, along with negotiating cuts in the federal budget and savings in Social Security and Medicare to make good on his pledge in Beijing to do something about the United States’ low savings rate.

The key to whether Congress proves willing to give Mr. Paulson more time lies, in the administration’s view, with the business groups the members listen to.

That is why the Treasury chief met with the United States Chamber of Commerce, the National Association of Manufacturers and leaders of Fortune 50 companies before he went to China. He plans to meet with them again when he gets back. If they see currency moving in the right direction, they may be more patient.

But without concrete evidence that the bilateral trade imbalance between China and the United States has started to shrink, Mr. Paulson’s aides concede, he does not have too much time before Congressional pressure leads to bills imposing tariffs or other sanctions on China.

The Chinese see President Bush as ready to veto such legislation, but administration officials hope it never comes to that.