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# 2013 POLICY RECOMMENDATIONS FOR THE OBAMA ADMINISTRATION

Steven W. Lewis, Ph.D.  
C.V. Starr Transnational China Fellow

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# *U.S. – China Relations: Energy and Environmental Policy*

*By Steven W. Lewis, Ph.D.*

## **Overview**

Assuming current conflicts between China and the United States on security matters—in the South and East China Seas, and in cyberspace—can be solved through skilled negotiation and diplomacy, the major long-term threat the two superpowers pose to each other is a lack of coordination in solving shared energy and environment problems. Our mutual love of decentralized government, and unchecked consumption, has produced a situation in which the two largest economies each lack effective national energy and environmental policies; moreover, neither feels the need for such policies in the absence of actions to create them on the part of the other. Increasingly, China and the United States are competitors in a race toward unsustainable growth, and if we are not careful we will soon also become unwitting partners in an energy and environmental suicide pact.

A second-term Obama administration should take prudent action now to avert disasters that are very real and yet fortunately still years away from manifesting themselves:

- **Recommendation 1:** The president should leverage his immense personal popularity with young people to engage the American and Chinese publics and move them toward shared action to solve shared energy and environment problems.
- **Recommendation 2:** The administration should renew efforts to integrate the Chinese government into the energy policy coordination organizations of the major energy-consuming nations, including the International Energy Agency.
- **Recommendation 3:** The administration must not only deepen the information and research ties between U.S. federal and Chinese central government energy regulators, they must also take them to the next level and broaden them to include the major regulators of energy investments in both societies: local governments.

## **Background**

Although currently there is increased potential for conflict between the United States and China in the South China Sea and the East China Sea, in cyberspace, and across the trade negotiations table, relations in general between the United States and China are fundamentally based on cooperation. And yet, even assuming the Obama

administration's able experts and diplomats can cool down the above hot spots—as they are working hard to do—and that they can ensure top foreign affairs and economic officials who are retiring are replaced by equally capable and China-savvy negotiators, America and China will surely still face considerable obstacles to future coexistence. This is inevitable not because of differences in political ideology (i.e., one society is led by a government with a multiparty democratic system, and the other is a state based on one-party authoritarian control of all organizations and groups); or because of differences in economic structure (i.e., one is based on small and medium enterprises and has very few state-owned companies, the other supports and depends upon a core of enormous central-government-owned manufacturing and financial enterprises).

The biggest threat that America and China pose to each other in the long-term is not a lack of cooperation, but rather a lack of coordination. We are the two largest economies, the two largest consumer societies, and the two largest decentralized political and economic systems. Chinese and Americans may differ on many political and cultural beliefs, but what we share is a love of competition and of consumption. We look up to the Acropolis but we spend all of our time playing in the Agora, enjoying the give and take, the take and the give.

Chinese provinces and municipalities compete with each other intensely for capital, labor, and technology. An offer to investors of tax breaks and local government subsidies in Shenzhen in South China is soon matched by greater, undercutting offers from Shanghai in East China, or Dalian in Northeast China. The same competition exists between Houston, Chicago, and New York. And Chinese and American laborers and professionals alike work some of the longest hours seen anywhere. Americans are accustomed to a few weeks of vacation each year, and so are most Chinese. American and Chinese consumers are equally relentless: there are no blue laws that keep businesses closed on weekends or evenings in either Los Angeles or Wuhan, or New Orleans or Xiamen. Chinese and Americans work hard and shop harder. As many of the light goods consumed in America are made in China, and as many of China's top scientists, educators, and innovators are educated in America, and as the government budgets of each country are dependent on the continued consumption of financial instruments and strategic investments of the other, there is a very real symbiosis: a state of "Chimerica," as some observers have dubbed the union of the world's two largest economies. America has replaced the Mutual Assured Destruction relationship with the Soviet Union during the Cold War with one of Mutual Assured Dependence with the People's Republic of China.

Fortunately for all concerned, both Americans and Chinese now recognize that such unchecked and unregulated consumption is not sustainable. The majority of Americans now believe in global warming and demand government action to slow the consumption of carbon fuels and to increase research to find new ways to keep greenhouse gases from radically changing our environment. Surveys in China reveal similar beliefs there, with the Chinese central government proposing aggressive industrial policies to curb carbon-intensive energy use as part of its 12th Five Year Plan (2011-2016). Chinese citizens are

increasingly mobilizing to protest harmful industrial byproducts in their living spaces, and it is only a matter of time before the citizens of the world's most polluted cities—Beijing and Shanghai—react as London's did after the Great Smog of 1952 and demand clean air legislation and a shift to cleaner forms of energy.

The danger to both China and America is that we will respond in radically different ways, and in particular adopt new technologies and systems of energy production and distribution and consumption that are not compatible with each other, thereby depriving both of our societies of the economies of scale and scope that might make such technologies affordable to all. This outcome is even more likely given the sustainability strategies of the two groups of governments who have moved early in order to try to capture the first-mover advantage in technological change: Western Europe and Japan/South Korea. The global effort to achieve sustainable growth is currently locked in stasis, waiting for the two largest consumer societies, the United States and China, to try to decide if they will follow either the European or the East Asian models—or if they will instead each go down their own road, or each share a common path. China and the United States need to come to a decision soon on whether or not they will walk down the same path to sustainability.

**Recommendation 1: The president should leverage his immense personal popularity with young people to engage the American and Chinese publics and move them toward shared action to solve shared energy and environment problems.**

The individual consumer today has unprecedented access to energy resources. The global climate clearly cannot survive the addition of hundreds of millions of new Chinese middle-class consumers who use energy as freely and wastefully as their U.S. counterparts. President Obama needs to lay the foundation for a new type of international energy public diplomacy, one that mobilizes consumers in China and the United States to shift to sustainable energy use and conservation techniques. Surveys show that both the Chinese and the American public are concerned about global warming, and that both populations value clean urban environments over unfettered industrial development. Neither population, however, sees its energy consumption and conservation as related to the energy consumption of the other. Furthermore, Chinese and Americans do not realize that their shared need for more reduced energy demand creates a vast potential marketplace for the low-cost adoption of clean energy technology and the training of conservation techniques. President Obama thus faces the critical long-term task of making American and Chinese consumers realize that, being part of the same problem, they need to collaborate on the adoption of lasting solutions to shared energy and environmental problems.

He should start with American and Chinese youth. President Obama's popularity with future generations of Chinese leaders was amply demonstrated during his chat with university students in Shanghai in fall 2009. The students were not just enthusiastic

about speaking directly with a charismatic world leader, they were excited to talk with somebody a generation close to theirs and one capable of communicating across cultures and generations. The new Chinese Party leader, Xi Jinping, showed his ability to speak more like an average person during his inaugural press conference on November 16, 2012, but it is unlikely he or other Chinese leaders will ever seek to engage China's young people in the language they actually use. Rules of Party discipline requiring that the Party Secretariat vet all public addresses by senior leaders make this especially problematic. Or, in other words, the Chinese government has few means to motivate China's youth to tackle energy and environment policy in a sustained and exciting way. President Obama, however, because of his charisma and his age—he is 10 years younger than President Xi—is capable of generating and then maintaining enthusiasm among Chinese and American students during his second term and for many years beyond.

In his 2009 meeting with Chinese students, President Obama skillfully redirected questions about himself toward answers that talked about a shared future between American and Chinese youth, including environmental and energy matters. It is now time for President Obama to go the next step and start a new public diplomacy initiative designed to bring together young Americans and young Chinese. As advocated by the Baker Institute Energy Forum, and by such advisers to the Obama administration as Kenneth Lieberthal and David Sandalow, a transnational or international youth corps focused on energy and environmental education in both societies would go a long way toward generating enthusiasm among both American and Chinese young people. Philanthropic foundations and individuals in both China and America could be persuaded to set up a nonprofit, public diplomacy initiative that would manage such a program in the years beyond the final Obama administration.

The Obama administration should also consider new forms of media designed to persuade both American and Chinese consumers that they are jointly responsible for the world's future sustainability. Recent research by the Baker Institute Transnational China Project reveals that America and China have much untapped potential in public service advertising (PSA) in their public spaces. Surveys of PSAs in the subway systems of American and Chinese cities show they share similarities, including a focus on energy and environmental issues, as well as rules requiring that 10 percent of spaces for all advertisements be reserved for PSAs. What they also reveal, unfortunately, is that most American and Chinese PSA producers view energy and environmental issues as largely local ones: people need to pitch in within their community to help, and local governments are leading the way on sustainability, etc. Missing in this is a global counterbalance to the worldwide proliferation of consumer ads telling people to shop like global middle-class consumers. But with little cost to taxpayers, Chinese and American students, citizen groups, and nongovernmental organizations (NGOs) could work together to develop PSAs that set up a dialogue between American and Chinese publics and begin to teach future generations in both societies the value of thinking of sustainable growth as a shared problem (which it certainly is). Both American and Chinese populations need to realize they cannot achieve sustainability without joint action, and

that each of them are working together toward this goal. Cooperation in this area of PSAs could also help generate cooperation between publics on other global problems, such as overconsumption of antibiotics.

**Recommendation 2: The administration should renew efforts to integrate the Chinese government into the energy policy coordination organizations of the major energy-consuming nations, the International Energy Agency in particular.**

The United States and its Organisation for Economic Co-operation and Development (OECD) partners have been discussing how to bring the future large consumers—India and China—into the oil supply stabilization arrangements of the International Energy Agency (IEA). In its second term, the Obama administration should continue to support these multilateral negotiations. These future oil consumers, and our Asian allies Japan and South Korea, need to have market access to diverse supplies of oil and gas—Asian countries currently receive relatively little oil and gas from Latin America, Russia, and Africa. China has only recently begun to import significant amounts of oil from Russia and Kazakhstan. These new energy superpowers also need to build adequate strategic petroleum and product reserves and to participate in international emergency release arrangements. Over the last decade, China has experienced gasoline shortages in its economically vibrant and yet resource-poor coastal regions because the country has not yet built stockpiles sufficient to see it through short-term disruptions in supply. The United States and other IEA nations must continue to work with the Chinese government to make sure China does not become a more aggressive seeker of overseas oil supplies or even a panic buyer in world energy markets.

On a related matter, the administration should also broaden the mandate of the new Global Shale Gas Initiative of the State Department to include working with the Chinese government and its oil and gas companies, at central and local levels, to explore the potential of shale oil. U.S. shale oil has added more than one million barrels a day (b/d) to domestic oil production, and an equal advance in China would greatly help China offset its four million b/d of imports from overseas, including two million b/d from the Middle East. Currently, the old oil-producing regions of China's North and Northeast—Heilongjiang, Jilin, and Liaoning in the Northeast, and Shandong and Hebei in the North and East—have made no efforts to develop shale gas, but they have expressed strong interest in shale oil. With advice from the U.S. State Department and joint ventures with many of the oil and gas multinational companies, and shale gas development companies of America, the three central national oil companies in China—CNPC, Sinopec, and CNOOC—are developing shale gas in Southwestern China's Sichuan Province and Chongqing Municipality. As a forthcoming report from the Baker Institute Center for Energy Studies shows, such assistance could potentially greatly help wean China's interior Northern and Western regions off of coal, but assistance in developing shale oil in the Northeast and North would make China much less dependent on its traditional Middle East energy suppliers, including Iran.

**Recommendation 3: The administration must not only deepen the information and research ties between U.S. federal and Chinese central government energy regulators, they must also take them to the next level and broaden them to include the major regulators of energy investments in both societies: local governments.**

In the last few years, the Chinese and American governments have set up joint energy research facilities in China and the United States. At the fourth meeting of the U.S.-China Strategic Economic Dialogue in June 2008, officials from both countries created the U.S.-China Ten Year Energy and Environment Cooperation Framework. Five task forces were formed to develop (1) clean, efficient, and secure electricity production and transmission, (2) clean water, (3) clean air, (4) clean and efficient transportation, and (5) conservation of forest and wetland systems. More recently, the formation of the new Bureau of Energy Resources within the State Department gives new strength and capacity to our efforts to work with the Chinese government on negotiation issues. This has followed a continual growth in institutional ties between the U.S. federal government and the Chinese central government. The annual meetings of U.S. and Chinese officials initiated during the Clinton administration have been replaced by daily, personal contact between the two large central bureaucracies.

The inclusion of energy and environmental issues in the Strategic Economic Dialogue should continue so long as these issues do not become subordinated to other economic interests or stalled. And if these task forces do not continue to produce concrete, measurable progress according to the goals outlined in the energy and environment cooperation framework, both governments should consider a higher level of formal interaction on energy issues. As the United States and other countries have done in the past, each government could task key central leaders with handling energy and environment cooperation. The U.S. vice president should be prepared to go to Beijing to discuss with the new 18th Politburo of the Chinese Communist Party under General Secretary and President Xi Jinping and premier-designate Li Keqiang what can be done to move forward ties on energy and environmental issues if the strategic dialogues do not bear fruit.

The Obama administration must be mindful that in energy and environmental matters it needs to keep its negotiating gaze fixed upon talks with Chinese officials with Politburo ranking. As a December 2011 Baker Institute Energy Forum report outlines, the National Energy Commission has an impressive title and high bureaucratic profile, and yet in practice its implementation strength is undeveloped. The National Energy Bureau under the National Development Reform Commission is still understaffed, and on energy and gas policy is largely dependent on the three national oil companies. The Obama administration must be able to credibly demonstrate that it can dispatch the vice president to Beijing to talk with the members of the new Politburo Standing Committee who run day-to-day economic policy if regular talks by lower level officials do not produce the required coordination and cooperation. Relying solely upon the Strategic and

Economic Dialogues or upon official ties from U.S. agencies might not move both sides past bureaucratic inertia. On the American side, the U.S. Department of Energy is highly focused on nuclear security and nonproliferation issues, even in its offices in Beijing, and the State Department's new Bureau for Energy Resources is focused on energy talks among diplomats and energy security experts.

But we also have to ask whether or not existing bureaucratic ties can themselves produce the type of long-term cooperation necessary for sustainable economic growth, especially growth that would reduce demand for energy. The current era of globalization is one marked by the increasing economic power of local government. China's central government directly controls nuclear energy and, through the three major national oil companies, guides investment in oil and gas; most of China's power is, however, produced by its 31 provincial and municipal governments. China's most advanced export manufacturing provinces alone spend \$3-4 billion each year on new power generation. In the new field of shale gas, it is local governments that are taking the lead, with the blessing of the central government, which feels that the three national oil companies do not have the proper incentives to be aggressive and innovative in developing shale gas. Shaanxi and Shanxi in China's coal belt of North China, for example, have already announced their own plans to develop shale gas in order to "gasify" their economy and move away from excess dependence on coal. Similarly, the coal- and oil-poor provinces of East and South China, the country's most advanced economically, are also moving boldly to partner with foreign companies to explore shale gas.

The Obama administration needs to ramp up its influence in the provinces and, more importantly, get the Chinese localities learning from American localities. The Department of Energy has thus far sponsored a few trips by local officials to visit with California energy and local governments, and this sort of local-to-local diplomacy needs to be increased—especially efforts to work with the local governments of America's major shale gas and shale oil producing states to introduce oil and gas policy at the local level to Chinese provincial energy officials, who are almost exclusively experts in power. In a related matter, Chinese localities would benefit greatly from talking with local environmental protection agencies and also civic groups and think tanks about shale gas and shale oil. If China is to develop this potentially transformative new set of fuels, its local governments will need help from the American local governments who know it best.

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*Steven W. Lewis, Ph.D., is the Baker Institute's C.V. Starr Transnational China Fellow and faculty adviser for the Jesse Jones Leadership Center Summer in D.C. Policy Research Internship Program. He is also a professor in the practice and an associate director of the Chao Center for Asian Studies, as well as an affiliated faculty member of the Department of Sociology at Rice University.*