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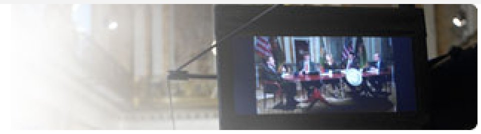

Remarks by Secretary Geithner at the Commonwealth Club of California

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As prepared for delivery

SAN FRANCISCO - It is a pleasure to be back at the Commonwealth Club, one of our nation's great forums for the discussion of public policy.

Three years ago, President Obama laid out a broad strategy for rebuilding the American economy.

He recognized then, as I am sure all of you do, that we live in a global economy, and this global economy will be a potential source of economic growth for the United States, but also a source of challenges.

The President recognized that to confront the global financial crisis, we had to work to support growth around the world, not just focus on putting out the financial fires in the United States. He recognized that American workers and American companies faced more intense competition, as other nations work to attract investment and factories, research and development facilities, and engineers and scientists.

And he recognized that to build a stronger foundation for growth in the United States, we could no longer borrow lavishly from the rest of the world to finance an economy driven by consumption and housing. Future growth would have to come more from investment and exports, and we would have to return to living within our means.

The President put in place a powerful and effective strategy for rescuing the American economy from the financial crisis. As a result of these policies and those of the Fed, the American economy went from falling at an annual rate of about 9 percent at the end of 2008, to positive growth in the summer of 2009. We helped pull the world economy back from the brink of a global depression. And the early years of recovery have been led by investment and exports.

In 2010 and 2011, as the engine of the American economy started to work again, we were hit by the European crisis, by Japan's disaster, and by higher oil prices. Economic growth slowed, and so did the pace of repair of the damage left over from the crisis. These were powerful reminders of the ways in which events beyond our borders can affect how fast we grow.

But parts of the world, and particularly emerging markets, have been a source of strength for the United States since the crisis. China has been a significant part of this growth. Overall, American exports have increased about 34 percent since 2009. American workers and American companies are becoming more competitive, productivity is up, supported by rapid increases in private investment, financed by a recovering financial system.

Next week, the Secretary of State and I travel to China for the fourth round of the U.S. – China Strategic and Economic Dialogue (S&ED). No other country presents China's particular mix of opportunities and challenges.

I want to talk about those opportunities and challenges, but I will start with a few fundamental propositions about our economic relationship with China.

First, the economic relationship between the United States and China provides significant benefits to both our nations. Even though we compete in many areas, our economic strengths are largely complementary.

Second, China faces a very complicated set of challenges as it transitions toward a more open, market oriented economy and financial system, facing rising costs, and slowing labor force and productivity growth.

Third, our priorities in our economic relationship with China – from its exchange rate to its treatment of intellectual property – reflect changes that are fundamentally in China's interest and essential for sustainable economic growth.

Fourth, and finally, the prosperity of Americans depends most importantly on the economic policies we pursue to strengthen American competitiveness. Even as we work to encourage further reforms in China, we need to understand that our strength as a nation will depend not on choices made by China's leaders, but on the choices we make here at home.

We have focused our economic policy toward China on achieving two broad strategic objectives:

The first is to expand opportunities for U.S. companies to export and sell to China, to level the competitive playing field, and to encourage economic reforms that would move China away from its export-oriented growth model and extensive subsidies for Chinese companies.

Our second objective is to deepen our cooperation with China on a range of international economic and financial issues, so that we are better able to work together on common global challenges, like the global financial crisis of 2008-09 and the ongoing European crisis. We want to build a stronger framework for economic cooperation that will allow us to balance the economic interests of what are – and will be for the foreseeable future – the two largest economies in the world.

We have made significant progress on these objectives over the past three years.

- Since early 2009, U.S. exports of goods to China have almost doubled, growing twice as fast as our exports to the rest of the world. In 2011 alone, the United States exported around $130 billion in goods and services to China, supporting well over 600,000 jobs here at home. Exports of goods from California exceeded $14 billion, supporting more than 65,000 jobs.
- China has committed to improving the protection and enforcement of U.S. intellectual property rights. To make sure that government agencies only use legitimate software, China has committed to increase budgetary resources for software purchases, to conduct audits and inspections, and to accelerate deadlines for provinces and municipal government to use only legal software. China also committed that technology transfer and technology co-operation is not a precondition for access to the Chinese market.
- When China's efforts to encourage indigenous innovation by limiting government purchases to an approved list of Chinese domestic products threatened to undermine market access for U.S. firms, President Obama successfully pressed to unwind China's indigenous innovation accreditation system.
- China has opened up new sectors to foreign firms, such as auto liability insurance and bond underwriting.
- China cut some tariffs earlier in the year, and China has launched a pilot program to reduce taxes on services, which we hope will be part of a larger reduction in taxes and tariffs which can make the price of consumer products in Shanghai twice as high as in San Francisco.
- China appears to be prepared to negotiate new rules on official export financing with the United States and other major exporters so that U.S. goods and services will be competing based on quality and price rather than the terms of foreign government financing.
- China's exchange rate has appreciated and is up about 13 percent against the U.S. dollar when accounting for differences in inflation since June 2010 and 40 percent since 2005. China also recently announced that it is widening the band to allow market forces to play a greater role in setting the exchange rate and is continuing to remove controls on capital flows in and out of China.
- China's trade surplus fell to less than 3 percent last year, compared to around 8 percent of China's GDP the year before President Obama entered office.

Despite this important progress, we have unfinished business and new challenges ahead.

Looking forward, in addition to our long-standing concerns with piracy of U.S. intellectual property, government procurement preferences, taxes and tariffs and other limitations on market access in some sectors, there are several Chinese reforms that are particularly important to the United States.

First, China's financial system is still dominated by large state-owned banks, who favor lending to large state enterprises, with comprehensive controls on deposit interest rates. This system limits the returns to savers to below the rate of inflation, forcing them to save excessively to achieve their financial goals and insure against life's risks. This both limits consumption and starves China's most innovative firms and sectors of capital, despite massive domestic savings.

Savers in search of higher yields and private firms in search of funds to grow their businesses gravitate to informal financing, with less prudential regulation and consumer protections. In a step in the right direction, China launched a pilot program last month in Wenzhou to allow new private lenders to lend to private enterprises.

To promote a more efficient financial sector and more efficient financial intermediation, interest rates will need to better reflect market forces. Raising the ceiling on deposit rates will also allow Chinese households to earn a higher return on their savings, both increasing their income and reducing their need to save, thus increasing their ability to consume goods and services, including from the United States.

These financial sector reforms are critical to China's continued growth – and that growth in turn represents tremendous opportunity for American companies and workers building and growing the things and offering the services the Chinese most seek. Financial reform in China will help reduce one of the main advantages China's state-owned enterprises have in competing with U.S. companies.

China's state-owned enterprises still compete with a range of unfair advantages in the Chinese and global markets. They have privileged access to cheap land, resources, and credit. They monopolize many of the most profitable sectors in China, including oil and telecommunications. But even where state-owned enterprises compete with private enterprises, their implicit backing by the Chinese government discourages private firms' entry and expansion.

Channeling resources into large state enterprises, while many of China's most dynamic private firms are starved for credit, ultimately hurts China's economy, and recent studies have highlighted how much more inefficient Chinese state enterprises are than their private counterparts. But it also hurts U.S. companies and workers who compete with these firms.

If China's state enterprises want to be treated like commercial enterprises by the rest of the world, they need to act more like commercial enterprises, including by paying market-based dividends to their shareholders and making their corporate governance and finances less opaque.

Finally, while we welcome the reforms to China's exchange rate system, the process of correcting the misalignment of the exchange rate remains incomplete, and the Chinese currency needs to appreciate further against the dollar and the other major currencies.

A stronger, more market-determined renminbi will help reinforce China's reform objectives of moving to higher value-added production, reforming the financial system, and encouraging domestic demand. It will provide China the independence and flexibility to respond to future changes in growth and inflation. And it will help the world economy, reducing a source of unfair competition with China's trading partners.

As we have worked to advance reforms in China, we have been forceful in protecting American companies from unfair competition.

- Since 2009, the Department of Commerce has issued a total of 36 antidumping and countervailing duty orders on unfairly traded imports from China.
- The President used the Section 421 safeguard remedy for the first time to protect U.S. jobs in the tire industry from a harmful surge in Chinese imports.
- We have successfully challenged China in the WTO, including most recently on China's export restraints on raw materials, limitations on the distribution of film and other media, and subsidies benefitting its domestic wind power sector.

The President recently announced the creation of the Interagency Trade Enforcement Center to aggressively challenge foreign unfair trade practices, including from China. We have been aggressive in protecting our interests and will continue to do so.

These are our main objectives and concerns with China. China, of course, wants certain things from the United States. China wants greater access to U.S. technologies and high-tech dual use exports. It wants to be able to invest more in the United States. It wants to continue to have access to our market and would like to be accorded the same terms of access as exports from countries we consider market economies.

We are willing to continue to make progress on these issues, but our ability to do so will depend in part on how much progress we see from China on issues that are important to us.

I want to conclude by emphasizing again that the solutions to our challenges in the United States rest first and foremost in the policies of Washington, not of Beijing.

Fundamentally, how many jobs and how much wealth we create will be the result of the choices we make in the United States – not the choices of others.

In our efforts to rebuild and put Americans back to work, we have to make sure we are making the investments and reforms that will be essential to our capacity to grow in the future.

As countries like China, India, Brazil, and other emerging economies grow and expand, we want to see a substantial part of that growing demand outside of the United States met by goods and services that are created and produced in the United States and fueled by investment in the United States.

If we are successful in doing that, we will be stronger as a nation. But to be successful in meeting that challenge, there are things we must do. Investments in education, to help Americans compete in the global economy. Investments in innovation, so that our economy can offer the best jobs possible. Investments in infrastructure, to reduce costs and increase productivity. And reforms to improve incentives for investing in the United States – including reform of our business tax system.

These investments and reforms have to come as part of a carefully designed, balanced package of long-term reforms to restore fiscal sustainability.

These are our economic challenges. And they are not just an economic imperative, they are a national security imperative. Our strength as a nation depends on the ability of our political system to move quickly enough to put in place solutions to our long-term problems.

Our great strengths as a country remain our openness to ideas and talent, our capacity to innovate, our excellence in higher education, a willingness to invest public resources strategically in scientific research and discovery, and the political will to confront challenges with wisdom and force.

China's rise offers us the opportunity of dramatic growth in demand for things Americans create and produce.

We should welcome both the opportunity and the challenge.

Thank you.

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