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With China slowing, talks with the U.S. take on a new tone

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At the peak of China's economic expansion, many in the United States worried about how the country's rapid growth would increase commodity prices, thin out U.S. manufacturing jobs and disrupt the balance of power in the global economy.

As officials from the two countries convene their latest high-level economic talks and a new government organizes itself in Beijing, the focus has shifted dramatically amid an economic slowdown that has made China seem suddenly more normal — growing at rates akin to other large developing nations rather than the superhuman pace that touched 14 percent just a few years ago.

That rate is now down to below 8 percent and by some accounts still falling; growth of U.S. exports to the country have all but stalled; and trouble in the country's financial sector rocked world markets a few weeks ago.

China reported trade data Wednesday that pointed to weaker growth in the second quarter. Exports fell 3.1 percent in June from a year earlier, the first decline since January 2012, while imports dropped 0.7 percent.

The seemingly unthinkable question is now being posed: Is China faltering?

"It is a different dynamic from what we have seen. . . . This is more-moderate growth from an economy that has started maturing from the go-go days of before," said John Frisbie, president of the U.S.-China Business Council. With the new government in Beijing still taking power and heading into a potentially pivotal party congress this fall, "the debate is real. . . . The slowdown matters."

The annual U.S.-China Strategic and Economic Dialogue begins Wednesday with Secretary of State John F. Kerry and Treasury Secretary Jack Lew leading the U.S. delegation, and China state counselor Yang Jiechi and vice premier Wang Yang heading the Chinese team. Top-level security, central bank and other officials will also be involved.

In an op-ed in The Washington Post ahead of the discussions, Yang pledged a "deepening" of China's reforms and said that the mood set by President Obama and President Xi Jinping in their "no-necktie" meetings last month would carry through to this week's talks.

The backdrop is predictably complicated, evidence of how central the U.S.-China relationship has become to world political, security and economic affairs. Along with perennial issues such as North Korea, human rights and China's policy of closely controlling the value of its currency, recent U.S. allegations about cyber-espionage and corporate hacking have become a central part of the discussion. American officials are pressuring China for a response while simultaneously trying to deflect the revelations of former NSA contractor Edward Snowden, who during his stopover in Hong Kong alleged that the United States does plenty of snooping on its own.

The issue has become such a core concern — potentially "destabilizing," in the words of U.S. Chamber of Commerce international economics head Myron Brilliant — that the two sides have set up a separate working group to help avoid sidetracking the rest of the discussion. New panels also have been established on climate change and energy security, issues of increasing urgency in China as it battles both a rapid run-up in energy demand and what have become dangerous pollution levels in major cities.

Those sorts of constraints are just part of a changing economic landscape that has pulled China back to earth. The country would need to double its current per-capita annual income of around $6,600 to be considered among the high-income countries, and if growth slows much more, it risks becoming caught in the "middle-income trap" — development that stalls as rising labor and other costs erode the advantages a country enjoys early in the development process.

Labor leaders, some members of Congress and other groups in the United States still worry about the loss of jobs to China and argue that the country's currency and other strategies to boost exports continue to give it an unfair advantage. Ebbing Chinese growth has meant a slower rise in U.S. exports to the country. Coming at a time when the U.S. economy seems to be firming and imports are on the rise, that produced a record trade deficit with China of $440 billion last year.

But investment by U.S. companies into China has slowed, while Chinese companies — looking for technology, growth and other opportunities that have become harder to find at home — are increasingly going overseas, sometimes with controversial results. The Senate Agriculture Committee is scheduled on Wednesday to hold a public hearing about the proposed takeover of Smithfield Foods, the world's largest pork producer, by a Chinese company trying to lock in supply for an increasingly meat-hungry nation and gain access to U.S. technology.

Changes in U.S. monetary policy and the potential for rising interest rates may divert even more capital from China, said Cornell University economist and China expert Eswar S. Prasad. The dropping cost structure for energy in the United States, meanwhile, coupled with the steady rise in China's labor bill, has the potential to further change international investment patterns. China, Prasad said, will likely press U.S. officials for a better understanding of those trends.

Overall, U.S. officials say they expect the economic pressures being felt inside China to push the country toward some of the decisions that the United States and other Chinese trading partners have long advocated: cutting subsidies to state-owned businesses, allowing freer movement of investment capital into and out of the country, and deregulating a financial sector dominated by state-owned banks and state-dictated interest rates.

There have been recent signs of change.

When banks ran short of cash a few weeks ago, the People's Bank of China held back any quick help, which many analysts read as a signal that the central bank wants market forces to play a bigger role in the financial industry. Last week, ahead of the talks with the United States, Chinese regulators said they were prepared to allow private banks to start playing a larger role in the economy.

As with many earlier pronouncements, U.S. officials say the pace of change will be key.

"From everything that we have been hearing both in private conversations and what we have seen in senior-level statements and in their own papers and communiques, there is a strong commitment to move forward," said a senior U.S. official. "How quickly they do it is still a question. It is critically important, and they recognize that."