

U.S.-China Economic Relations Under the Trump Administration at the 2-Year Mark

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Since entering office in 2017, President Trump has upended longstanding tenets of U.S. trade policy and launched the most aggressive set of new U.S. tariffs and trade restrictions since at least the Reagan administration in the 1980s. Actions include renegotiating the U.S.-Korea FTA (KORUS) and NAFTA, using “Section 232” of the Trade Expansion Act of 1962 to impose tariffs on most steel and aluminum imports into the U.S. in a bid to support U.S. smelters, using “Section 301” of the Trade Act of 1974 to impose tariffs on approximately half of U.S. imports from China, and threatening to use Section 232 to impose tariffs reportedly up to 25% on U.S. imports of automobiles.

The administration’s aggressive stance on trade has upended diplomatic relationships and prompted multinational companies to re-consider aspects of their global supply chains. It has also brought retaliation, including Chinese tariffs on most Chinese imports of U.S. goods. European countries and other U.S. allies affected by Trump’s steel and aluminum tariffs have also retaliated with tariffs of their own against imports of U.S. goods, with many of the retaliatory tariffs targeting perceived politically important constituencies in the U.S., such as U.S. whisky distillers, who are heavily concentrated in the home state of Republican Senate Majority Leader Mitch McConnell.

But Trump’s aggressive trade policies also began to deliver some successes in 2018, including a successful renegotiation of NAFTA, now renamed the U.S.-Mexico-Canada Trade Agreement (USMCA), a renegotiated Korea-U.S. FTA, and at least some willingness by European and Japanese officials to discuss greater market access for U.S. products. While many major U.S. importers and trade associations have complained about the tariffs, the tariffs continue to draw support from several of the key constituency groups that they are intended to assist, such as the U.S. steel industry.¹

While U.S. tariffs against imports from allies are seemingly driven largely by the Trump administration’s general protectionist bent, Trump’s trade actions against China reflect a broader set of concerns that is more widely supported by members of the United States congress and American experts outside of government. These include both longstanding U.S. concerns over Chinese trade practices and market access barriers, and growing U.S. geopolitical competition with China—what the Trump administration’s National Security Strategy, released in December 2017, refers to as the return of “great power competition.” These geopolitical concerns have been central to the administration’s recent aggressive efforts to block the deployment of Huawei telecommunications technologies in new “5G” mobile communications networks around the world, and in the administration’s increasingly vociferous opposition to China’s “Belt and Road Initiative” (BRI). And because of increased U.S.-China geopolitical competition, U.S. use of targeted trade controls, investment restrictions, potential targeted sanctions, and other measures against China, will likely continue even if, as is widely expected, Trump and President Xi reach a broad agreement on many trade issues in the coming months and reduce some of the tariffs that are currently in place.

Deploying New Tools

Over the course of late 2017 and 2018, the Trump administration has deployed a growing array of trade and economic tools to pressure China over unfair trade practices and perceived national security threats. The highest profile of these has been the Trump administration's Section 301 investigation against China, which the Trump administration announced in August 2017 and which in March 2018 concluded that China engages in a range of unfair trade practices. Pursuant to the 301 Action, the Trump administration has imposed tariffs of 25% on imports of Chinese goods valued at approximately \$50 billion per year, with most of the goods subject to these tariffs linked to economic sectors that China has prioritized under its "Made in China 2025" national industrial development plan. In September 2018 the administration began imposing a 10% tariff on imports of Chinese goods valued at approximately \$200 billion annually. The Trump administration initially expressed an intent to raise the 10% tariffs to 25% in early 2019, but has indefinitely postponed the increase while Washington and Beijing continue their ongoing trade negotiations. The administration has also reportedly prepared plans to impose tariffs on substantially all remaining U.S. imports of Chinese goods, worth an additional approximately \$250 billion annually, but those plans are also on hold pending the outcome of the trade negotiations.

But while the tariffs have attracted the bulk of the headlines regarding the U.S.-China trade war, Washington has also begun to deploy a parallel and complementary set of targeted tools to pressure China over specific perceived abuses. The first of the tools is a significant ramp-up in scrutiny of Chinese investment in the U.S. under the Committee on Foreign Investment in the U.S. (CFIUS), a Treasury Department-led process to screen certain foreign investments in the U.S. for national security concerns. CFIUS began to apply heightened scrutiny to Chinese investments in the U.S. towards the end of the Obama administration, and in 2017 and 2018 the Trump administration used CFIUS to block Chinese firms from acquiring American semiconductor firm Lattice Semiconductor² and Xcerra Corp, a semiconductor testing company.³ The Trump administration also used CFIUS to block Singapore-domiciled chipmaker Broadcom from acquiring Qualcomm, one of the largest U.S. chip manufacturers, on the grounds that the acquisition could undercut Qualcomm's R&D and ultimately America's technological edge over Chinese rival companies such as Huawei.⁴ Other proposed acquisitions have been withdrawn or avoided due to concern that they would not clear CFIUS. While CFIUS has not published details on its total caseload in several years, this tightened CFIUS scrutiny has almost certainly been a contributing factor to a sharp decline in Chinese direct investment in the U.S. that has occurred since a peak in 2016.

The second targeted tool is the Commerce Department's "Entity List," a list that prohibits U.S. companies from exporting most goods to designated companies. Starting in 2015, the Obama administration began to use the Entity List to restrict the export of certain high-end U.S. chips to certain military-linked computer centers in China.⁵ This list attracted

widespread attention in April 2018 when the Commerce Department used it to prohibit U.S. exports to Chinese telecommunications company ZTE after ZTE violated the terms of an earlier settlement agreement over Iran sanctions violations. Given ZTE's reliance on U.S. chips and other technologies, the Commerce action essentially forced ZTE to suspend major business operations until it reached a new settlement with Commerce and was taken off the list in July of last year. In October 2018 the Commerce Department put a Chinese chipmaker accused of stealing U.S. trade secrets, Fujian Jinhua Integrated Circuit Company, on the Entity List.⁶ There are also reports that the Commerce Department has used a different export tool to prevent Huawei's own U.S. R&D division from exporting certain high-end technologies to its parent company in China.⁷

CFIUS and export controls will likely play a substantially larger role in U.S.-China trade and investment relations over the next several years. In August 2018, Congress enacted two new statutes: the Foreign Investment Risk Review Act of 2018 (FIRRMA), and the Export Control Reform Act of 2018 (ECRA). These acts substantially expand both CFIUS and export controls: FIRRMA expands CFIUS to cover minority foreign investments in certain sensitive and high tech sectors, and ECRA has directed the Commerce Department to develop new export controls on "emerging technologies" and "foundational technologies" that will likely include a variety of technologies that will be increasingly important across business, industrial, military, and consumer applications, including artificial intelligence, advanced robotics, and autonomous vehicles.

The Department of Justice and the FBI, meanwhile, have significantly expanded efforts to prosecute Chinese individuals and companies that engage in economic espionage, cyber attacks, and other actions that violate U.S. law. Over the past several years U.S. prosecutors have indicted multiple China-linked individuals and entities for IP theft, including Huawei, members of the PLA, and various other individuals involved in IP theft. In November 2018, the Justice Department formalized its expanding efforts to investigate and prosecute Chinese IP theft by announcing a new initiative to combat Chinese economic espionage.⁸

Finally, the Trump administration has begun restricting visas for Chinese students to study in certain sensitive fields in the U.S., although overall Chinese enrollment in U.S. universities actually rose modestly in 2018.⁹ Newspaper stories have indicated that the Trump administration has considered drastic reductions of visas for Chinese students, though it has not acted on the plans.¹⁰ While the shift in visa policies is partly related to the administration's general crackdown on immigration into the United States, it also reflects concern about Chinese students gaining access to U.S. technical and technological expertise and then returning to China to commercialize and/or militarize it.

Beijing's Response

To date, China has generally adopted a policy of reciprocating against U.S. actions but has generally avoided trade and commercial steps that would escalate tensions with Washington. For example, China reciprocated against U.S. tariffs on Chinese goods by imposing tariffs of its own on Chinese imports of U.S. goods, and China now imposes retaliatory tariffs on a large majority of all U.S. goods exported to China.¹¹ But China imposed these retaliatory tariffs at a pace that tracked the U.S. tariff escalation, and the tranches of Chinese tariffs were proportionate to the U.S. tariffs. China also blocked Qualcomm's proposed \$44 billion

merger of European semiconductor firm NXP,¹² but has allowed other major mergers, such as Disney's purchase of Fox, to proceed.¹³ Despite periodic press reports that individual American companies have suffered mysterious licensing and customs delays that may be informal Chinese retaliation for U.S. trade pressure, China does not appear to be mounting a systematic, widespread campaign of informal measures to adversely impact U.S. business interests. And while China has taken the highly provocative step against Canada of arresting several Canadian citizens in response to Canada's arrest of Huawei CFO Meng Wanzhou, an action Canada took at the request of the U.S. after the U.S. indicted Meng over alleged violations of U.S. sanctions, China does not appear to have engaged in similar retaliatory arrests of American citizens.

The measured nature of China's response is also evident in China's willingness to negotiate a potential trade agreement with the Trump administration and the steps that Beijing has already begun to take, and has indicated that it is potentially prepared to take, in order to reach a *détente* with Trump. For example, China has indicated a willingness to commit to purchasing hundreds of billions of dollars in additional U.S. products, such as energy, agricultural products, and technology. More systemically, China has recently rushed to enact a new law that China says will provide additional market access and reduce "forced technology transfer" requirements, both longstanding U.S. complaints.¹⁴ China has also reportedly been willing to negotiate at least limited restrictions on currency manipulation,¹⁵ has begun to publicly downplay its "Made in China 2025" industrial development policy,¹⁶ and has signaled that it is prepared to provide greater market access to U.S. and western firms.¹⁷ Many U.S. China experts—not to mention many Trump administration officials—have expressed a healthy skepticism about whether China will actually follow-through on commitments: China, for example, has previously committed to various forms of market access for U.S. firms in several industries, such as credit cards, but has failed to deliver on its commitments. Nonetheless, China's apparent willingness to agree to commitments in a comprehensive fashion and to at least take some steps towards implementation illustrates China's interest in de-escalating, rather than escalating the dispute and in seeking some reductions in the U.S. tariffs. China has also responded to the trade war by increasing incentives for companies to keep doing business in China and for companies affected by Trump's tariffs: for example, in late 2018 China announced that it would increase export tax rebates to "help reduce costs for the real economy, help it cope with the complex international situation and maintain stable foreign trade growth."¹⁸

Impacts

The Trump administration's aggressive deployment of trade tools against China and Beijing's retaliation has had undeniable commercial and economic impacts.

As was widely reported in March 2019, Chinese goods exports to the U.S. actually rose by approximately \$34 billion in 2018 to a total of \$539.5 billion. U.S. goods exports to China fell by \$9.6 billion to \$120 billion and the overall U.S.-China trade gap in goods rose to \$419 billion.¹⁹ (The trade gap was somewhat narrower if services are included). But despite some news headlines suggesting that surging U.S. imports from China marked a failure of Trump's trade war, Trump's trade war may have actually provided a temporary, short-term boost to Chinese exports to the U.S. as companies raced to send goods to the U.S. in advance of tariffs coming into effect. For example, early data from the first two months of 2019 show

a likely sharp decline in the trade deficit between the U.S. and China.²⁰ (The increase in U.S. imports in 2018 was also driven by factors unrelated to the trade war, such as the growing U.S. economy and the consumer spending stimulus impacts of the Trump administration's tax cuts enacted in late 2017).

Impacts on direct Chinese investment in the U.S. have been even sharper. The Rhodium Group consultancy estimates that Chinese FDI flows (greenfield investments and acquisitions) into the U.S. fell from a peak of \$46 billion in 2016 to \$5 billion in 2018 though CFIUS reviews are only one factor in the decline in Chinese FDI in the U.S. and Chinese venture capital flows (e.g. minority investments in U.S. firms, which have a smaller overall headline figure) into the U.S. appear to have hit a record last year.²¹ (Given that FIRRMA implementation did not occur until late 2018, most of Chinese venture capital investments in the U.S. in 2018 would not have been affected by FIRRMA, but investments in 2019 will be). According to Chinese statistics, however, U.S. direct investment in China actually rose modestly during the first 10 months of 2018, though the rise in U.S. investment was significantly slower than the increases in FDI in China by other countries.²²

While geopolitical tensions and the U.S. expansion of CFIUS review under FIRRMA are likely to keep Chinese FDI in the U.S. at subdued levels in 2019, U.S. investment in China is likely to increase this year as a result of both apparent Chinese decisions to ease restrictions on U.S. FDI investment in China and a decision by major stock market fund index provider MSCI to quadruple the weighting of Chinese equities in important global indices, meaning that billions of dollars of index-fund linked investment will likely flow into China.²³

Anecdotal evidence indicates that a number of multinational companies, including Chinese companies, have responded to the Trump administration's tariffs by taking steps to begin diversifying their manufacturing supply chains away from China and to other countries in Asia, such as Vietnam and India. While migration of manufacturing supply chains, particularly for lower-value products, had already been occurring over the past several years in response to rising Chinese costs, press reports indicate that the tariffs are likely speeding the shift.

Enlisting Allies?

Prior to mid-2018, the Trump administration's diplomatic efforts to build a global coalition against China's abuses were limited. Indeed, the Trump administration's decision in March 2018 to impose tariffs on steel and aluminum imports globally, including traditionally close U.S. allies such as Canada, Japan, and European countries, alienated foreign governments and at least temporarily limited governments' interest and willingness to join a U.S.-led coalition against China.

Over the last nine months, however, the Trump administration has renewed U.S. diplomatic efforts to enlist allies in a multinational campaign against Beijing. The U.S. Trade Representative (USTR), Robert Lighthizer, has established working groups with Japan and with the European Union to develop a collective approach to addressing Chinese trade practices and investment. The U.S. has also encouraged countries to join the U.S. in using the World Trade Organization (WTO) to press China to end various unfair trade practices, and in March 2018 the Trump administration filed a WTO case challenging China's protection of intellectual property.²⁴

More prominently, U.S. Secretary of State Michael Pompeo and other senior Trump officials have launched high-profile campaigns to dissuade third countries from two specific kinds of business with China: 1) purchasing Chinese telecommunication equipment, notably Huawei equipment for use in next-generation “5G” mobile communications networks, and 2) dissuading countries from participating in China’s Belt and Road Initiative (BRI).

Throughout 2018, the Trump administration aggressively pushed countries to reject Huawei equipment in 5G networks, arguing that Huawei equipment poses a security threat, and deploying high level delegations to foreign capitals and to major mobile telecommunications conferences to press the case. The Trump administration has also threatened more aggressive measures against countries that allow Huawei equipment in 5G networks, for example stating publicly that Germany would face a downgrade in U.S. intelligence sharing if Germany allows Huawei equipment to be used in German 5G networks. The U.S. has also taken legal action against Huawei itself, indicting the company under U.S. law both for violations of U.S. sanctions on Iran and for stealing U.S. trade secrets. The Trump administration has fought the BRI primarily by highlighting concerns over countries falling into a Chinese “debt-trap” and by discouraging allied nations from participating in the BRI.

The European Union, Japan, and other countries are either currently implementing or are seriously discussing enhanced screening of Chinese investment. The European Union filed a WTO case against China’s technology transfer practices in June 2018.²⁵ More broadly, the European Union does appear to be shifting towards a more hawkish overall posture against Chinese trade issues, driven by both growing internal EU concern about Beijing’s actions and the Trump administration’s diplomacy. A European Commission white paper on China released in March 2019, for example, labelled China a “systemic rival” and urged the European Union to adopt a relatively tough set of trade remedies if China failed to make significant concessions by the end of 2020.²⁶

That said, in the broadest, strategic sense, most U.S. allies appear to be seeking to walk a line between Washington and Beijing without siding definitively with either side. For example, while Australia and New Zealand announced in early 2019 that they would ban the use of Huawei equipment in the core of 5G networks, other U.S. allies, including Germany and the United Kingdom, appear to be preparing to allow the use of Huawei equipment, though subject to heightened security requirements and perhaps not in all parts of 5G networks.²⁷ China has convinced more than 60 countries, including a number of smaller European countries, to endorse the BRI, and in March 2019 appeared poised to convince Italy to endorse the BRI, which would mark the first time a G7 country made such an endorsement.²⁸

The Path Forward

Over the past several months, both Washington and Beijing have broadly suggested that they may be nearing an agreement to resolve some of the elements of their trade war. The outlines of such a deal appear to involve a commitment by Beijing to substantially increase its purchases of U.S. goods, to end (or at least curb) its longstanding practices of requiring tech transfer as a condition of allowing investment, to open additional sectors of its economy to foreign investment, and to strengthen intellectual property protections and to reduce IP theft. Additionally there also appear to be commitments of some type

on currency manipulation issues and subsidies. In exchange, the Trump administration would agree to refrain from escalating U.S. tariffs on China and, likely over the mid- to long-term, to reduce existing tariffs. There is also speculation that the deal could involve other U.S. concessions, such as dropping the abovementioned U.S. request to extradite Meng Wanzhou, Huawei's CFO, from Canada to the U.S. to face charges related to alleged Iran sanctions violations.

However, even if Washington and Beijing do reach such a deal, the Trump administration is likely to continue deploying many of the targeted tools discussed above to address specific Chinese abuses. For example, implementation of FIRRMA (to strengthen CFIUS review) and ECRA (to expand U.S. export controls) is proceeding in Washington and does not appear likely to be substantially affected by the outcome of the trade negotiations. Similarly, the Trump administration is likely to continue deploying targeted measures against specific Chinese companies involved in IP theft and other wrongdoing even if a deal is reached.

In addition, a potential trade deal does not appear likely to reduce the significant tension regarding the use of Huawei equipment in 5G networks, which is driven in large part by counter-espionage and national security concerns, and not simply by trade concerns. Similarly, Trump administration national security officials appear unlikely to curb their counter-BRI diplomacy even if Trump's trade officials secure a trade deal with Beijing.

Questions for the Longer Term?

Having evaluated the Trump administration's current approach towards China and likely developments over the next two years, let's look to the future. Several major questions hang over the next several years of U.S.-China economic relations.

The first of these is whether the Trump administration will pursue a strategy of a broader "decoupling" of the U.S.-China economic relationship. A number of foreign policy experts in Washington have called for an economic decoupling, or, in more extreme cases, an economic "divorce," and some Trump administration officials are broadly sympathetic towards policies that would structurally reduce U.S.-China economic ties over the mid- and longer-term. These experts and officials would like to see reduced U.S.-China economic ties over time even if Trump and Xi reach a trade deal.

Other foreign policy experts, and other Trump administration officials, instead seek to use the leverage the U.S. has generated over the past two years to press China for major structural reforms, which is a large part of the potential deal under discussion in the current U.S.-China trade negotiations. For these experts and officials, if China actually agrees to such reforms and a trade deal is reached, there will be a continuation of a deep U.S.-China economic relationship—though as discussed above, ongoing specific points of friction, such as communications technologies, are likely to continue regardless of any agreement.

As an analytic matter, the Trump administration is likely to answer the question of whether it is pursuing a strategy of "decoupling" within the next several months, because in practice the answer will largely depend on whether the Trump administration reaches a trade deal with China. If the Trump administration reaches and implements a deal, then, practically

speaking decoupling is unlikely to occur over the next several years because increased Chinese purchases of U.S. products and greater Chinese openness to new U.S. business investment in China should actually deepen economic ties between the two countries.

If, however, Washington and Beijing do not reach a deal, a broader economic decoupling becomes substantially more likely. A long-term continuation of the existing U.S. tariffs with no apparent end date and, in a “no deal” scenario, the potential for further escalation in both tariff rates and in the products that the tariffs apply to will prompt multinational companies to further expedite efforts to diversify supply chains away from China. Meanwhile, continued retaliatory Chinese tariffs will prompt U.S. producers, particularly of agricultural commodities and energy, to continue developing markets in countries other than China given that China’s retaliatory tariffs make U.S. commodity products relatively uncompetitive in China.

The second major question is whether, and the extent to which, the U.S. will use traditional market-liberalizing agreements as a part of its economic strategy towards both China and East Asia, and the extent to which the Trump administration will use other “carrots” as part of its economic strategy in Asia.

Under the Trump administration U.S. trade and international economic policy has taken on a “stick forward” approach, with liberal doses of tariffs, sanctions, ramped up investment reviews, and new export controls. Even trade deals, which have long been seen as a liberalizing tool that offers America’s allies increased market access to the U.S., have taken on a much tougher, “America First” slant, with the renegotiations of NAFTA and KORUS focused heavily on increasing U.S. market access rather than offering more access to the U.S. market.

That said, in recent months, the Trump administration has expressed a limited degree of support for more traditional economic carrots. For example, the administration has said that it will seek to negotiate a trade agreement with Japan, though it remains unclear how serious the administration is in pursuing such agreements and whether the administration would be willing to make concessions on U.S. market access that would make such a deal attractive. Still, it is not impossible that the Trump administration will eventually deploy at least bilateral trade agreements in Asia as part of an evolving strategy to contain and compete with Beijing. 2018 also saw an important development with respect to U.S. development financing, which will have important impacts on the U.S. economic posture towards developing countries in Asia and around the world. Congress passed, and the Trump administration signed, the BUILD Act, which merged the U.S. Overseas Private Investment Corporation (OPIC) and the development finance programs of USAID into a new U.S. Development Finance Corporation and doubled the overall funding cap. This has the potential to significantly expand U.S. development finance in key developing economies and may simultaneously help advance U.S. trade and commercial ties between Washington and smaller developing economies.

The third major question hanging over Washington’s trade relationship with China is how American allies will manage their strategic and economic relationships with both Washington and Beijing. As discussed earlier, most U.S. allies appear to be trying to walk a middle path between the U.S. and China, and do not want to be forced to pick sides in an

increasingly tense geopolitical standoff. They generally have no interest in being drawn into competing economic and political blocks. But in a scenario of future escalation between Washington and Beijing, and particularly if the U.S. and China do not reach a trade deal, allies will likely be increasingly pressed to pick sides.

The final major question hanging over the U.S.-China economic relationship is what happens after the American presidential election in 2020. Chinese President Xi seems secure in power for the foreseeable future. But the U.S. presidential election is already gearing up and the U.S. may have a transition of government in less than two years.

If Trump wins, it seems safe to expect that the United States will see a continuation of the strategy that has emerged over the past two years, and the U.S. and China will likely have a broadly confrontational relationship even if Trump and Xi do reach a trade deal.

Rather more uncertainty, however, hangs over the policies of a potential Democratic president. Without a doubt, a Democratic president will take a more hawkish line towards China than did President Obama, particularly with respect to China's economic policies. Many Democratic politicians have long been somewhat skeptical of trade policy and have advocated for hawkish moves against China: Senate Minority Leader Chuck Schumer, for example, welcomed Trump's tariffs against China last year.²⁹ Democratic candidates such as Elizabeth Warren and Bernie Sanders are long-time critics of trade deals and would take at least as strong a stand against Chinese trade practices as has Trump. Democrats are also growing concerned about China's assertive foreign policy both in East Asia and globally, and Democratic politicians increasingly express support for aggressively challenging Beijing. As Senator Bob Menendez, the top Democrat on the Senate Foreign Relations Committee, said in March 2018, "I agree with President Trump when it comes to recognizing the scope of the challenge that China presents to the United States and to the entire international order."³⁰ (Menendez also made clear that he strongly disagreed with elements of Trump's strategy to address the challenges that China poses for the United States). Democrats have historically expressed greater concern about foreign repression and human rights abuses than the Trump administration does, and a Democratic president might take a somewhat stronger stand against China's domestic repression than the Trump administration has, though given the myriad issues in U.S.-China relations, China's domestic repression would not likely be a first-tier issue even under a Democratic president.

That said, while a Democratic president would not be likely to take a materially softer line towards Beijing on trade issues, at a strategic level a Democratic president would likely have several reasons to reduce tensions with Beijing. For example, several Democratic candidates, including Warren and Sanders, have articulated support for cutting U.S. defense spending and for increasing spending on domestic priorities. Significant defense cuts, if implemented, would likely push Washington towards a policy of reducing military tensions in East Asia, even if the bulk of the cuts would come from U.S. military operations in the Middle East.

A Democratic president would also likely seek cooperation with Beijing on climate change issues. A ton of greenhouse gas emitted in Guangzhou has the same impact on global climate change as a ton of greenhouse gas emitted in Ohio, and China has already overtaken the U.S. as the world's largest greenhouse gas emitter. A Democrat serious

about combatting climate change—and Democrats increasingly see climate change as the single greatest mid- and long-term threat that the U.S. faces—will find that they need to cooperate with Beijing, creating a strong incentive for a Democratic president to manage strategic tensions with China.

Finally, Democrats are also likely to reverse a number of Trump’s immigration policies, given the Democratic Party’s growing support for immigration into the U.S. and longstanding ties to major educational institutions, which generally welcome foreign students.

How to Conceptualize the U.S.-China Economic Relationship

I would like to offer a concluding thought on how to conceptualize the U.S.-China economic relationship in what I see as a baseline scenario in which the U.S. and China reach a trade agreement but continue to have sharp differences over specific policies and industries, such as telecommunications. In this scenario, the economic relationship is characterized by neither broad economic and political cooperation and engagement, nor by a broad decoupling of the world’s two largest economies. Instead, the relationship will be characterized by what I term “strategic coupling,” a more transactional approach to economic relations in which the U.S. and China are economically coupled across many industries, but increasingly decoupled in a handful of key industries that each side sees as too sensitive for deep interconnectedness.

Some elements of a “strategically coupled” relationship may flow only one way, not both. For example, I expect that the U.S. will broadly continue to allow U.S. companies to sell computer chips to China, with some exceptions for extremely high-end chips, but that the U.S. may increasingly restrict China’s sale of computer chips to the U.S. out of national security concerns, much as the U.S. already restricts the sale of certain Chinese telecommunications equipment in the U.S. The U.S. may similarly push to use CFIUS to restrict Chinese investment in certain high-tech sectors in the U.S. even while pushing China to allow greater U.S. investment in China’s high-tech sector.

More broadly, a U.S.-China economic relationship based on “strategic coupling” is likely to put a greater emphasis on assessing end-users, including end-uses in China. Assuming the U.S. and China do reach a trade deal, U.S. companies may find themselves more able to do business in China (as China opens its market), but, at least with respect to certain high-tech business, only with customers and end users who are several steps removed from the Chinese government, or at least the Chinese defense establishment.

A world of U.S.-China “strategic coupling” will present challenges for the U.S., for allies, and for the private sector as governments and companies navigate specific sectors where there is pressure for decoupling, and specific sectors where cooperation continues and even deepens. It is a world that is likely to evolve over time, with specific parameters subject to change. The next several years in U.S.-China economic relations are likely to provide as much fodder for discussion and debate as the last two years have already provided.

Endnotes

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