PISM POLSKI INSTYTUT SPRAW MIĘDZYNARODOWYCH
THE POLISH INSTITUTE OF INTERNATIONAL AFFAIRS

BULLETIN

No. 71 (1142), 18 May 2018 © PISM

Editors: Sławomir Dębski • Bartosz Wiśniewski • Rafał Tarnogórski

Karolina Borońska-Hryniewiecka • Anna Maria Dyner • Aleksandra Gawlikowska-Fyk
Sebastian Płóciennik • Patrycja Sasnal • Justyna Szczudlik • Marcin Terlikowski • Tomasz Żornaczuk

China's Policy towards the U.S.: An Attempt to Defend Economic Interests

Marcin Przychodniak

U.S. President Donald Trump's declarations on applying tariffs on goods from China confirmed current negative evaluations by Chinese authorities of U.S. policy under his administration. The U.S. is an important market, but first and foremost a source of much-needed technology for Chinese leader Xi Jinping's economic modernisation plans. That is why China will not excessively escalate the current trade dispute but it will try to gain EU cooperation to oppose U.S. trade policy.

The Trump administration's changes in U.S. policy towards China—recognition of it as a threat in the National Security Strategy[1], blocking certain Chinese investments, and tightening tariff policy—is a danger to China's plans to modernise its economy. The authorities in Beijing are trying to calm relations with the U.S. Just how important the normalisation of relations with the U.S. is for China was demonstrated in March by the majority of nominations of political posts related to foreign policy (including Vice Chairman Wang Qishan) going to those who have had experience negotiating with the U.S. The Chinese offer to increase imports, made by Vice Premier Liu He during his visit to Washington in February, also aimed at stabilisation of relations. However, the visit by a U.S. delegation headed by the secretary of the U.S. Treasury in May to Beijing failed to achieve serious progress. Liu He returned to Washington this month (15–19 May).

Competition for Technology. For China, the U.S. is primarily a source of modern technology and human capital in the IT sector. China-based enterprises Alibaba, Huawei, Tencent and others invest in American startups and gain information from Chinese working in American research facilities. This is how China is trying to ensure the success of its economic reforms—"Made in China 2025" programme—through digital solutions. AI development, big data, and the internet sector in general are other areas China is working on to try to overtake the U.S. as the global technology leader.[2] The U.S. demands China reduce its subsidies to the digital sector, blocks certain Chinese investment, and plans to limit research by Chinese in American universities, currently being considered by the administration, makes the accomplishment of China's plans more difficult. These restrictions apply to the microchip market, for example, where China is the biggest consumer (over 60%) and most chips (90%) are imported from abroad. Recently, Chinese telecommunications company ZTE was charged with violating U.S. sanctions by cooperating with Iran and was punished by the American authorities with a fine of $890 million and a seven-year ban on importing microchips. Chinese investment in the U.S.'s modern technology sector increasingly is being suspended (although in 2017 it still amounted to $10 billion). Especially interesting was an attempt to take over of

[1] M. A. Piotrowski, B. Wiśniewski, "The U.S. National Security Strategy: The Trump Administration's Approach," *PISM Bulletin*, no. 128 (1068), 21 December 2017.

[2] M. Przychodniak, "Digitalisation in China: Transformation of the Economy and Social Engineering," *PISM Bulletin*, no. 43 (1114), 15 March 2018.

American company Qualcomm, a deal blocked by the administration. The U.S. took the action to stop the buyout because of concerns the new owner from Singapore would have limited investment in 5G technology in favour of China's Huawei. The U.S. Congress is working on a bill to allow the administration to block not just takeovers but any investment in key technology or the critical security sector in the U.S.

Crisis Management by China. The U.S. also considers its high trade deficit with China to be a problem in their relations. That is why President Trump has been threatening a trade war, including the high tariffs on Chinese goods. The Chinese authorities are indeed not interested in an escalation of the dispute but are trying to pressure the Trump administration to change its policy. In April this year, China decided to impose tariffs on some agriculture products in response to U.S. restrictions on steel and aluminium imports. The tariffs seemed particularly aimed at producer states considered part of Trump's political base, e.g., Missouri, Indiana, and North Dakota. Pressure on the administration also comes from China's threats to broaden the catalogue of tariffs. Other countermeasures China is considering include restrictions on people with dual, Chinese-American citizenship from leaving the country. The authorities already hinder the activities of American companies already present on the Chinese market, for example, by expanding customs inspections on cars from the U.S. or putting American food exports to China under stricter phytosanitary controls.

Aside from the restrictions, the Chinese authorities also are signalling a willingness to compromise by declaring the possibility of increasing U.S. imports (e.g., energy resources) or opening its market to more American companies. During his speech in April at the Boao Forum for Asia, Xi announced he would lift some restrictions, such as those on the automotive sector. From 2020 for electrics and from 2022 for others, foreign carmakers will be able to operate independently in China without establishing a joint venture with Chinese partners.

EU Context. China is looking towards the EU, which is also subject to American trade limitations. It is afraid that possible restrictions from the EU on Chinese investment will additionally weaken the Chinese economy. Despite a block on foreign companies in many sectors of the Chinese market, China uses the rhetoric of free trade and defence of globalisation to persuade the EU to cooperate with it. Therefore, China has drafted tariffs that target, for example, U.S.-based Boeing but not European Airbus. China's vice minister of commerce tried during recent conversations with Germany, Italy, France, Spain, the UK and EU ambassadors in Beijing in April this year to persuade them to take a common stance towards the U.S., though without success then. In the context of the rivalry with the U.S., China reiterated its interest in possible investment projects within the Three Seas Initiative (TSI) in the final declaration of the "16+1" summit in Budapest in November 2017. China's attention was also focused on President Trump's presence at the TSI summit in Warsaw in July 2017.

Conclusions. The Chinese authorities are facing a serious challenge to stabilising economic relations with the U.S. On one hand, because of the difference in potential and the need to import technology, it is not ready for a more open or deeper confrontation with the U.S. On the other hand, Xi's need to defend Chinese interests makes it impossible for China to agree to the American demands presented by the Treasury secretary in Beijing in May. The U.S. not only expects China to increase imports of U.S. goods by at least $200 million by 2020 but also to limit subsidies under the "Made in China 2025" programme, end mandatory technology transfers on foreign companies operating in China, and cease cyberattacks to acquire intellectual property from the U.S.

Changes to China's investment and trade policy because of the U.S. pressure, such as opening its market further and decreasing subsidies, are also in the EU's interest. In the short term, it is not very probable. Changes also should not be expected even if there is China–EU cooperation connected to the Chinese slogans of a defence of "globalisation" and "free trade." This is because China mostly counts on cooperation with the EU against the U.S. and the slogans the Chinese have used so far show they are mostly designed to secure their own interests. But it is also not in the EU interest to support Trump's protectionist trade policy. So, the EU should still pressure China on the European Commission level towards an investment control mechanism, underlining the need for more openness and reciprocity and solve all the disputes over the World Trade Organisation mechanism. In this context, Poland`s support for EU institutions' policy will be an important sign of European solidarity. It may also increase the possibilities for Polish companies seeking to operate on the Chinese market.