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Trade dispute enters second half

From here on, the rivalry between the two largest economies will become a contest with a global dimension

By CHENG SHI

China and the United States reached a consensus to suspend tariff hikes and restart trade talks at the meeting between President Xi Jinping and his US counterpart Donald Trump in Argentina on Dec 1.

Yet the Canadian police detained Meng Wanzhou, Huawei's global chief financial officer, and could deport her to the US where she could face charges for evading US curbs on trade with Iran.

These contrasting signals show the complexity of the China-US trade conflict and, since the conflict has reached a critical stage, four major changes can be expected.

First, the trade conflict between the two largest economies has shifted from being a blitz to a stalemate. The first half of the game, which stretched from March to November, can be seen as a fight for time and space.

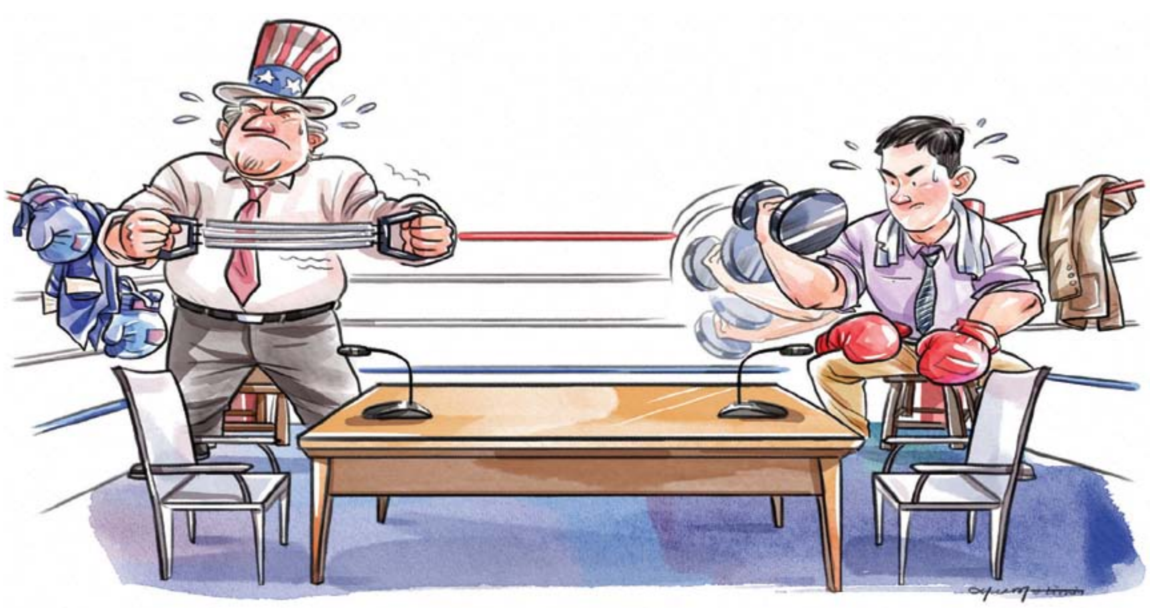
Taking advantage of the time window provided by tax cuts at home and China's reform pains and shrinking room for stimulus, the Trump administration adopted a "maximum pressure" strategy. The first three rounds of trade sanctions were thus carried out one after another in quick succession, each one more aggressive than the last, with the aim of bringing China to heel.

Yet the landscape of the contest has now changed in two aspects.

To begin with, the Trump administration's strategy is taking a bite out of the US economy, made clear by volatility in the stock market, the International Monetary Fund's (IMF) downgrading of its US growth forecast by a large margin, as well as the mass layoff plans of leading automobile enterprises.

Also, both the Republicans and the Democrats have arrived at the consensus that the US should seek to contain China's rise and safeguard US supremacy. Threats posed by the Trump administration's previous strategic arrangements targeted at China, including the Indo-Pacific Strategy, US-Mexico-Canada Agreement and the announcement it will seek trade agreements with Britain, Japan and the European Union, will be around for a long time.

In these circumstances, the two countries have bidden farewell to the illusion of a quick victory after the G20 summit and confronted the reality of a long-term stalemate as the short-term pressure starts to moderate.



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Second, the tariff strikes on each other in the second half of their contest will be more targeted and accurate compared with the relatively comprehensive attacks before. Historically, the disparity in strength with its opponents and the convergence of interests has determined what kind of approach the US adopts in such contests.

When it had a huge economic advantage and weak bonds of shared interests, it used the extreme solution of economic blockade and comprehensive Cold War against the Soviet Union.

In the 1980s, its approach against Japan was less extreme, as the US' economic advantage was significantly less compared with the economic advantage it enjoyed over the Soviet Union, and the two countries had more shared interests.

That the US' economic advantage when compared to China is relatively limited and the two countries are each other's biggest market with the largest potential decides that managing a comprehensive conflict is a cost neither country could afford. This is exactly why the side effects of Trump's policies were quickly amplified at home, and also why the administration has slowed down its attacks.

Looking ahead, although the US will not easily scrap the trade sanctions already in place, it will hesitate to upgrade the standoff to a comprehensive confrontation. The third round of sanctions, which would have targeted $267 billion worth of Chinese exports, in particular is expected to cause much pain on both sides and thus is unlikely to fully materialize.

In the near future the US will probably focus on containing the development of China's high-tech sector by, for instance, imposing high tariffs on imports from China's emerging industries, cutting off the transfer of technology, confining the talent flow and freezing the overseas assets of China's core enterprises and institutions, with the ultimate goal of impeding the upgrading of China's manufacturing industry.

On that account, China's relevant industries should remain alert and take precautions, and the government should offer necessary protection to key enterprises, technology, assets and talent.

Third, the rivalry between China and the US will become a contest with a global dimension. As one of the core platforms for global policy coordination, the G20 Leaders' Summit provided the opportunity for the two countries to break the ice, but it also produced a joint communique which has cut off the phrases of opposing protectionism.

This mixed signal shows that apart from bilateral relations, multilateral platforms and institutions including the G20, the World Trade Organization (WTO) and the IMF will become the key stages for China-US competition.

Hereafter, the China-US trade contention, the progress and retrogression of globalization and reform of the global economic governance system will be bound together.

In this sense it is urgent for China to take two global challenges into its strategic considerations. One is the wave of populism that is undermining the policy rationality both in developed countries including Italy, Germany and the United Kingdom and emerging markets represented by Brazil and Mexico.

The imitation of Trump's policies in these countries would weaken the consensus on multilateralism and further smash the trammels on Trump's protectionism and populism. In addition, the global economic governance system has come to a fork in the road. Under the repeated assaults from populism, protectionism and isolationism, the flaws in the system have been exposed, making reform a matter of urgency.

Looking forward, the reform of international institutions including the WTO, IMF and World Bank may walk on two opposite and absolutist paths: Either, yielding to the threat of the US' pulling out, trade and financial issues are politicized and expanded into conflicts over the rules, system and orientation, which will eventually lead to the discretization of the global value chain and the tendency of clique-forming in policy choices; or, optimization of the dispute-resolving mechanism and multilateral cooperation mechanism to allocate more say to developing countries according to their contributions, thus checking certain countries' unilateralism and propelling the global economy back to the path of openness, inclusiveness and coordinated recovery.

So, in the second half of the China-US contest, how to make good use of the multilateral platforms, file reasonable appeals and lead reform of the global economic governance system while avoiding the containment of an economic Iron Curtain will be a new problem confronting China.

Fourth, the game theory will change from answering challenges to self-improvement. In the second half, the firmness, speed and depth of the two countries' respective strategic reform will decide the winner. China should hence focus on improving its economy based on reform and opening-up.

Domestically the new round of reform needs to be deepened and the government needs to develop policies to underpin growth in 2019. On one hand, market access for private enterprises should be significantly widened, providing more room for the development of private and small and medium-sized enterprises, optimizing China's economic structure and its market.

This would also help build a market environment of competitive neutrality and weaken the pressure that developed countries exert on China.

On the other hand, China should further strengthen the protection of intellectual property rights (IPR) and provide the same protection for foreign companies' IPR to reduce the external resistance to technology transfers.

Externally, a new round of high-level opening-up should be advanced. The automobile market and service industry should be gradually opened and the use of the negative list for foreign investment be promoted to share China's growth opportunities with other countries and expand the bonds of shared interests with the US.

Bilateral cooperation with major economies apart from the US — for instance, the European Union, Japan and India — should also be strengthened to further integrate the global industrial chain through tools and mechanisms including the Regional Comprehensive Economic Partnership and a trilateral free trade agreement between China, Japan and the Republic of Korea.

The more extensive and firm China's network of friends is, the better it will be able to prevent the US' China policies going to the extreme.

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