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# Rebooting U.S.-China Trade Ties: “Enter Ye Through the Narrow Gate”

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Nearly two weeks after the U.S. “Trade Avengers” unleashed during their visit to Beijing what one reasonably could call “trade shock and awe” with a very aggressive—if thoroughly researched and well-crafted—set of demands targeting the yawning U.S. trade deficit with China and the core of that country’s throaty industrial policy, China this week is taking its turn with the visit of Chinese Communist Party (CCP) Politburo member and Vice Premier Liu He, President Xi Jinping’s economic point man who is almost universally described as a thoughtful, pragmatic, and mild-mannered policy academic. In the interim, voices from a wide swath of official Washington have sounded the alarm about the dangers of Chinese influence operations and the presence of alleged subversives, while President Trump himself seemed to cast aside these growing concerns by suggesting via Twitter that he would ask the Commerce Department to overturn its action against the Chinese telecommunications firm ZTE—long a focus of the U.S. security community for suspected cyber espionage activity and irrefutable violations of U.S. law—in response to protests that reportedly emanated directly from President Xi. With such frenetically sustained action in such a short period of time, the fog of war seems particularly thick at the moment. As such, it seems like a good time to slow down and have a think about how we got here, what actually is going on, and, with a little bit of luck, perhaps think about some ways to craft a viable way forward.

Just like milestone birthdays in one’s personal life, important political anniversaries also can incline the mind toward reflection. Next year, of course, marks the fortieth anniversary of the reestablishment of diplomatic ties between the United States and China. As such, much breath and a lot of ink have been devoted to analyzing the course of the bilateral relationship over that nearly half-century. Although certainly not a universal opinion, it seems fair, if perhaps overly reductionist, to suggest that the general conclusion among a substantial number of U.S. officials, policy analysts, and journalists has been that the consistent U.S. policy emphasis on engagement with China during those forty years was, at the end of the day, a sham. In this rendering, naïve groups of senior policymakers in succeeding U.S. administrations and in most of the U.S. China-watching community were hoodwinked by wily CCP leaders who talked the talk of integrating into the so-called U.S.-led rules-based international order, but all the while they had a secret master plan to instead subvert that order and challenge U.S. primacy throughout the globe. In a slightly less menacing (if no less absurd) version of this narrative, China was, indeed, headed generally toward this hoped for integration under the stewardship of deceased paramount leader Deng Xiaoping and his handpicked successors Jiang

Zemin and Hu Jintao until Xi Jinping arrived and, through a ruthless consolidation of power, decided instead to change course in what now regularly is referred to in shorthand as Xi's "authoritarian turn."

But this conclusion seems utterly wrongheaded when examined in the light of hard facts. On the Chinese side of the equation, for example, Deng Xiaoping may have appeared warm and cuddly when donning his cowboy hat during his famous 1979 visit to the United States, but he could be just as ruthless and grasping as any other authoritarian leader. Deng's exceptionally courageous and dogged pursuit of the policies of reform and opening certainly are worthy of praise, but they cannot, and therefore should not, be separated from the fact that he was content to sit idly by as Chairman Mao's loyal lieutenant as Mao decimated his political rivals during the Anti-Rightist Campaign (1957-59) and the Great Leap Forward (1958-62). Nor should we forget that Deng used every ounce of his massive personal prestige with the People's Liberation Army to, with steely determination, rally his many reluctant commanders to execute the brutal Tiananmen crackdown of June 4, 1989. Similarly, Xi Jinping is no Jack-in-the-Box-like figure who has pulled a fast one with a sharp directional turn in the last couple of years made all the more stark after his sweeping consolidation of power at last fall's 19th Party Congress. In fact, it is this author's contention, as supported by a large body of written work and public commentary, that everything Xi has done over the last five years was abundantly clear, whether explicitly or in embryonic form—from the moment he was introduced to the world as China's new top leader in the fall of 2012, as encapsulated in his call for his country to pursue the "China Dream" set on a foundation of "the great rejuvenation of the Chinese nation." This by no means suggests the United States should express support for, or even acquiescence in, Xi's policies, but only that it should not be reacting with the borderline hysteria that now seems to be gripping Washington.

Indeed, a similar examination of the U.S. approach over the last forty years makes equally clear that the architects of the opening with China, as well as the presidents and policymakers that followed, generally were clear-eyed about the strategic imperatives underlying the relationship and the limits those realities imposed on bilateral cooperation. President Nixon and Dr. Henry Kissinger mainly saw in China a strategic counterweight to a Soviet Union they perceived to be on the march after the U.S. defeat in Vietnam. In his recent masterwork (*By More than Providence*) analyzing the full sweep of U.S. grand strategy toward Asia since the founding of the United States, my colleague, Dr. Michael J. Green, makes equally clear that subsequent U.S. administrations, if perhaps overconfident in their faith that growing prosperity would lead China toward at least more economic openness, generally understood that the CCP was never going to voluntarily change its political system, even if they—and, arguably, the current administration, still—struggled with accepting the idea that perhaps this should not be a direct U.S. policy goal. So we shall forgo a retelling of that history here in the interest of brevity and getting straight to the point, which is that, if anything, the fault in succeeding iterations of U.S. China policy has not been that we were misled, but rather that policymakers have struggled with the task of developing clear red lines for our relationship with China, and, absolutely critically, for failing to **operationalize** those red lines (we will return to this critical point below).

So, if we didn’t get it dramatically wrong, why all the hubbub, and the associated, undeniably dramatic ground shift in Washington when it comes to thinking about our relationship with China? A source of endless frustration with much China analysis of late is the seeming interest (or is it necessity?) to boil the complex, incredibly nuanced tableau of U.S.-China relations down to overly simplistic, sock-puppet-like narratives (e.g., China is our friend/China is our implacable enemy; Xi Jinping is a new emperor/Xi Jinping is merely the vessel for the collective CCP leadership, and so on). But, in this case, we will make an exception to try to drive home a critical, if simplistic, point. And this is that, for the vast majority of the forty years discussed above, the economic relationship between the United States and China has been one of extreme complementarity. In fact, (then Vice) President Xi captured this perfectly on his maiden journey to Washington in 2012 when he characterized our economic integration as the “ballast and propeller” of the overall bilateral relationship. Put another way, our complementary economic ties have served as a shock absorber for the more competitive—or even conflictual—elements of our relationship, including a host of perennial security issues and the differences in our respective values and governing systems. In short, those other tensions always are with us, but they have only rarely been immediate, and were not sufficiently grave to outweigh the tremendous economic benefits to be had by both our countries.

But, with China’s legitimate desire to break through the middle income trap and advance to the forefront of the world’s developed economies, our economic relationship is turning more competitive. To achieve Xi’s new—and ambitious—goal established at the 19th Party Congress of attaining “socialist modernization” by 2035, to say nothing of “the great rejuvenation of the Chinese nation,” he and China must go *exactly* where the United States must go as they focus the country’s economic development plans on the industries and services of the future world economy. Moreover, two related realities serve to substantially exacerbate the potential for increased tension. First, China’s use of a robust industrial policy toolkit—subsidies to favored domestic champions, seemingly unlimited state-backed funding, and an expansive regulatory regime, to name just a few—to advance its goals has alienated one of its most important traditional allies, the U.S. (and other foreign) business community. No longer can the CCP rely on U.S. business to call for restraint when the U.S. Government considers policies across a range of areas that might be unwelcome in Beijing. In fact, there is substantial evidence that at least some elements of the U.S. business community, and especially those in the traditional manufacturing industries, have been egging on the Trump administration to push back on China.

Secondly, and perhaps more importantly, Xi and his Politburo colleagues are exceptionally determined to achieve these goals because they judge (correctly) that the very viability of continued CCP rule likely hangs in the balance. In other words, unlike in democratic polities, where political parties sketch out sweeping goals in their electoral platforms knowing full well they will achieve almost none of them, Xi and the CCP have no such luxury. These are the perils of performance-based legitimacy, and, in this context, it means that the CCP and its leaders are going to fight very hard to succeed using whatever means they have at their disposal.

Taken in combination, these factors suggest that the previous pursuit of “strategic trust” between the United States and China risks being replaced by “strategic divergence.” With the economic shock absorber no longer functioning as before, the previously suppressed more competitive elements of the relationship are coming more readily, and more quickly, to the fore. Moreover, it is fair to say that several of President Xi’s policies have acted as an accelerant to that process. The displacement of China’s previous low-profile foreign policy with projects such as the Belt and Road Initiative and the militarization of China’s artificial islands and edifices in the South China Sea cause many to wonder about China’s motives and designs for the region and beyond. Similarly, Xi’s steady emphasis on the leading role of the CCP and Marxist ideology (even with Chinese characteristics) in shaping China’s future direction rings cacophonously in the ears of Western leaders and especially to the Trump administration. The result is the advent of what could well be described as “the new holy trinity,” wherein the United States now characterizes China in its most authoritative declarations of U.S. strategic policy as a strategic competitor and revisionist power practicing predatory economics.

With the problem (at least hopefully) accurately diagnosed, we now can turn our attention to an examination of what it means for the current trade dispute between our two countries and how our respective leaderships might choose to manage the situation. To cut to the chase, the trade spat can be seen to fundamentally turn on two key dilemmas. The first is the seeming tension between what we might for convenience refer to as the backward looking and the forward looking elements of the dispute. The backward looking issues focus on the alleged loss of traditional manufacturing jobs to China over the last few decades and the associated desire to protect, or perhaps even advance, those industries in the United States. The forward looking elements deal with matters related to the future knowledge economy (especially services) and related concerns about Chinese theft of core U.S. intellectual property (IP) and information technology (IT). The second, but closely related dilemma is the tension between the tactical goals (reducing the substantial bilateral trade deficit) and their associated tools (the threat of tariffs) and the structural ones (grappling with Chinese industrial policy as an enabler in the competition for the industries of the future, and the consideration of policies like greater investment or visa strictures to try to combat it).

Putting aside the bilateral aspect of these tensions for a moment, the seemingly clear tensions *within* the Trump administration on these dilemmas are making the bilateral discussion more fraught. Judging from news accounts, anyway, “the Avengers” frequently seem to spend as much time fighting with each other over these matters as they do fighting the Chinese. Although undoubtedly oversimplified, the general narrative is that U.S. Trade Representative Robert Lighthizer and White House Director of Trade and Industrial Policy Peter Navarro are focused on the backward looking and structural pieces while Treasury Secretary Steven Mnuchin and National Economic Council Director Larry Kudlow are more concerned with the future looking and tactical bits. Making things still more complicated are the contradictory signals from the administration as to who actually has the lead on these matters. One day Ambassador Lighthizer appears to have the conn, while another it seems to be Secretary Mnuchin. To underscore the point, one of Liu He’s chief gripes from his last visit to Washington reportedly was that every U.S. official he met with claimed that he was Liu’s interlocutor.

Regardless of the parlor game aspect of the debate, the critical factor always seems to be who has the ear of President Trump, and he seems to like to play his advisers off against one another.

Turning back to the bilateral picture, the two dilemmas discussed above have made it difficult for the Chinese to zero in on exactly what the U.S. side wants them to do. Of course, the Chinese should not be allowed to use such claims as an excuse to defer action, and it certainly is true that one reason they repeatedly raise the issue of specific asks is to determine the minimum they can do to get over the current rough patch. Still, the reported frequent U.S. retort, “you know what you need to do,” while potentially emotionally satisfying, is problematic. Like it or not, China’s political system is a top-down, heavily stovepiped Leninist bureaucracy. Xi’s concentration of power, although potentially ameliorating some of these realities in the long run, appears to be exacerbating them in the short term. So, without some sort of clear guidance as to U.S. priorities, inertia will always be the favored posture of the Chinese policy system. Some may argue that the list of demands presented by the U.S. delegation in Beijing resolves this dilemma by making abundantly clear what our asks are. But asking China to fundamentally unwind the central pillars—the 13th Five-Year Plan, Made in China 2025—of its economic blueprint for the next several decades just isn’t realistic, especially for the type of bureaucracy just described above.

So what, if anything, is to be done? Both parts, the backward looking, tactical elements and the forward looking, structural challenges each are freighted with their own unique difficulties. As such, it seems like the best place to start is to adopt what can best be described as a bifurcated or two-track approach. Under such a scenario, the two sides should work hard to come to a quick consensus on the backward looking, tactical pieces while deferring the forward looking, structural issues for future rounds of dialogue. In fact, news accounts of the current state-of-play suggest that this dynamic already is taking shape, with the U.S. side seemingly ready to accept a “mini-deal” focused on relief from threatened Chinese tariffs on agricultural imports, some additional deficit-reducing purchases, and a few new commitments on market access, while China clearly has underscored the long-term strategic relevance of the structural fight with its arguably over-the-top insistence on relief for ZTE.

Some have argued, almost reflexively, that such an approach constitutes a “bad deal,” at least for the United States. That certainly would be the case if the Trump administration takes such an agreement, declares victory, and abandons the field when it comes to the long-haul structural gladiatorial combat. If, however, there is a general recognition, preferably by both sides, that the deficit-focused tariff squabble is fueling the most anxiety—whether in China, the United States, or around the globe—about a potential trade cataclysm, while the less immediate structural debate can be played out over decades, and perhaps even mostly out of public view, then a modicum of stability probably can be achieved. From there, sorting out whether such stability can be made durable over any relatively lengthy time horizon likely would turn on how the two issues are negotiated.

For example, if a bargain on tariff relief is merely a Band-Aid, as opposed to a genuine effort to tackle the issues like overcapacity that underpin it, then the deal is unlikely to last long. Similarly, iron-faced insistence that China completely abandon its plans, even as currently construed, for moving up the



global value and supply chains is equally infeasible. So, as is so often the case on such vexing questions, the Goldilocks rule—or, perhaps better, a middle path—probably has the most applicability here. For the tactical issues, such a middle path would land somewhere between the Band-Aid described above and the all-out declaration of hermetically-sealed protected industries on each side. It could focus on requiring China to offer up fresh access, with ironclad, near-term implementation timelines, to sectors that were never on the table as part of its WTO accession or the now-defunct Bilateral Investment Treaty negotiations, while the United States could offer to take a breath on pending investment and visa restrictions that would make China much more reluctant to agree that its trade deficit with the United States is a problem.

On the structural side, a jumping off point could include a U.S. offer to acknowledge (as opposed to accept) China's desire (as opposed to right) to move up the global value and supply chains, and perhaps to make that acknowledgement public in the form of a major policy address (similar to Ambassador Robert Zoellick's 2005 "responsible stakeholder" speech). This is, after all, what Washington has been encouraging China to do for the last few decades. In return, China could agree, with some sort of robust verification mechanism, to curtail the toothiest elements of its industrial policy, such as subsidies to strategic industries and the juicing up of national champions with state cash for competition with foreign multinationals in third country markets. Or, if such a plan was deemed entirely too level-headed, we could perhaps agree that we are, indeed, entering a multi-decade cold war on IT and IP, but that this war can, and therefore should, largely be fought in the shadows, where it can avoid scaring our respective markets and populations about a pending trade war that risks tipping into a hot war (the tired Thucydides Trap meme).

Which brings us, finally, to the issue of how we correctly diagnose the problems in the economic relationship, as well as how we define and operationalize, as noted above, our redlines with China. Here, the Trump administration deserves some credit for its determination to avoid Einstein's definition of insanity, or the practice of doing the same thing over and over again while expecting a different result. In many ways, the administration's candor in calling out, and therefore popularizing, some of China's most unfair or potentially anticompetitive trade practices has shone a necessary light on the problem areas (Ambassador Lighthizer has dramatically enhanced U.S. awareness of the potential pitfalls associated with the Made in China 2025 program, for example, which previously was the exclusive domain of China nerds like yours truly).

But, although the diagnosis of the disease may be correct, the calculation of where U.S. leverage best lies is critical when operationalizing U.S. redlines. The demands presented in Beijing, for example, risk being interpreted by the CCP as the last gasp of an aging prize fighter who is trying to hold onto the championship title for at least a few more bouts. A better approach, perhaps, is to improve our understanding of what actually is happening in China, what President Xi's priorities are for his economy, and how that may give us more effective leverage. For example, few U.S. commentators on the trade dispute have mentioned that President Xi, during his early April remarks to the first meeting of the newly-upgraded CCP Central Financial and Economic Affairs Commission, stressed that, as part of the government's crackdown on financial risk, local governments and state firms should

expect to feel the same deleveraging pressure that we saw in the interbank area throughout the second half of 2017. Similarly, few have commented on new central bank Governor Yi Gang’s series of remarks about wanting to loosen capital controls after China’s earlier (over) tightening of the capital account in response to massive capital outflows. What does this have to do with U.S.-China trade tensions, you might ask? A lot; for China cannot move ahead with confidence on these very pressing domestic priorities while such immense uncertainty remains with regard to its export picture resulting from the tensions with Washington. Understanding that point gives far more enduring leverage—one might call it “smart leverage”—to U.S. negotiators than threats that could backfire if China chose to truly test U.S. resolve.

In closing, it may appear odd or ironic that the title of this piece draws on “the Good Book” for a suggested approach in dealing with the CCP. But it should not surprise those of us who believe that our best policy approaches often have their roots in the values we share and cherish. It’s also worth noting that, like so many of the bits of wisdom from that source of inspiration, the injunction is accompanied by a warning. “For wide is the gate and broad is the road that leads to destruction.”

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