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China and the U.S.: Cooperation, Competition and/or Conflict

An Experimental Assessment

PART THREE: SHAPING ECONOMIC COMPETITION TO SERVE STRATEGIC INTERESTS

**Working Draft
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Photo: GOH CHAI HIN/AFP/ Getty Images

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Shaping Economic Competition to Service Strategic Interests

As has been noted earlier, economic competition offers China its best path to achieving its strategic interests and gains. China fully understands this and is rapidly evolving from a nation whose success depended on exports that depended on the efficient use of low-cost labor to becoming a sophisticated exporter of advanced manufactured goods with trading links to a wide range of commodity exporters and importers in advanced industrialized states.

China's "belt and road" system has become a symbol of such economic activity and global integration, along with its steadily rising global trade position. Almost inevitably, this expansion has expanded China's influence in the rest of Asia, as well as in Europe, the Middle East, Africa, and Latin America. It has also led China to expand the role of its naval forces, arms exports, and security ties – as was the case with colonial powers, the U.S. and Russia before it.

Here, China has an inherent geographic advantage over the U.S. in dealing with Southeast Asia, Central Asia, and South Asia, and in creating new land routes between Asia and Europe. China's "belt and road" efforts indicate that it will establish major new ports, create stronger maritime routes, and use roads, rails, and pipelines to strengthen its economic and strategic position.

These efforts will give China potential advantages in power projection and military influence as well. It is important to note, however, that China so far seem more interested in expanding its economic interests and leverage than in establishing direct military ties and strategic partnerships. It has expanded its role in UN peacekeeping, but it has not shown that it intends to follow the U.S. and Russian example in creating major military deployments outside China's immediate sphere of influence.

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DEVELOPMENTS IN ECONOMIC POLICY

Key Takeaways

- > China is non-compliant with some of its World Trade Organization (WTO) obligations.
- > Recognizing that “Made in China 2025” and OBOR have sparked concerns about China’s intentions, China’s leaders have softened their rhetoric when promoting these programs without altering the programs’ fundamental strategic goals.
- > China continues to operate as a centrally controlled, planned economy. China restricts inbound investment, limits other countries’ exports, and pursues state-guided investment overseas, including in strategic sectors.

Sustaining China’s economic growth is one of the CCP’s strategic objectives. China’s incomplete transition to a market economy has resulted in laws, regulations, and policies governing the tradable goods and services sectors, market access, and foreign direct investment that disadvantage foreign firms vis-à-vis their Chinese counterparts. China’s senior leaders recently reaffirmed their commitment to CCP control over the state-led economic apparatus, including through state-directed investment and innovation. In March 2018, the Office of the U.S. Trade Representative released findings of an investigation under

Section 301 of the Trade Act of 1974 that determined the acts, policies, and practices of the Chinese government related to technology transfer, intellectual property, and innovation are unreasonable or discriminatory and burden or restrict U.S. commerce, resulting in harm to the U.S. economy of at least \$50 billion per year.

China is non-compliant with some of its World Trade Organization (WTO) obligations, and China does not adhere to some of the agreed-upon rules and fundamental principles that undergird WTO agreements. In addition, because of its status as a “developing country” under the WTO framework, China is allowed to continue certain protectionist measures. Concerns include industrial policies that support domestic industries at the expense of foreign counterparts, commercial joint venture requirements, technology transfer requirements, subsidies to lower the cost of inputs, continued excess capacity in multiple industries, sector-specific limits on foreign direct investment, discriminatory cybersecurity and data transfer rules, insufficient intellectual property rights enforcement, inadequate transparency, and lack of market access particularly in the agriculture and service sectors. Market access remains challenging for foreign firms, as China’s restriction of inbound investment results in persistent underperformance in other countries’ services exports, particularly in the banking, insurance, Internet-related, professional, and retail services sectors.

Some recent Chinese laws seek further restrictions on foreign firms:

- > *National Security Law*: Adopted in July 2015, the law limits foreign access to the information and communications technology (ICT) market in China on national security grounds.
- > *Counterterrorism Law*: Adopted in December 2015, the law requires telecommunications operators and Internet service providers to provide information on technical support assistance to public and state security organizations “conducting prevention and investigation of terrorist activities.”
- > *Cyber Security Law*: The law, which went into effect in June 2017, promotes development of indigenous technologies and restricts sales of foreign ICT. The law also mandates that foreign companies submit ICT for government-administered national security reviews, store data in China, and seek government approval before transferring data outside of China.

As China restricts inbound investment and limits other countries’ exports to China, it also pursues state-directed investment overseas. Along with heavy investments in infrastructure and commodities to support its economic growth, China is investing in technologies that will be foundational for future innovations with both commercial and military applications.

China obtains foreign technology through imports, foreign direct investment, the establishment of foreign research and development (R&D) centers, joint ventures, research and academic partnerships, talent recruitment, and industrial and cyberespionage. In December 2018, two Chinese nationals were indicted for conspiracy to commit computer intrusions, conspiracy to commit wire fraud, and aggravated identity theft. The Chinese nationals worked for a company in China called Huaying Haitai Science and Technology Development Company and acted in association with the Chinese Ministry of State Security’s Tianjin State Security Bureau. Through their involvement with a hacking group operating in China known as Advanced Persistent Threat 10 (APT10), the Chinese nationals conducted global campaigns of computer intrusions targeting intellectual property and confidential business and technological information at managed service providers. The APT10 group stole hundreds of gigabytes of sensitive data and targeted the computers of victim companies involved in aviation, space and satellite technology, manufacturing technology, pharmaceutical technology, oil and gas exploration and production technology, communications technology, computer processor technology, and maritime technology.

Recent government policies have promoted innovation focused on strengthening domestic industry, while placing additional restrictions on foreign firms. Recognizing that some of its

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programs such as “Made in China 2025” and OBOR have sparked concerns about China’s intentions, China’s leaders have softened their rhetoric when promoting these programs without altering their fundamental strategic goals.

- > *“Made in China 2025”*: China has become aware of acute concerns that advanced industrial countries have regarding “Made in China 2025,” and in June 2018, Chinese media outlets were ordered to downplay use of the term. Announced in May 2015, the “Made in China 2025” plan sets targets for higher levels of domestic manufacturing in strategic industries by 2020 and 2025 with the goal of increasing indigenous innovation. China plans to award subsidies and strengthened protection of domestic industries, while increasing pressure on foreign firms to transfer technology in order to do business in China. The plan also seeks to favor domestic enterprises at the expense of foreign participants in China’s markets.
- > *OBOR*: OBOR is intended to develop strong economic ties with other countries, shape their interests to align with China’s, and deter confrontation or criticism of China’s approach to sensitive issues. Countries participating in OBOR could develop economic dependence on Chinese capital, which China could leverage to achieve its interests. The growth of China’s global economic footprint also makes its

interests increasingly vulnerable to international and regional turmoil, terrorism, piracy, and serious natural disasters and epidemics, which places new requirements on the PLA to address these threats. Some OBOR investments could create potential military advantages for China, should China require access to selected foreign ports to pre-position the necessary logistics support to sustain naval deployments in waters as distant as the Indian Ocean, Mediterranean Sea, and Atlantic Ocean to protect its growing interests.

China has employed economic tools coercively during periods of political tensions with its neighbors. Following the collision of a PRC-flagged fishing boat with a Japanese Coast Guard vessel near the Senkaku Islands, China halted exports to Japan in 2010 of rare earth elements used in high-tech industries. In 2016, after the visit of the Dalai Lama to Mongolia, China suspended talks on a major assistance loan, worsening Mongolia’s fiscal challenges and eventually driving it to seek a bailout from the International Monetary Fund. China also increased fees on imports of mining products from Mongolia and temporarily closed an important border crossing. China used economic and diplomatic pressure unsuccessfully in 2017 in an attempt to urge South Korea to reconsider the deployment of the Terminal High-Altitude Area Defense (THAAD) system.

Roads, Belts, and Strait Jackets: China's Growing Global Engagements

Roads, Belts, and Being an Asian Land Power

While the U.S. strategic focus on China has generally been on Eastern China and its role in the Pacific, China's geography gives it maritime trading routes to the Middle East and Europe, and gives it a continent-sized land bridge to Central Asia and Europe. China has actively exploited these routes in the past, and its economic revival and the collapse of the Former Soviet Union has led to the rebirth of these trading routes and a major expansion of China's influence in Asia and in Russia.

The Shanghai Cooperation Organization is one symbol of this rebirth, although it remains a relatively limited force in uniting Asia and expanding China's influence. China's revival of its trading routes across Asia to Europe, and by sea through the Indian Ocean, however, has become an increasingly important part of China's strategic position.

The maps in this section that show the patterns in China's belt and road initiatives illustrate this fact, and the large number of roads, ports, and infrastructure projects shown in these maps are matched by increasing Chinese investment, arms sales, and military influence. China's plans are extremely ambitious, however, and the extent to which China can actually develop such economic ties and influence is far from clear.

Some countries have already found that China's willingness to invest, and offer aid and loans, serves China's interests at their expense. Some Chinese projects have also proved to be poorly planned and provide far fewer benefits to China than were initially promised. Accordingly, much will depend on how well China can improve its efforts to win the support of other states, and its plans and project execution. Grand strategic ambitions come easily; grand strategic successes are a very different story.

China's 70th Anniversary White Paper on Belt and Road

We will build a high-quality Belt and Road together with our partners. The Belt and Road Initiative is based on the principles of extensive consultation, joint contribution and shared benefits, and is guided by the Silk Road spirit characterized by peace, cooperation, openness, inclusiveness, mutual learning and mutual benefit. With a focus on policy coordination, connectivity of infrastructure, unimpeded trade, financial integration and closer people-to-people ties, it has transformed from ideas into action, from vision into reality, from a conceptual initiative into a globally popular public product (see Box 10). In November 2016, the United Nations adopted a resolution welcoming economic cooperation initiatives such as the Belt and Road Initiative. In March 2017, the United Nations Security Council called on all countries in its resolution to promote the initiative and the building of a global community of shared future. The Belt and Road Initiative originated in China, but the opportunities and achievements belong to the whole world. According to a World Bank research report, the initiative will help 7.6 million people out of extreme poverty and 32 million out of moderate poverty. It will increase trade in participating countries by 2.8 to 9.7 percent, global trade by 1.7 to 6.2 percent and global income by 0.7 to 2.9 percent. The initiative is a veritable road to resource sharing, shared prosperity and common development. (World Bank, "Belt and Road Economics: Opportunities and Risks of Transport Corridors", June 2019.)

...The first is in policy coordination. Since the initiative was put forward, it has received positive responses from more than 160 countries, regions, and international organizations. By the end of August 2019, the Chinese government had signed 195 Belt and Road cooperation documents with 136 countries and 30 international organizations.

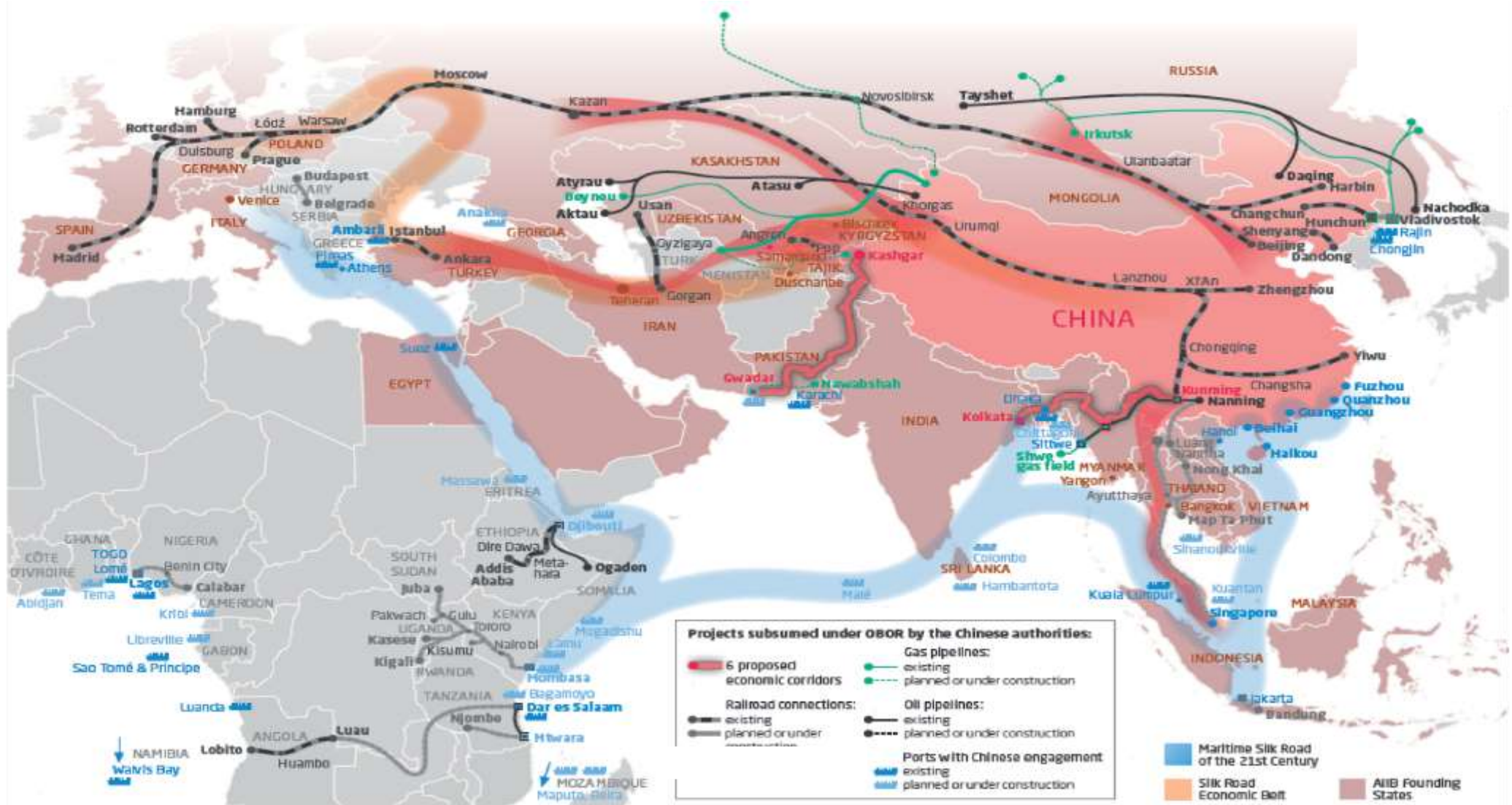
The second is in infrastructure connectivity. Great progress has been made in the construction of key interregional and intercontinental railway networks such as the China-Laos Railway, China-Thailand Railway, Hungary-Serbia Railway and Jakarta-Bandung High-Speed Railway. By the end of June 2019, a total of 16,760 China-Europe freight trains had carried almost 1.5 million TEUs of goods, reaching 16 countries and 53 cities abroad.

The third is in unimpeded trade. China has set up 18 pilot free trade zones. Since the First Belt and Road Forum for International Cooperation in 2017, China and other countries along the routes have signed more than 100 customs inspection and quarantine cooperation documents and established more than 40 customs inspection and quarantine cooperation mechanisms. From 2013 to 2018, the imports and exports of goods between China and other Belt and Road countries totaled nearly US\$6.5 trillion.

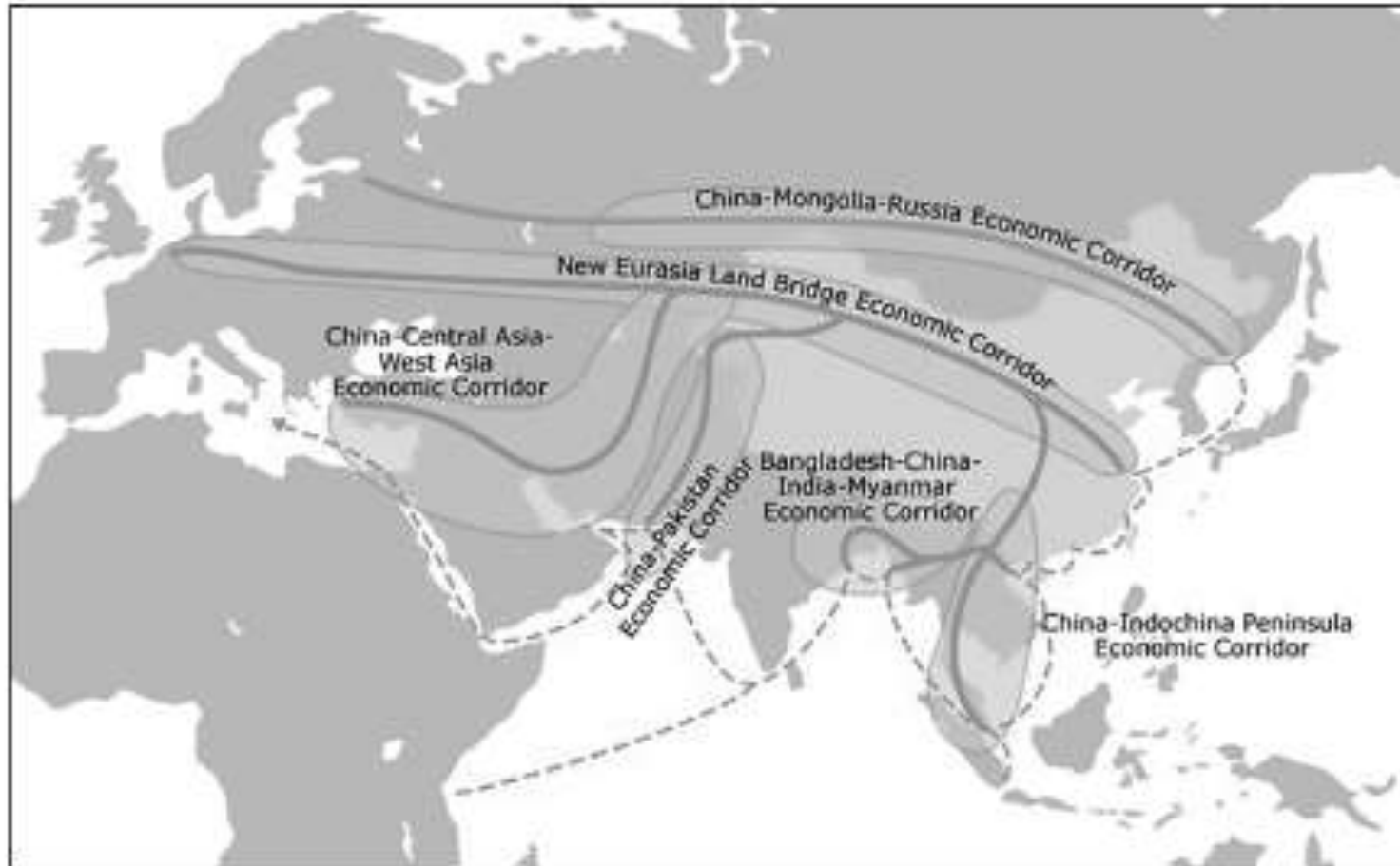
The fourth is in financial integration. The open, pluralistic and market-oriented investment and financing system has continuously improved. By the end of the first quarter of 2019, the People's Bank of China, the International Finance Corporation of the World Bank Group, the European Bank for Reconstruction and Development, and the African Development Bank had jointly financed nearly 200 projects covering more than 70 countries and regions. By the end of 2018, Chinese enterprises had invested more than US\$90 billion in Belt and Road countries, and the turnover of contracted projects had exceeded US\$400 billion.

The fifth is in closer people-to-people ties. As of July 2019, of the 136 countries that had signed Belt and Road Initiative cooperation documents with China, China had concluded mutual visa exemption agreements with 113 countries covering different types of passports, and visa facilitation agreements or arrangements with 25 countries. Since the Belt and Road Initiative was launched in 2013, China has concluded mutual visa exemption agreements with 71 participating countries and visa facilitation agreements or arrangements with 11. Since the First Belt and Road Forum for International Cooperation, China has provided RMB2 billion in emergency food assistance to developing countries along the routes, and has launched 100 "happy home" projects, 100 poverty alleviation projects, and 100 healthcare and rehabilitation projects. In 2017, 38,700 people from countries along the routes studied in China on scholarships from the Chinese government. In 2018, China hosted 500 young scientists from other Belt and Road countries to conduct research exchanges.

China's Expanding Strategic Interests: One Belt, One Road (OBOR) in 2017



China's Different Belt and Road Initiatives



The Asian Development Bank estimates that Asian states will need \$26 trillion in infrastructure investment from 2016-2030.

In the five years of the BRI, it has extended to more than 80 participating countries making up 30% of the global GDP.

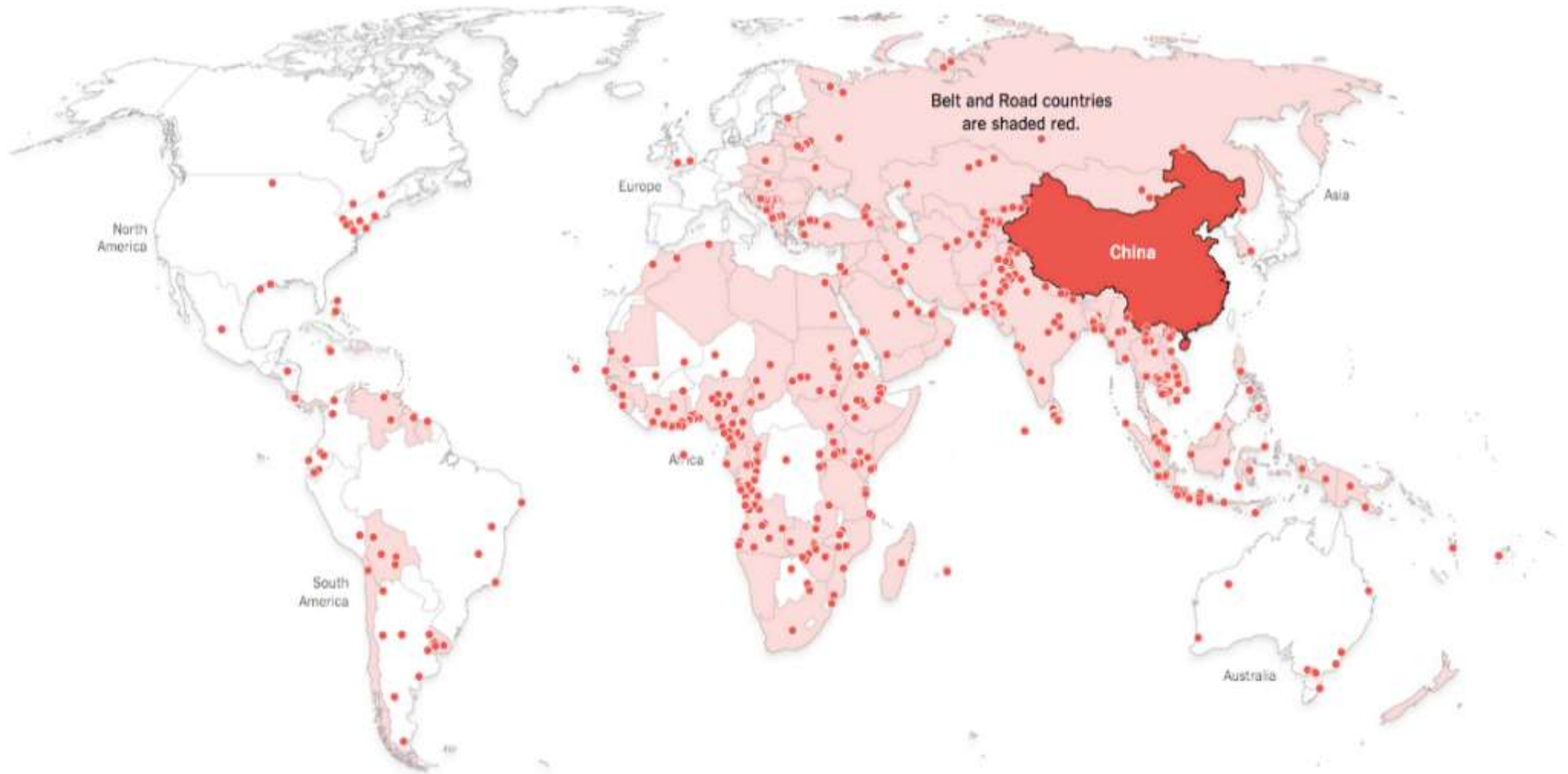
Source: Hong Kong Trade Development Council, "The Belt and Road Initiative," May 3, 2018.

China's BRI (Belt and Road Initiative)



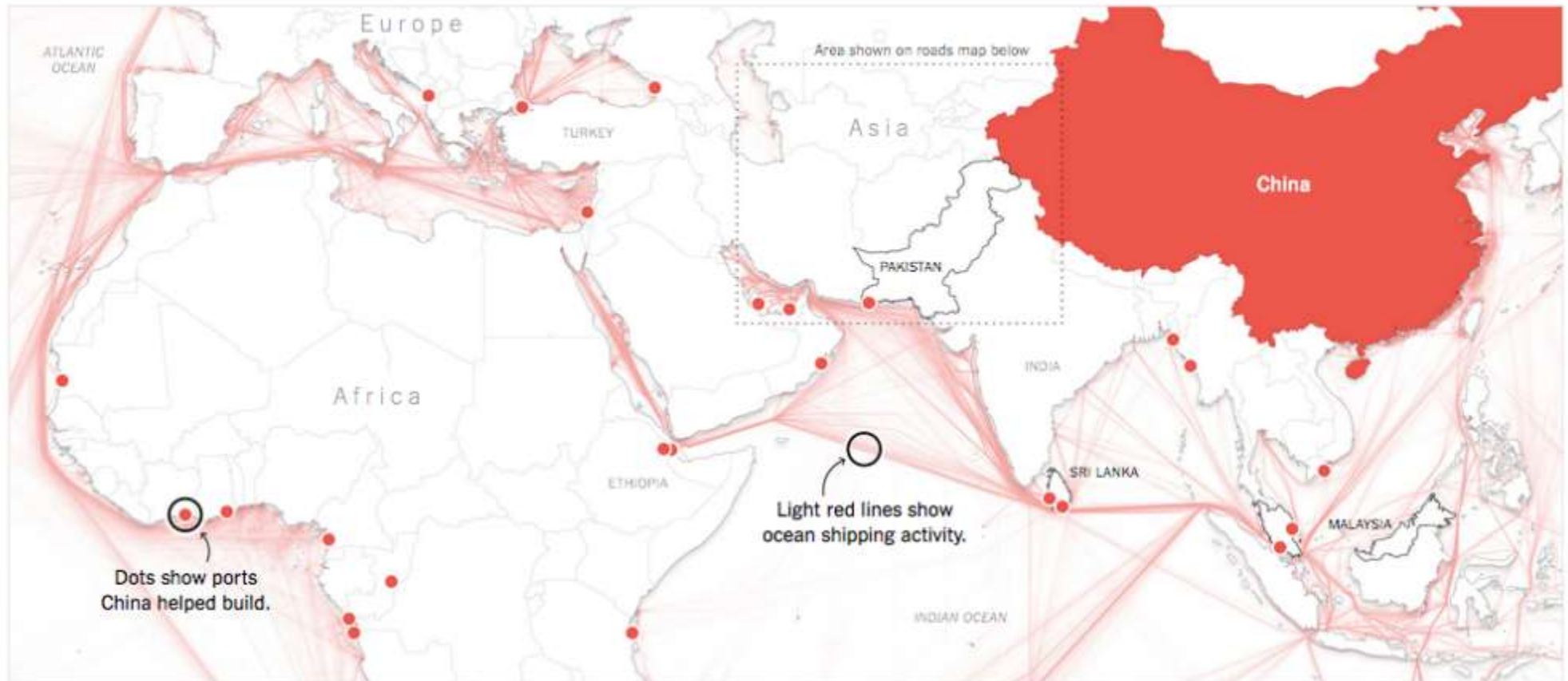
Source: https://www.google.com/search?q=map+of+china+belt+and+road&client=firefox-b-1-d&tbm=isch&source=iu&ictx=1&fir=66sfHK71h_jcuM%253A%252CmjDrrWaG4Z73hM%252C_&vet=1&usg=AI4_-kQGt_KqtZ7CCHJGE_ri4TY-FgRaXw&sa=X&ved=2ahUKEwj45dzTsOTiAhULyFkKHT2WD5sQ9QEwC3oECAIQGg#imgrc=7HfbLY9R651SIM:&vet=1

China's BRI (Belt and Road Initiative) – 112 Countries Worth of Global Projects as of 2018



China's BRI (Belt and Road Initiative) – Major Ports Projects as of 2018

Large ports in Pakistan, Sri Lanka and Malaysia — three countries along a major oil and commerce route from the Mideast and Africa — could someday double as naval logistics hubs.



Source: Shipping data from University College London Energy Institute.

China's BRI (Belt and Road Initiative) – Road Projects in Central Asia, South Asia, and Iran



Source: Center for Strategic and International Studies.

China's Growing Share of the Global Economy and Trade

China's Rising Global Role in Trade

China's success in becoming the world's leading trading state is far clearer. The exact figures involved may be uncertain, but the broad trends displayed in this section are not. Moreover, China's expanding role in global trade is having a major impact on the West, and other parts of the world, as well as Asia.

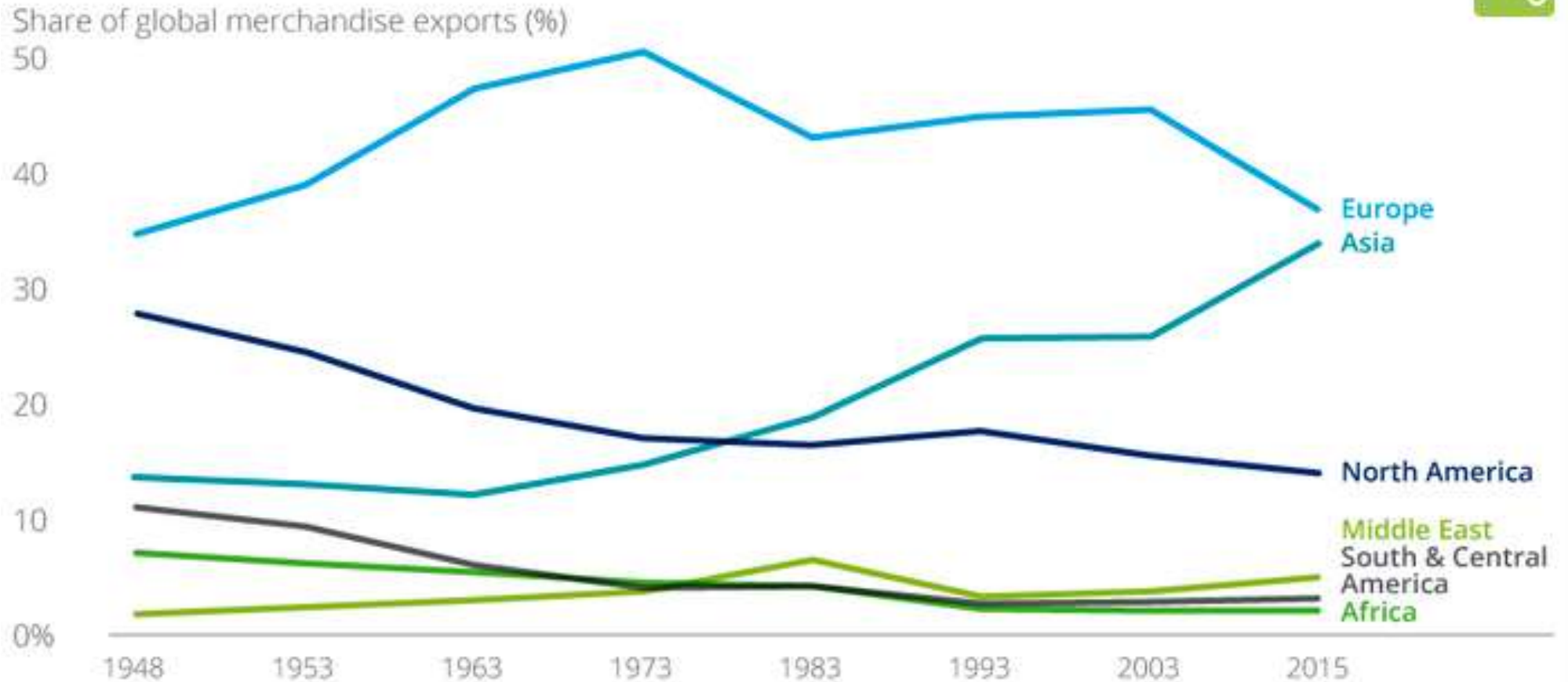
The graphics in this section show how quickly Asia as a whole has expanded its role in global exports. They also show how China's growing exports and investments export on the entire world, and the range of different trade routes involved.

They show that China's volume of trade has risen to the point where it is now larger than that of the United States and Japan, and the U.S. has become increasingly dependent on Chinese imports at the expense of a major trade deficit and exporting services that often help China develop its technology and manufacturing base.

As other charts in this study show, China's increasing volume of global trade has been driven by merchandise trade, increases in manufacturing capacity, and increasing levels of high technology exports – activities which benefit both China's civil and military industrial base.

They have, however, increased China's dependence on energy imports, on maritime traffic, and its own merchant marine. Trade has greatly explained China's global influence, but it has also increased China's global dependence on commodity and energy imports, the stable and secure flow of global trade, and the overall health of the global economy.

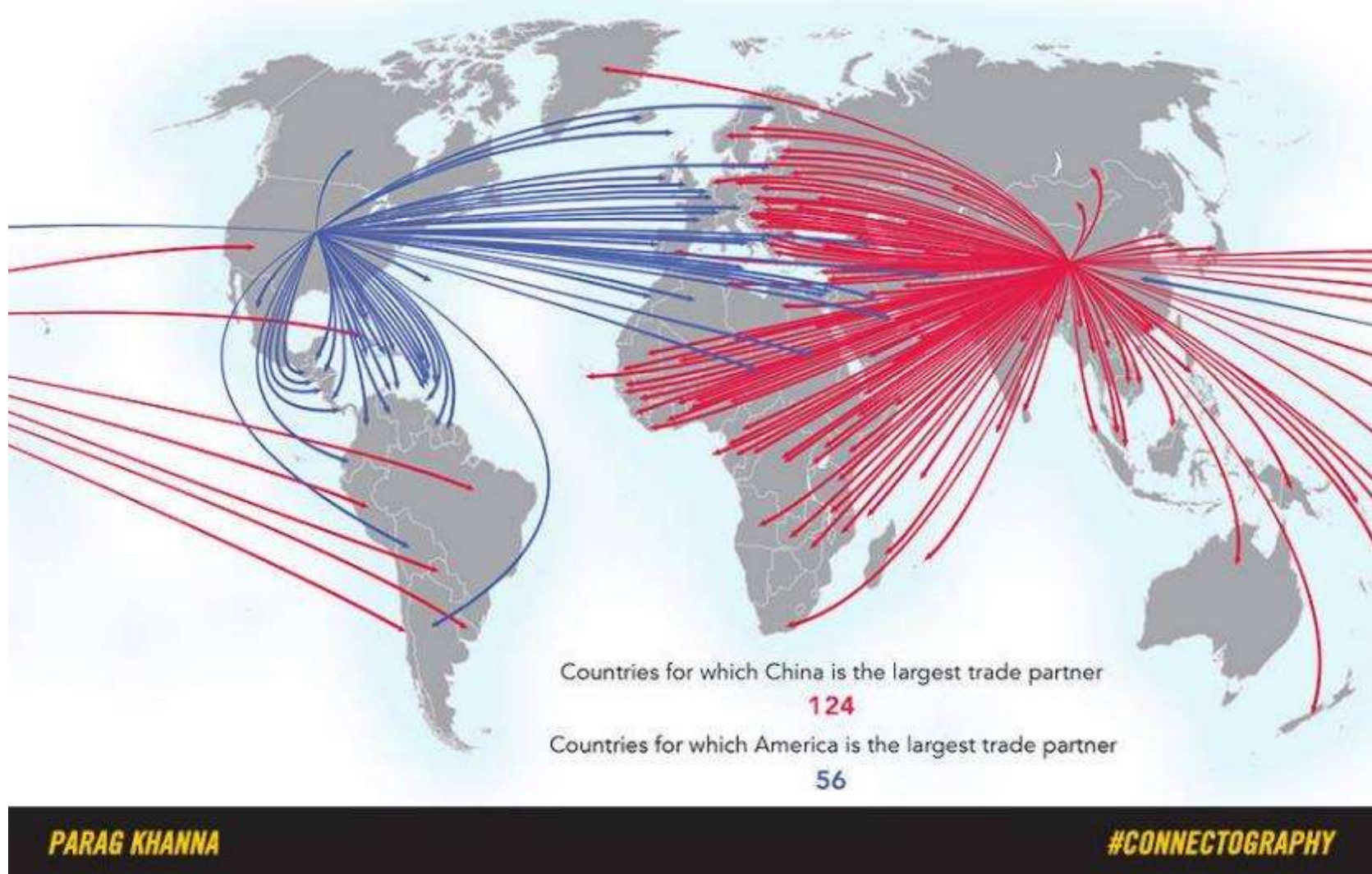
Regional Shares of World Exports: 1948-2015



Source: World Trade Organisation.

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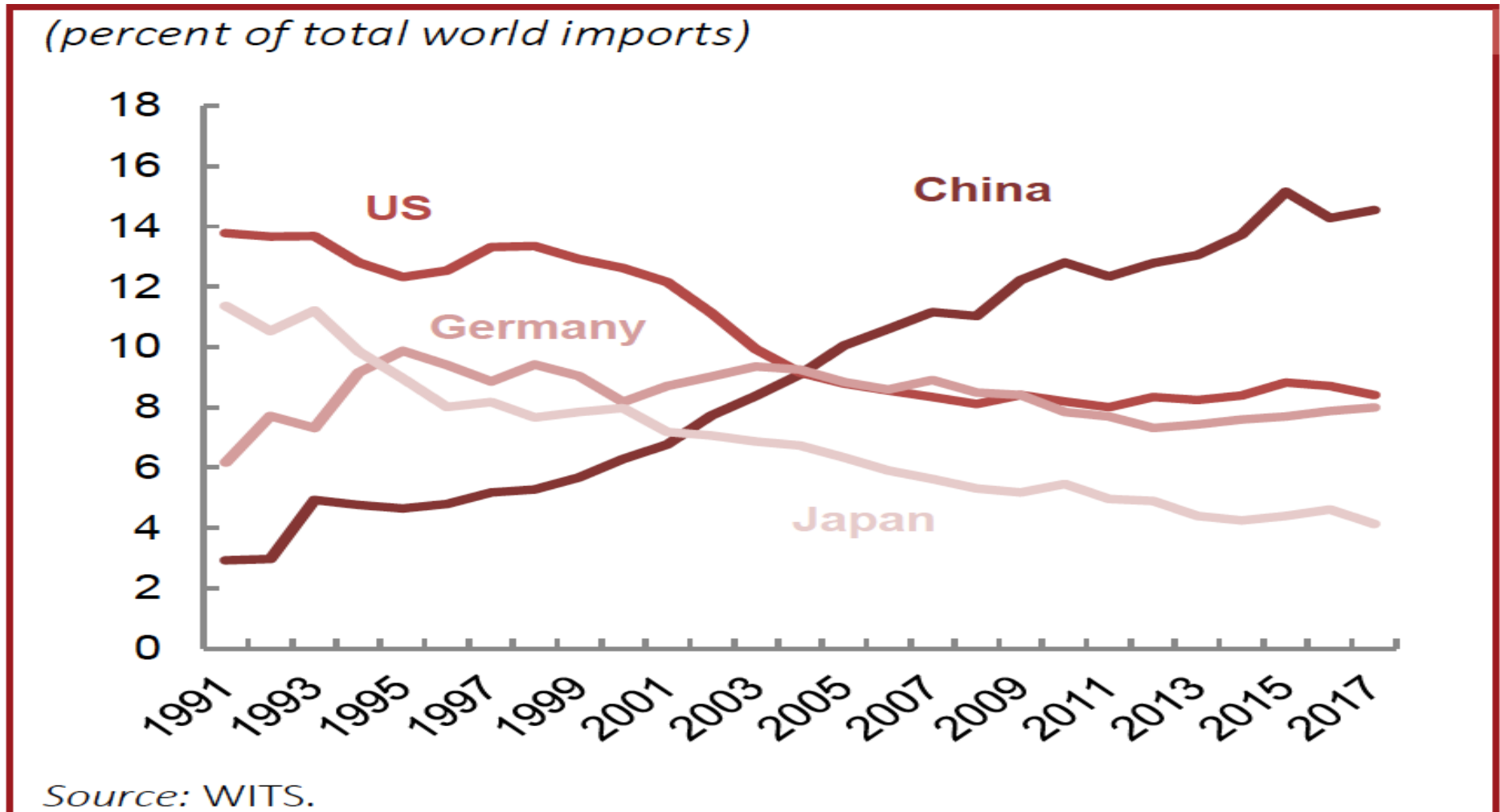
China vs. U.S. Trade Flows



Source: [https://www.google.com/search?q=Map+of+China%27s+trade&client=firefox-b-1&tbm=isch&tbs=ring:CT3yazFJlNebIjh9xjxu5BRSEAHh7C08FjXLTbKfehX0zxUcqsJjtx-kWGTxPaVfoig-7FW5HMe1N73CuG5eSM6m6ioSCX3GPG7kFFIQEfQK6GOS6bDxKhIAeHsLTwWNcsRZpQw1SAjcXoqEglNsp96fTPFRGe3Lp1h9UgeioSCRYqwmO3H6RYEboRDrAr7AzzKhIJa3E9pV-giD4RymVnNI2Wrb0qEgnsVbkcx7U3vRFLrJgRcRMtYCoSCcK4bl5IzqbqESEYozKSJeh_1&tbo=u&sa=X&ved=2ahUKEwjF2Pyo34XbAhXvV98KHdpsD88Q9C96BAgBEBS&biw=721&dpr=1.2#imgsrc=fcY8buQUUhD2rM:/.](https://www.google.com/search?q=Map+of+China%27s+trade&client=firefox-b-1&tbm=isch&tbs=ring:CT3yazFJlNebIjh9xjxu5BRSEAHh7C08FjXLTbKfehX0zxUcqsJjtx-kWGTxPaVfoig-7FW5HMe1N73CuG5eSM6m6ioSCX3GPG7kFFIQEfQK6GOS6bDxKhIAeHsLTwWNcsRZpQw1SAjcXoqEglNsp96fTPFRGe3Lp1h9UgeioSCRYqwmO3H6RYEboRDrAr7AzzKhIJa3E9pV-giD4RymVnNI2Wrb0qEgnsVbkcx7U3vRFLrJgRcRMtYCoSCcK4bl5IzqbqESEYozKSJeh_1&tbo=u&sa=X&ved=2ahUKEwjF2Pyo34XbAhXvV98KHdpsD88Q9C96BAgBEBS&biw=721&dpr=1.2#imgsrc=fcY8buQUUhD2rM:/)

Share of Global Trade in Goods by Country: 1991-2017

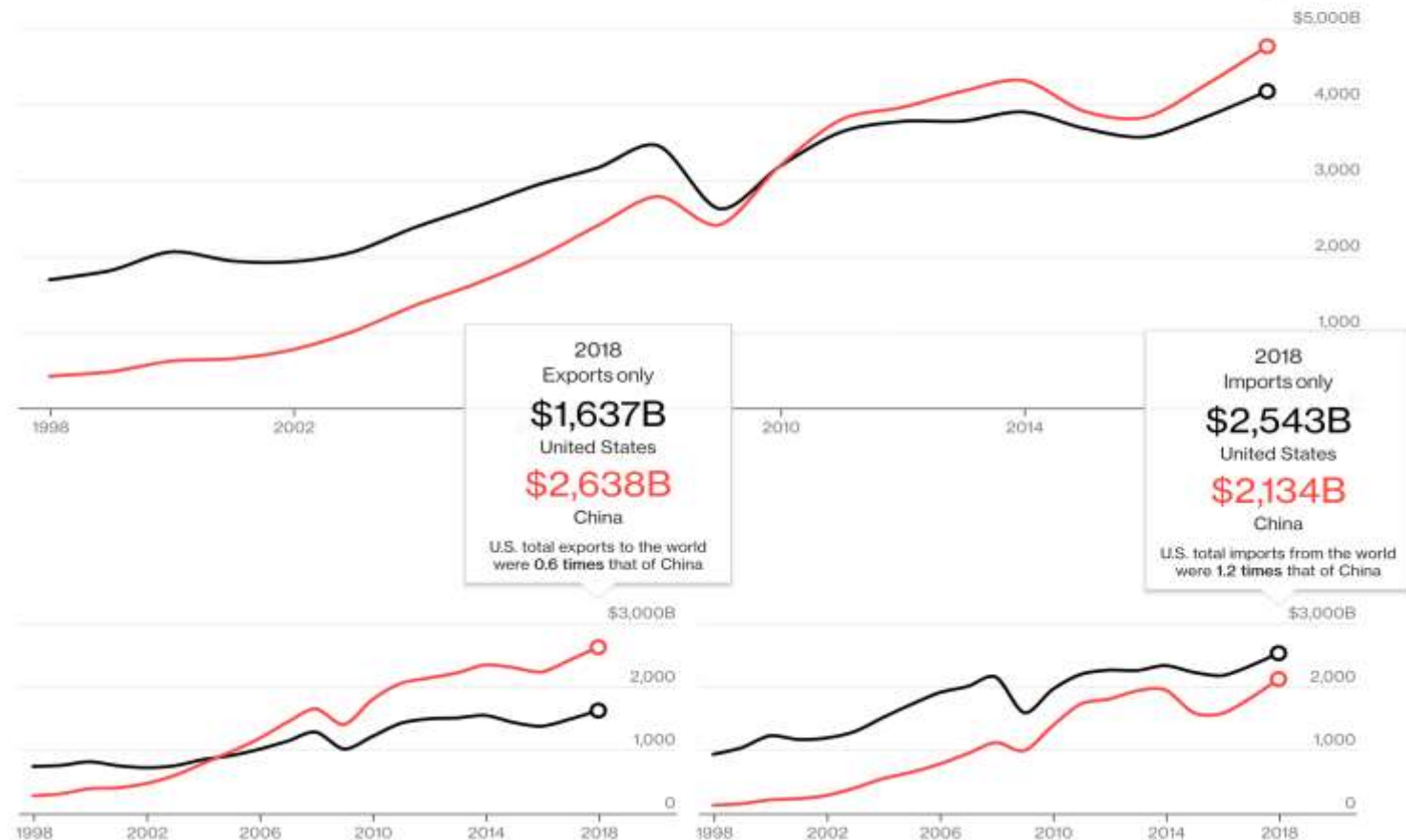
(Percent of World Imports)



Chinese vs. US Volume of World Trade: 1996- 2018

China is already the world's largest trading nation

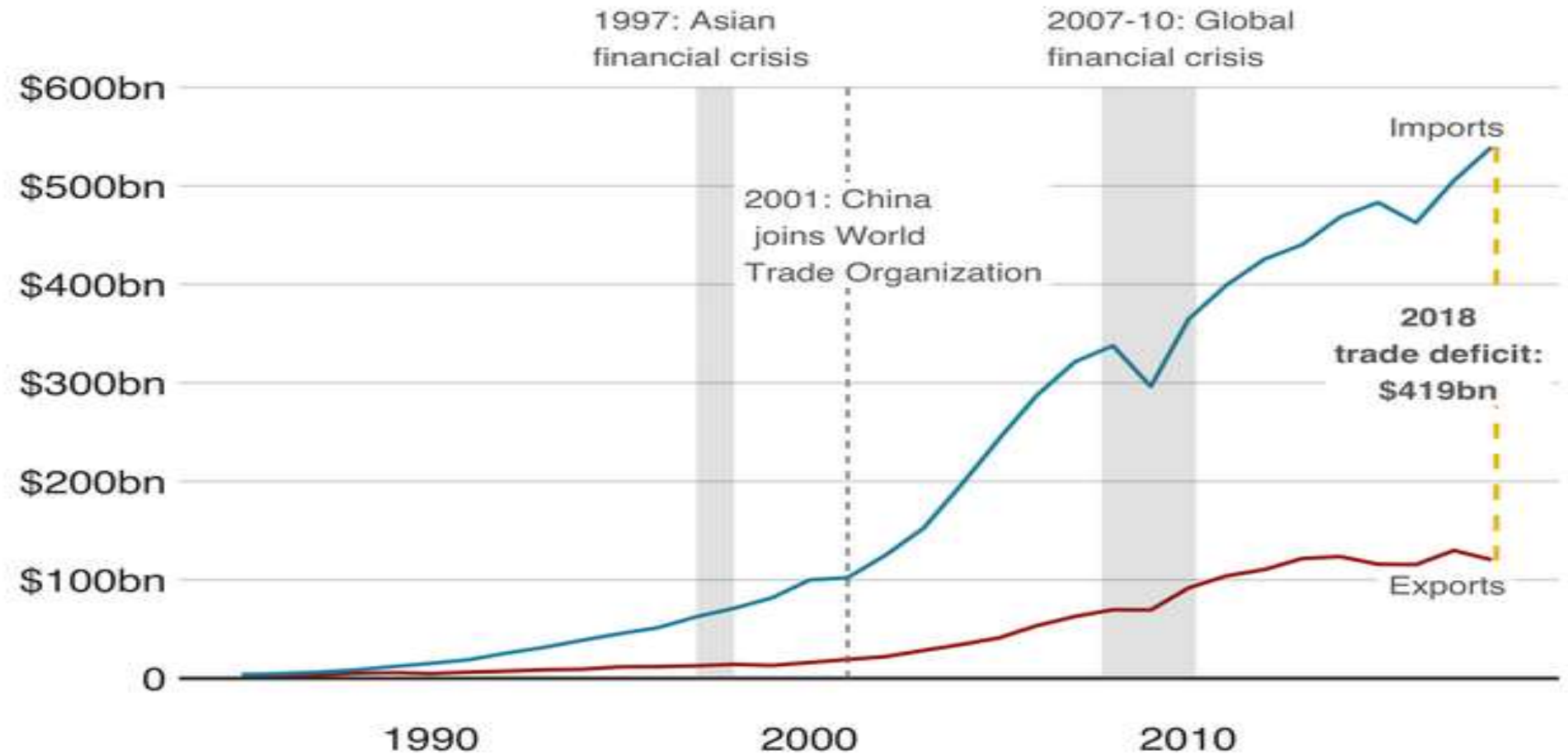
China's exporting prowess has fueled massive trade surpluses and tensions with the U.S. Its competitive advantage in many products is now so entrenched for both local and foreign firms that even the trade war has failed to dent it. A recent survey from the European Chamber of Commerce in China found just 6% of companies polled have moved or are considering moving relevant production out of the country. Meantime, its swelling ranks of middle class consumers mean many companies can switch to targeting sales toward them as tariffs increase.



[Malcolm Scott](#), [Cedric Sam](#): *Here's How Fast China's Economy Is Catching Up to the U.S.* Bloomberg May 12, 2016 | Updated: May 21, 2019, Sources: IMF (via Bloomberg). Additional work by: Christopher Cannon, Michael Keller and Ailing Tan

US Trade Balance with China : 1980-2018

US trade deficit with China has soared since 1985

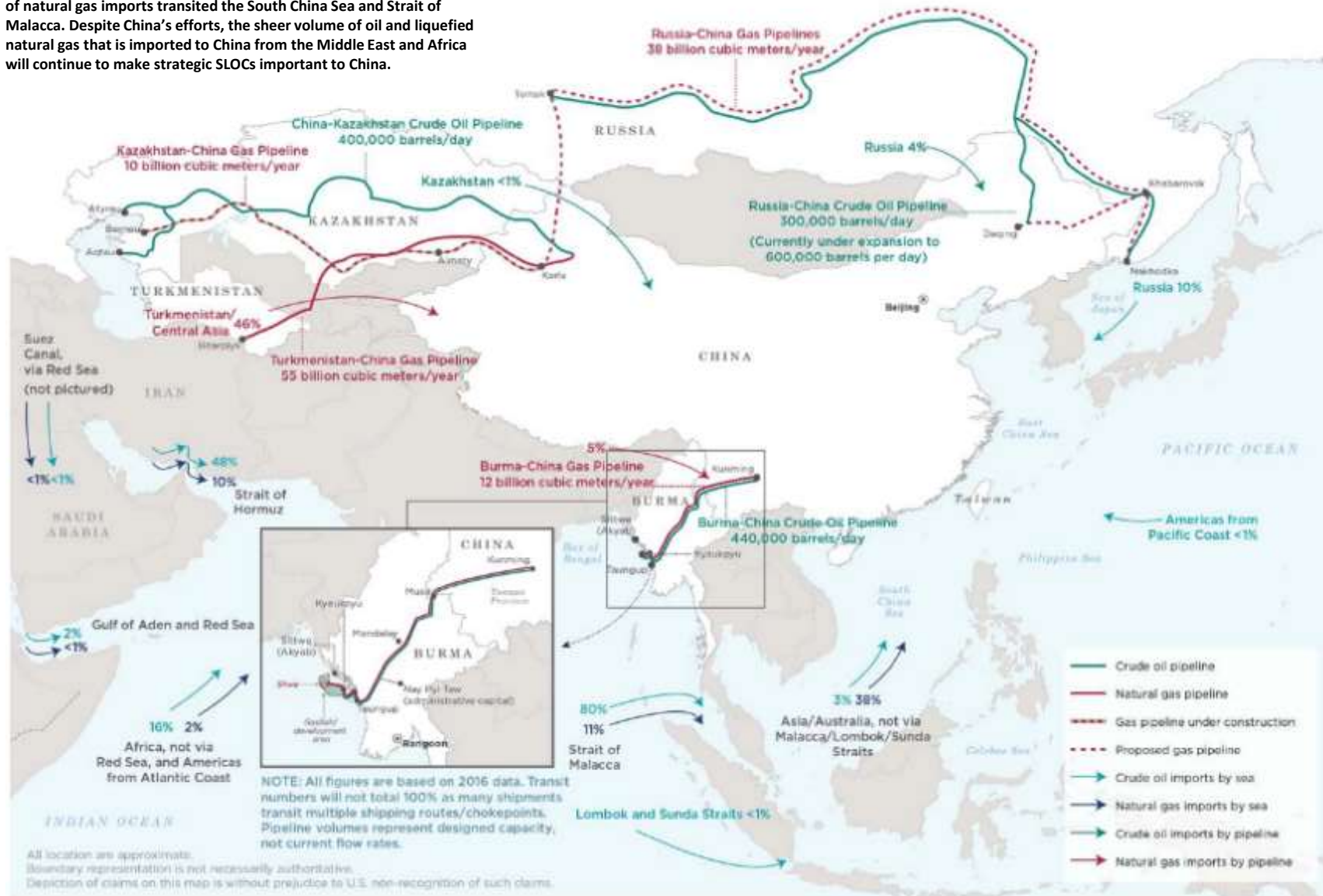


Source: US Census

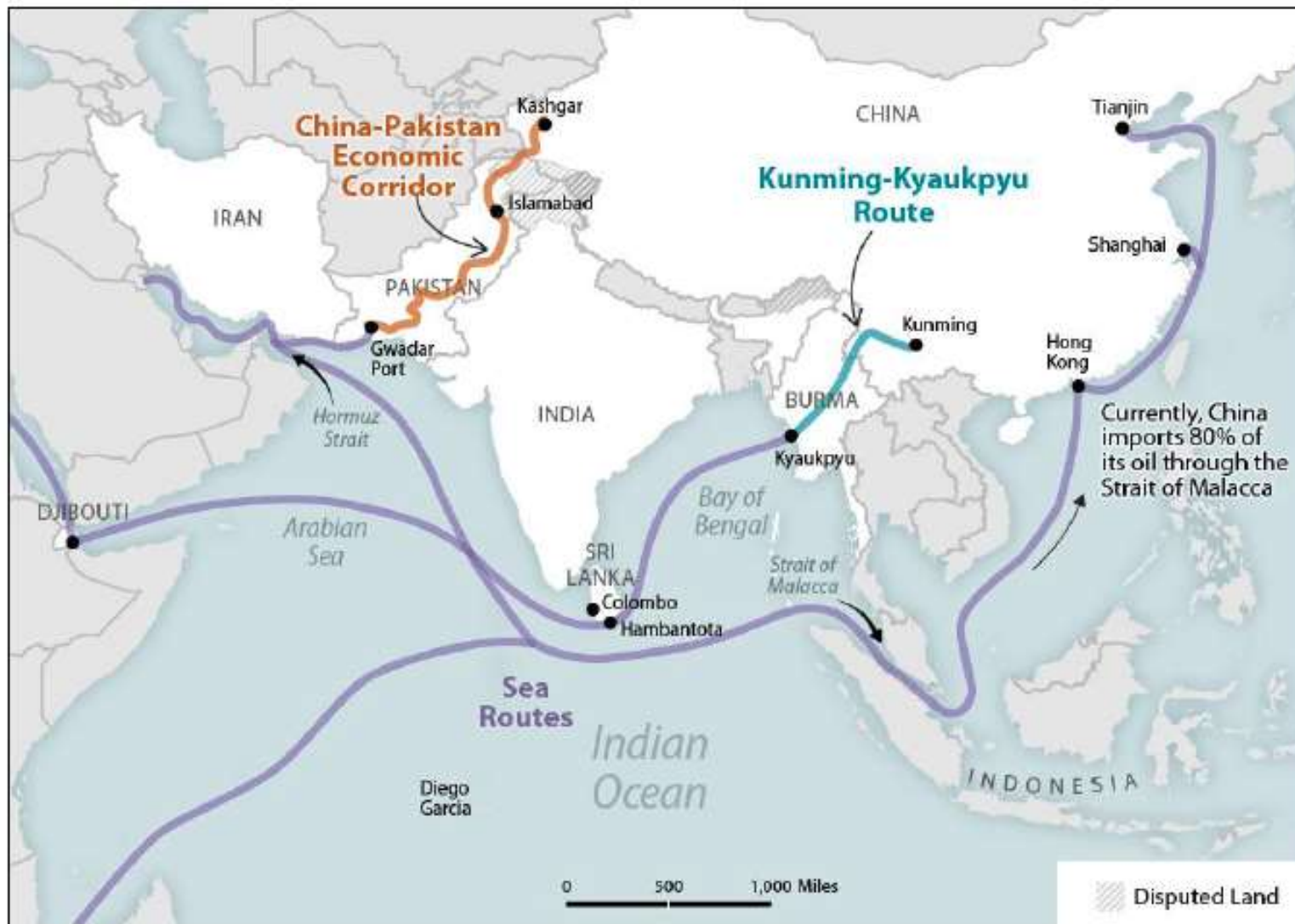
BBC

China's Energy Import Transit Routes

In 2016, approximately 80 percent of China's oil imports and 11 percent of natural gas imports transited the South China Sea and Strait of Malacca. Despite China's efforts, the sheer volume of oil and liquefied natural gas that is imported to China from the Middle East and Africa will continue to make strategic SLOCs important to China.

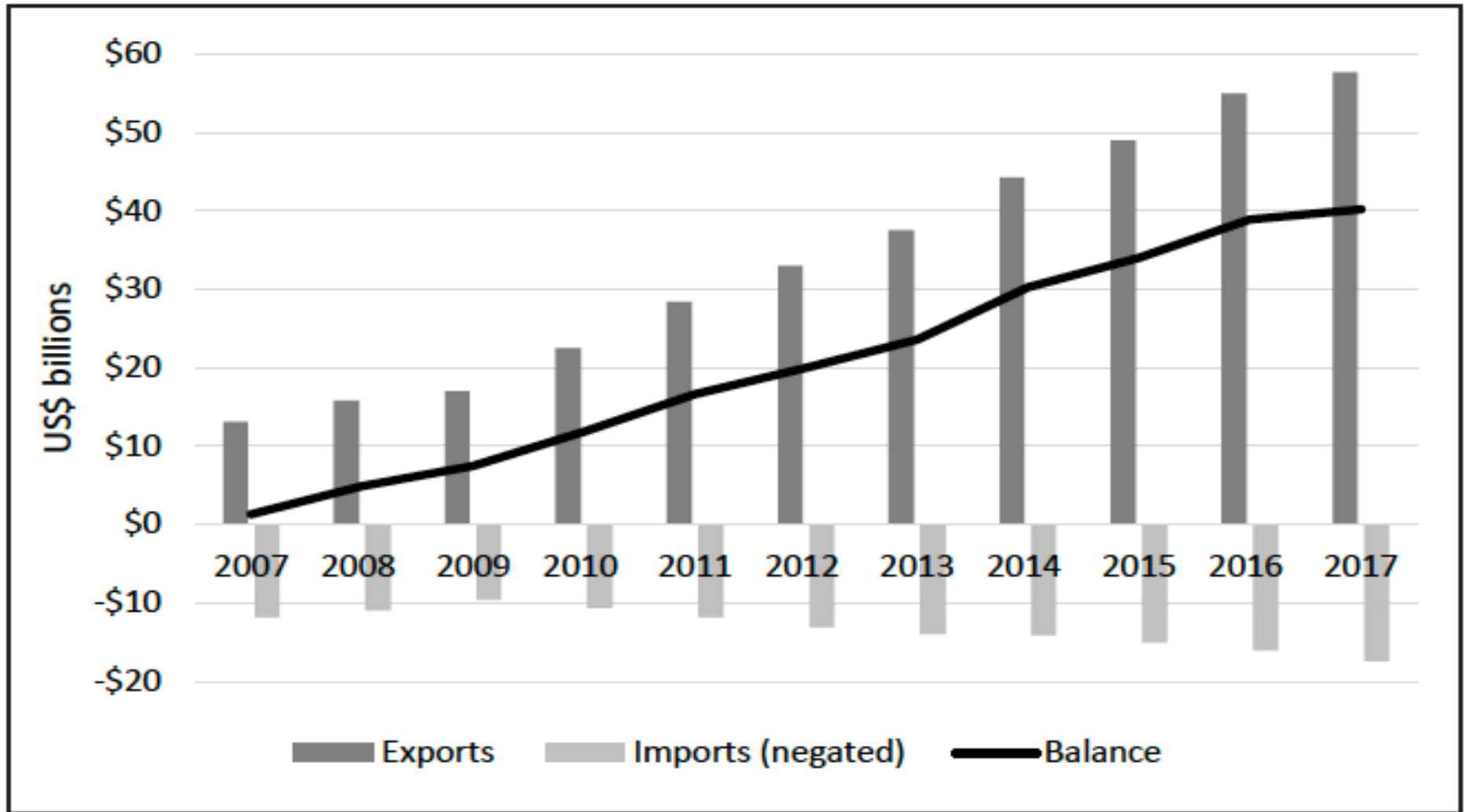


China's Indian Ocean Trade Routes



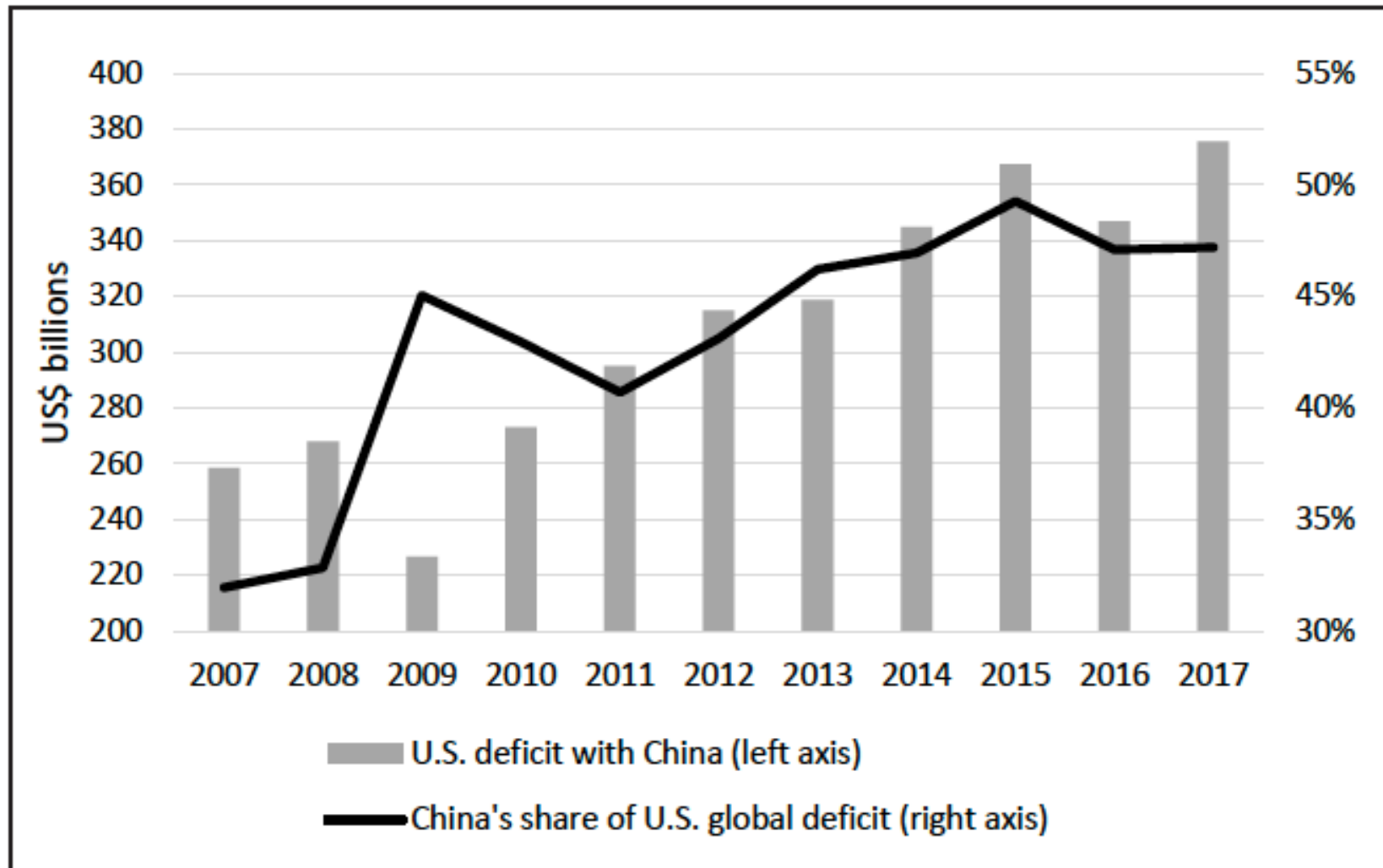
Source: Graphic created by CRS. Map and information generated by (name redacted) using data from the *South China Morning Post* (2017); the Department of State (2015); Esri (2016); and DeLorme (2016).

Positive US-China Services Trade: 2007-2017



Source: U.S. Department of Commerce, Bureau of Economic Analysis, Table 1.3 U.S. International Transactions, Expanded Detail by Area and Country, June 6, 2018.

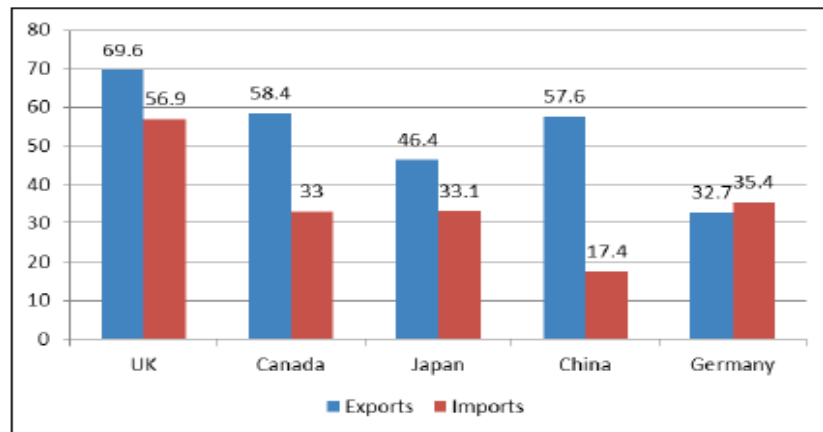
US Trade Deficit with China: 2007-2017



Source: U.S. Census Bureau, Trade in Goods with China.

U.S. Merchandise Trade Dependence on China: 2000-2017

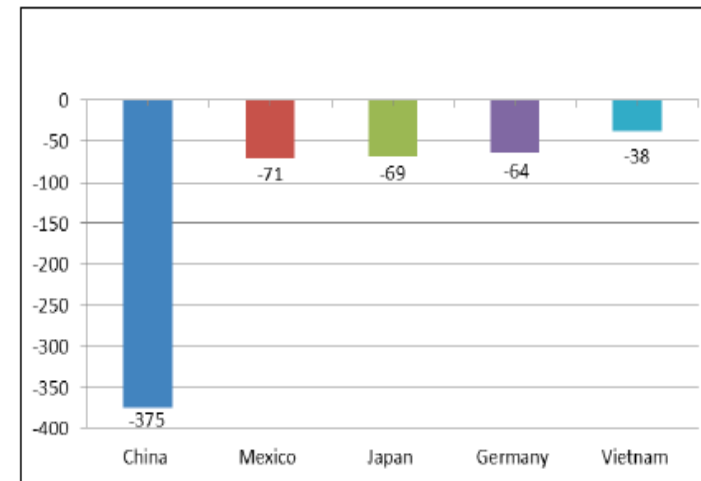
Figure 3. Major U.S. Services Trading Partners in 2017
(\$ in billions)



Source: BEA.

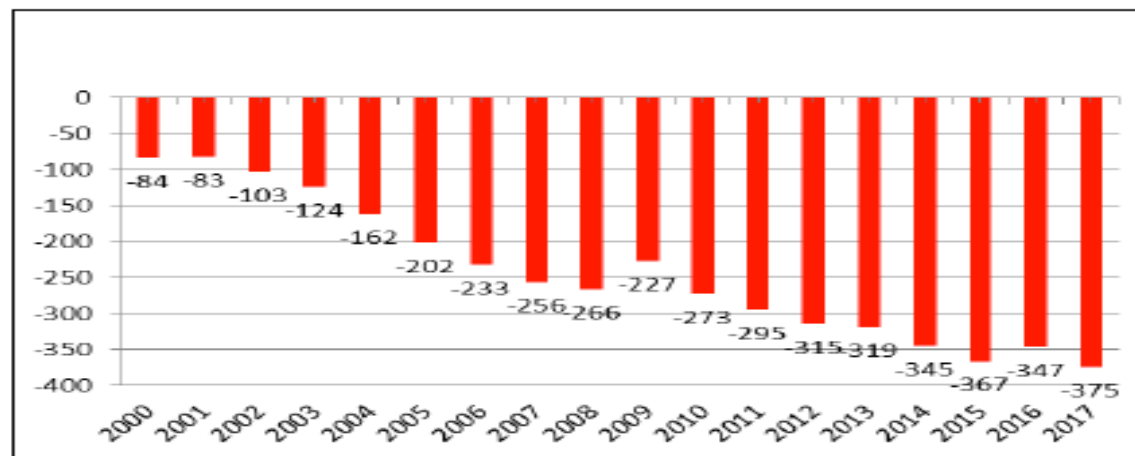
Note: Top five U.S. trading partners in total services trade (exports plus imports) in 2017.

Figure 5. Five Largest U.S. Merchandise Trade Imbalances in 2017
(\$ in billions)



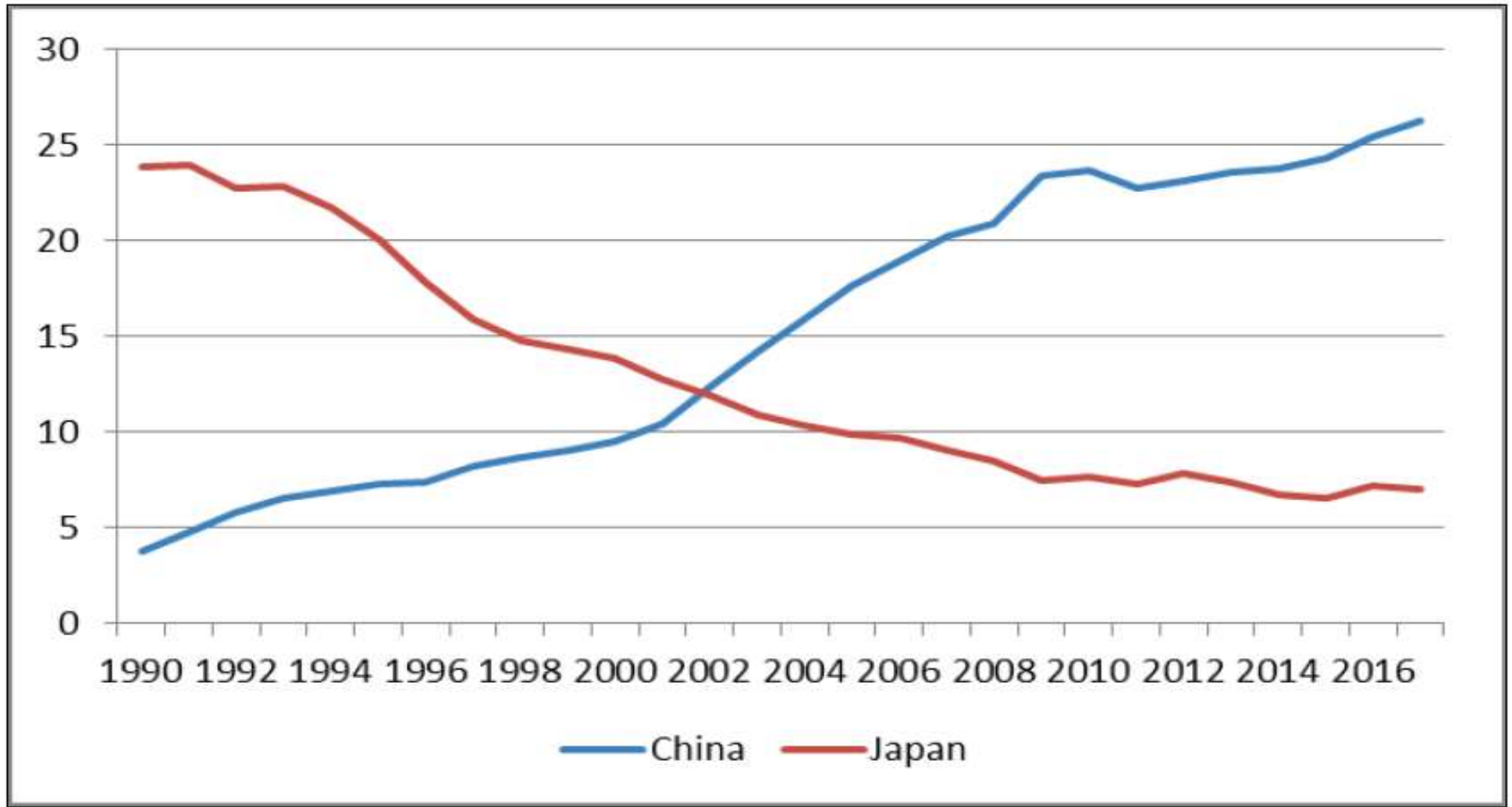
Source: USITC DataWeb.

Figure 4. U.S. Merchandise Trade Balance with China: 2000-2017
(\$ in billions)



Source: USITC DataWeb.

U.S. Shift from Japan to China as % of Total U.S. Manufactured Imports: 1990-2017



Source: USITC DataWeb.