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Trade wars: China fears an emerging united front

Beijing welcomed American disputes with Tokyo and Brussels but now faces isolation as G7 allies begin to co-ordinate policy

Tom Mitchell in Beijing SEPTEMBER 10, 2018

As another fruitless round of [China-US talks to avert a trade war](#) wrapped up in Washington on August 23, foreign officials were arriving in the US capital for a potentially far more consequential meeting the next day. The occasion was an unusual trilateral forum that brings together trade officials from the US, EU and Japan.

Their mission: to combat the allegedly [unfair trading practices](#) by unspecified “third countries”.

When US trade representative Robert Lighthizer and his EU and Japanese counterparts announced [their initiative](#) on the sidelines of last December’s World Trade Organization meeting in Buenos Aires, they did not single out any one country for fostering allegedly “unfair competitive conditions caused by large market-distorting subsidies and state-owned enterprises, forced technology transfer and local content requirements”.

But there was little doubt about the identity of the elephant in the room. As [EU trade commissioner Cecilia Malmstrom](#) said at the time: “There’s no secret that we think China is a big sinner here.”

The trilateral gathering represents a potentially critical shift in the confrontation between Washington and Beijing. Chinese Communist party and government officials are confident they can cope with a [full-scale trade war](#) with the US, which increasingly feels like a foregone conclusion in Beijing. On Saturday, Chinese officials woke up to President Donald Trump’s threat to tax all Chinese exports to the US — worth more than \$500bn last year — within months. On Sunday, they were greeted by a presidential tweet admonishing [Apple](#) to repatriate its China-based supply chain.



Chinese-built cranes are checked before they are exported to the US © AFP

What really keeps them up at night, however, is a potential co-ordinated assault by the Trump administration, EU and Japan on their unique model of Chinese “state capitalism” that has been integral to the country’s economic success over the past 40 years.

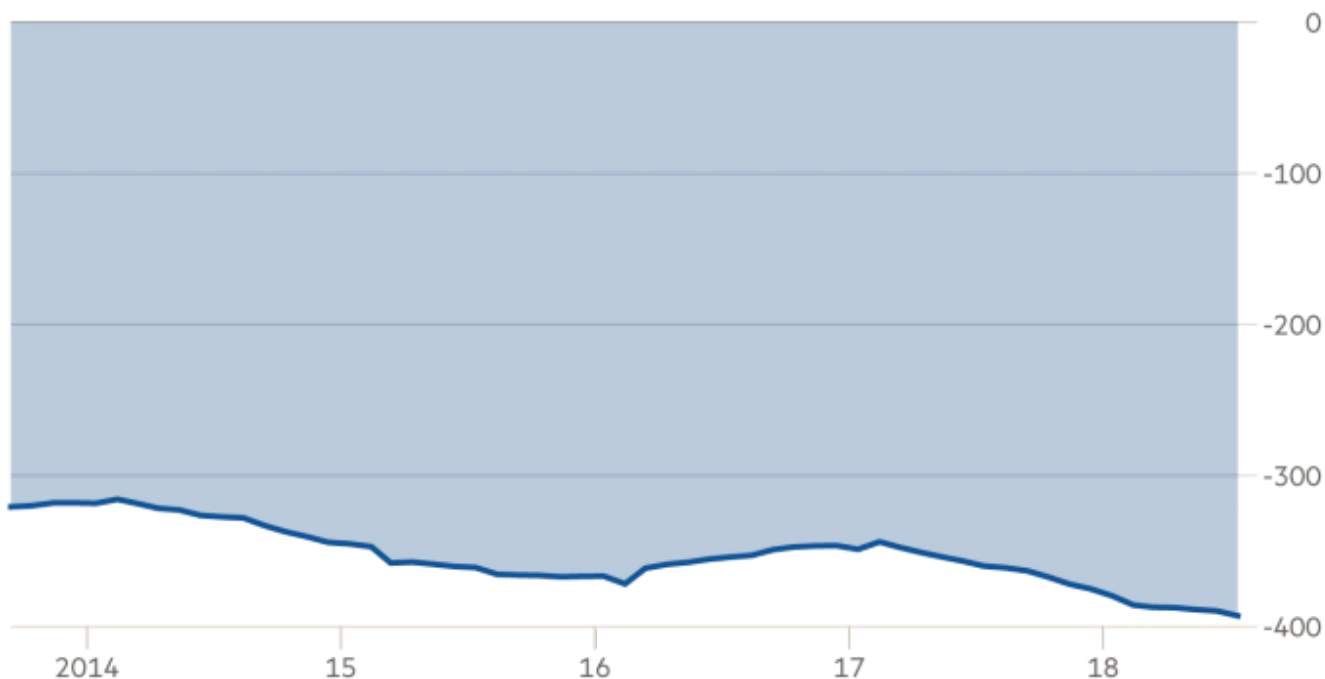
In recent months the EU and Japan have joined forces with the US in WTO complaints against “forced technology transfers” in China through mandatory joint venture structures with local partners. “No country should require or pressure technology transfer from foreign companies to domestic companies through the use of joint venture requirements, foreign equity limitations, administrative review and licensing processes,” Mr Lighthizer, Ms Malmstrom and Hiroshige Seko, Japan’s minister for economy, trade and industry, said in a joint statement in May.

After a period when Mr Trump picked trade fights with any number of countries, Beijing worries that he has stumbled on to a more effective trade strategy that involves isolating China.

“These sorts of moves make the Chinese very nervous,” says Eswar Prasad, a former head of the IMF’s China division who now teaches at Cornell University.

The US goods trade deficit with China continues to grow

Rolling 12-month sum, \$bn



Source: Thomson Reuters Datastream
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In private conversations, Beijing officials say they could not believe their luck when the US president this year simultaneously initiated trade actions against China, the EU, Canada, Mexico, Japan and South Korea. Mr Trump's initial scattergun approach took a lot of heat off Beijing, which is supported by Brussels and Tokyo in a WTO suit challenging US tariffs on imported steel and aluminium.

But since the now [famous photo of Mr Trump](#) squaring off against his G7 allies at their June summit in Quebec, there have been signs that three of the world's four largest trading powers may indeed combine forces to pressure China. In addition to Mr Lighthizer's talks with Brussels and Tokyo, the Trump administration is working to solidify its recent trade truces with the EU and Mexico, and [agree on a revamped Nafta pact with Canada](#).



Wei Jianjun, chairman of Great Wall Motor Co, is also reassessing its plans to export to the US © Bloomberg

Many are sceptical that the US president will succeed in training his fire on China alone. “For that to happen, Trump would have to behave in a very different way,” says one senior European banker. “The Europeans don’t trust him — and they shouldn’t.” His recent threat to leave the WTO, the banker notes, is an example of the kind of erratic behaviour that could rupture any alliance with the EU and Japan, which prefer to work through the multilateral trading body.

Mr Trump’s frenetic summer trade talks with the EU, China, Mexico and Canada have nonetheless added to the [pressures building on President Xi Jinping](#), who a year ago was coasting towards a Chinese Communist party congress that confirmed his status as the country’s [most powerful leader](#).

“In 2017 the mood in Beijing was, ‘everything is going great’,” says one person who has met Liu He, Mr Xi’s [economic tsar](#), and other top Chinese officials in recent weeks. “This spring they thought Trump’s tariff threats were a road bump. Now they know it’s not a road bump and even if Trump dies tomorrow, this problem is not going away. They also realise they have trade problems with Europe.”

When European Commission president Jean-Claude Juncker travelled to Beijing for a bilateral summit in July, he bluntly told premier Li Keqiang that he shared many of Mr Trump and Mr Lighthizer’s concerns about Chinese state capitalism. “His message to Li was we don’t necessarily like Trump’s methods, but it’s not like he’s imagining all this stuff,” says one person who sat in on a meeting between the two men.

For its part, Tokyo has been pleasantly surprised by a Beijing-initiated rapprochement over the past year. According to one Japanese official, a recent spate of [Chinese overtures](#) are all “thanks to Trump”. The official adds: “Trump’s trade policies have been influencing China’s diplomatic stance.”

But while prime minister Shinzo Abe is happy to seize on any opportunity to reduce tensions with Beijing, he is far more concerned about maintaining good relations with his US military ally. “China wants us to join their straightforward criticism of Trump’s trade policies, which we are of course very concerned about,” the official adds. “But we are also basically in total agreement with Trump’s viewpoints regarding market access and other [trade and investment] issues in China.”



Fruit products being processed for export from Anhui province © AP

Whether the Chinese leadership is ultimately confronted by the US alone, or by the US, EU and Japan, is important for Beijing, especially as it continues a campaign against risky financial practices that have slowed investment and economic growth. Yet the Chinese have also begun to conclude that there is much more to Mr Trump’s trade threats than empty bluster.

Mr Xi and Mr Liu have already been caught off guard. After more than a year of playing down [the risks](#), the two men finally woke up in May to the fact that Mr Trump’s repeated threats to penalise China for alleged intellectual property theft and other unfair trade practices were not theatre. That month the US president contradicted his Treasury secretary Steven Mnuchin, who said a trade war between the two countries had been put “on hold”, by announcing his decision to impose punitive tariffs on \$34bn-worth of Chinese industrial exports in early July.

Mr Trump is now poised to authorise a third round of tariffs that will take the total value of affected Chinese goods to \$250bn — about half of [Beijing’s total annual exports to the US](#). “The Chinese should be worried about Trump,” says Steve Bannon, Mr Trump’s former political adviser. “They’ve never had to confront anything like this.”

An increasing number of officials and analysts in Beijing now agree with Mr Bannon, seeing the escalating trade war as just the leading edge of a larger effort by the US to “contain” China. “The risk of China and the US sliding into a new cold war is increasing,” says Tu Xinquan, a professor at Beijing’s University of International Business and Economics. “It will be a nightmare for China, the US and the world.”

Wang Chong at the Charhar Institute, a Beijing-based think-tank, says China's current problem in the US is not just related to Mr Trump: "Both the Republican and Democratic parties have reached a consensus that they should try to curb China's development."



Former White House policy adviser Steve Bannon: 'Trump may be flexible on so much stuff, but the hill he's willing to die on is China' © Reuters

In a series of authoritative articles in party-controlled publications, Chinese officials have recently warned that the country faces a new era of "strategic containment" orchestrated by the US.

"In the wake of the US defining China as a 'strategic competitor', Sino-US relations will undergo a profound readjustment," Long Guoqiang, vice-president of the State Council's Development Research Centre, wrote in an August 29 article in the People's Daily. "In the past, the Soviet Union and Japan were hampered by the US. With the rapid development of China's economy and comprehensive national strength, the US has fully turned its attention on China."

"It's getting more and more obvious that the Trump administration is determined to contain China," adds Shi Yinhong, a foreign affairs expert at Renmin University in Beijing. "I think the next round of tariffs is inevitable. The trade war will last for quite a long time."



Liu He, China's vice-premier and Xi Jinping's economic tsar © Bloomberg

A few days after Mr Long's article appeared, an unsigned commentary in *Qiu Shi*, a Communist party journal whose title translates as *Seeking Truth*, also accused the US of seeking to "curb the development of developing countries, especially China".

Even people who are critical of China's trade and economic policies agree that such official interpretations of Mr Trump's ultimate goal are probably correct. They say the only trade deal he would accept from China is one Mr Xi could not possibly offer, because it would include concessions on how the party manages everything from industrial policy to state-owned enterprises and the renminbi. Others argue that Mr Trump's ideal outcome is in fact no deal at all, so he can implement long-term tariffs on all Chinese exports to the US in a bid to bring about a radical overhaul of global supply chains.

"People in the administration now understand that Trump may be flexible on so much stuff, but the hill he's willing to die on is China," says Mr Bannon. "Trump's focus is shifting the supply chains out of China."

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In one indication that this strategy may be working, on August 31 [Ford](#) announced that it was [cancelling plans](#) to export China-made Focus vehicles to the US from next year. The vehicles would have been subject to a 25 per cent tariff on Chinese car exports imposed by the Trump administration in August. Great Wall, China's most successful domestic SUV manufacturer, is also reassessing its plans to export to the US.

"The US national security establishment has rightly identified China as a strategic competitor," says another person who advises Chinese policymakers. "Their strategy is to contain China through trade."

The enthusiasm with which Mr Trump has slapped tariffs on Chinese exports this summer

‘The risk of China and the US sliding into a new cold war is increasing. It will be a nightmare for China, the US and the world’

Tu Xinquan, University of International Business and Economics in Beijing

has, contrary to the tough rhetoric of official party publications, contributed to a sense of unease among officials in Beijing who have their hands full with difficult financial reforms.

In such circumstances a trade war with the US is unwelcome but also viewed as unavoidable — at least in the short term — by an increasing

number of officials and their advisers.

For the time being, they believe all they can do is to try to limit the inevitable damage. “We had hoped that the escalating trade war would force US companies to talk sense into Trump but it’s not working,” says Prof Tu. “So we need to reconsider our retaliatory measures, which shouldn’t be too aggressive. If Trump wants to be a mad man, then so be it.”

Additional reporting by Xinning Liu in Beijing and Robin Harding in Tokyo

This article has been amended to correct the Canadian city where this year’s G7 summit was held.

Corporate ties US executives call for a change in China’s mindset

A deterioration in its traditionally friendly relationship with US corporate leaders and Wall Street financiers is adding to Beijing’s sense of isolation. While US business is strongly opposed to President Donald Trump’s tariffs, they are equally frustrated by the market access barriers and other restrictions they face in China.

According to two people briefed on the last round of Sino-US trade talks in August, Treasury undersecretary David Malpass referred his Chinese counterparts to an opinion piece by former AIG chairman Hank Greenberg in the Wall Street Journal.

Mr Greenberg, a longtime friend of Chinese vice-president [Wang Qishan](#), wrote that “discriminatory treatment of foreigners is embedded in the Chinese bureaucracy — in government policies, in regulatory procedures laden with obstacles and delays, in structural impediments such as turnover in government agencies resulting from forced early retirements, and in the mindset of Chinese officials”.

“This all needs to change,” Mr Greenberg added. “China cannot expect to continue receiving favourable trade and investment terms in foreign markets when it is unwilling to reciprocate . . . The US is right to press to level the playing field.”

The Chinese trade delegation, led by commerce vice-minister Wang Shouwen, did not react well to such critiques during a meeting with US business executives. “[Wang’s] was the exact wrong message.”

Letter in response to this article:

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