US-CHINA TRADE TENSIONS

IN THIS ISSUE

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Documenting the wartime viewpoints and diverse political sentiments of the twentieth century, the Hoover Institution Library & Archives Poster Collection has more than one hundred thousand posters from around the world and continues to grow. Thirty-three thousand are available online. Posters from the United States, the United Kingdom, Germany, Russia/Soviet Union, and France predominate, though posters from more than eighty countries are included.
By agreeing to restart stalled trade talks at their meeting in Osaka last week, President Trump and his Chinese counterpart Xi Jinping averted a new round of punitive measures in a trade conflict that’s moving into its second year.

But the respite is likely to be short-lived. The history of international conflicts over trade and economic matters suggests the outcome of the current trade tensions could be just the earliest stage in China’s campaign to replace the current rules-based trade order with a system aligned with Chinese mercantilist policies and practices.

Trade wars arise when one country’s pursuit of economic advantage goes beyond the bounds that other countries are willing to accept as legitimate forms of competition under the prevailing political and legal philosophies of the time. Whether conducted through commercial means such as tariffs or military action, trade conflicts are usually resolved when an international consensus is reached that either accommodates malign trade policy or curtails unfair competitive practices.

It’s a time-consuming, political, and inherently unpredictable process. Trade conflicts can last for years, or even decades, and often bring about significant—and unexpected—realignments of international power. Power shifts often hinge on the logistics and maritime capabilities of trade adversaries, and the importance of logistics increases as trade conflicts drag on. In the hands of mercantilist countries like China, logistics networks provide a physical presence from which to exert national power through the structures of international trade, a set of practical tools to acquire the economic influence needed to reward or coerce partners and adversaries alike.

Perhaps the best example is the commercial expansion of the Dutch Republic from the late sixteenth century to the late eighteenth century. In one of history’s biggest trade upsets, the Dutch displaced Portugal as the dominant player in the spice trade between Western Europe and Southeast Asia, akin to the competition today in semiconductors.

Pooling their funds through a financial innovation called the joint-stock company, the Dutch deployed fleets of ships that were bigger, better equipped, and better armed than the commercial vessels of much larger countries. The Dutch East India Company, known as the VOC from its Dutch name, the Vereenigde Oost-Indische Compagnie, was the prototypical state-backed entity, operating under a government charter that permitted the ostensibly commercial company to build forts, appoint governors, billet soldiers, and make treaties with foreign countries in the name of the Dutch States-General.
For nearly 200 years, the VOC flag flew over a tightly controlled trading empire run from a network of permanent trading posts centered on Batavia, the site of modern-day Jakarta in Indonesia. The VOC hegemony did not end until the British victory in 1784—in the last of four Anglo-Dutch Wars—secured the right to free trade with the Dutch East Indies for British merchants.

While the current trade tensions stem from the Communist Party of China’s pursuit of its own pernicious revival of mercantilism—the coercive, beggar-thy-neighbor economic policy favored by hegemonic regimes governed by political absolutism—China has a long tradition of protecting her domestic markets from foreign economic penetration. America’s early trade with China in the post-Revolutionary period, for example, was confined to the Thirteen Factories, warehouses where Westerners did business with the Cohong, the Chinese agents the emperor authorized to deal with foreigners. Even at the height of its power, and with no reluctance to use force, the VOC was limited to trading with the mainland from Formosa.

Today’s trade war is the latest episode in the effort to conduct free trade with China. In fairly short order, the US-China conflict has progressed from an effort by President Trump to levy tariffs, ostensibly to reduce the US trade deficit with China, to a fundamental conflict between the world’s two largest economies over the nature and stewardship of the global trade order.

At issue is whether China will substantively abandon its long-standing policy of illicitly or forcibly obtaining intellectual property from American and other Western companies, often by requiring that Western companies wishing to do business in China enter into joint ventures with Chinese partners, which become competitors with unnerving regularity. Among other trade-related concerns are China’s financial subsidies and regulatory support to Chinese state-owned companies that operate as the low-cost predatory producer in virtually every industry. This year, the United States restricted US companies’ sales of some semiconductor and IT equipment to Huawei, which manufactures digital hardware and networks that the United States says the Chinese government can utilize for cyber-espionage.

China is unlikely to change course. No longer able to offer lowest-cost labor, Chinese companies must move into higher-value businesses, and the “China 2025” plan to overtake the United States in key technologies requires a steady stream of innovation. But China faces an innovation gap, lagging far behind the United States and other Western countries in terms of triadic patents—the simultaneous application for legal protection of an idea in Japan, the Europe and the United States, a costly process that reflects the originality and potential value of ideas.

Without a reliable flow of innovation, China will not be able to fulfill its ambitions, and it is likely to retaliate as the United States moves to restrict its economic oxygen supply. To do so it will look abroad—to the global network of ports that its state-owned shipping and logistics companies have quietly built during the past decade.

China powered its economic rise by developing port, logistics, and shipping capabilities that enabled its manufacturers to offer Western companies one-stop shopping—cheap production and reliable distribution. As Chinese maritime expansion accelerated in the past decade, Chinese state-owned enterprises won long-term contracts to operate and develop ports for financially weak Western countries in both developed and emerging markets.

The main builder of China’s port network is China COSCO Shipping Corporation Limited. A twenty-first-century version of the VOC, naval experts describe COSCO as the logistics branch of the Chinese Navy. The company manages China’s primary port in the West at Piraeus, Greece, where it installed a Huawei IT network soon after taking over. As the dominant member of the Ocean Alliance, one of three global shipping consortiums, COSCO heads the only logistics network likely to have guaranteed access to Chinese manufacturing ports if the trade war heats up. COSCO’s partner in the alliance is CMA CGM, a French shipping line based in Marseille that received significant Chinese loans in 2015, and earlier this year bought one of the largest distribution companies in the United States The Ocean Alliance is working so well that its members met in Hainan in January and renewed their pact for a decade.
COSCO and other Chinese companies now control both ends of the Panama Canal, and strategically located ports in Brazil and Southern Europe, on both coasts of Africa, and across the Indian Ocean. This gives China a territorial presence—and political and economic leverage—that countries have typically achieved through military conquest, and a global maritime network that’s unprecedented for a rising power.

In recalling the ping-pong diplomacy of the 1970s during his meeting with Trump in Osaka, Xi provided an apt metaphor for the likely course of the trade talks: lots of back and forth. Prolonged discussion will give China time to utilize the coercive power of its commercial trade network. Ports in the Europe are likely to be the focus of Chinese efforts to ensure a backup supply of IP. “Innovation Centers” are planned near several Chinese-controlled ports, and the port of Marseille, CMA CGM’s base, is encouraging development of new data centers when Huawei’s undersea cable comes ashore there later this year. Italy’s recent agreement to have Chinese companies develop the port of Trieste will give Chinese SOEs (state-owned enterprises) close proximity to a leading naval shipbuilder, as well as innovative technologies for power systems for the marine and energy markets.

It will be virtually impossible for the United States to dislodge China from most ports where it has a presence. In most cases, Chinese control is based on long-term leases that would most likely be upheld in Western courts, and host governments have little incentive to eject Chinese SOEs that are delivering revenue gains, often by routing Alliance ships to Alliance-run docks. If trade tensions intensify, Chinese shipping companies could threaten embargos or other sanctions on countries and companies that side with the US economic leverage could help China prevent companies from moving manufacturing operations out of the country, by exposing companies or their home governments to pressure from Beijing; China has already forced companies to stop identifying Taiwan as a separate country to avoid commercial harassment of their operations in mainland China, and supply-chain control opens new avenues of coercion.

Control of ports presents China with opportunities to expand the reach of Chinese governance. This could occur by asserting the jurisdiction of Chinese commercial courts at ports under Chinese control, in the manner of nineteenth-century “treaty ports” where foreign law applied on Chinese territory. The Dutch States-General empowered the VOC to make treaties, and while Chinese logistics SOEs are not yet formally conducting matters of state, it might not be long before one attempts to use China’s maritime network to export Chinese governance. The unrest in Hong Kong about a law that would allow China to extradite people from the city to the mainland justice system shows the CCP’s desire to rapidly assert Chinese legal control. As soon as COSCO achieved control over the Piraeus port company, it changed the bylaws to allow board meetings to be held in China instead of Greece. And China launched a new commercial court earlier this year in Shenzhen as a venue for Chinese companies engaged in Belt-and-Road projects. Claiming that Chinese law applies to legal proceedings held within a foreign port might not be far off.

To counter China’s mercantile expansion, the United States will need to restore commercial maritime capabilities it has ignored during China’s economic rise. Top priority needs to be placed on securing adequate logistics vessels for the military. Eventually, the United States should work with Japan and other allies to organize commercial shipping resources to counter potential Chinese threats of disruption, and help companies move production out of China, and beyond the reach of China’s supply-chain power. While limiting direct trade in sensitive tech products, the administration could review whether the extension of the Ocean Alliance pact is warranted on national security grounds. Longer-term, the United States will need develop new alliances to enable investment in both civil and military infrastructure in the Pacific. The most pressing issue is the bankruptcy of a South Korean shipyard near Subic Bay; reports that two Chinese companies are trying to buy the facility sparked a backlash in the Philippines but the outcome is not settled.

Chinese control would jeopardize US access to Subic Bay. US naval experts have already warned that US vessels should no longer dock at Chinese-controlled ports due to the risk of being subjected to cybersurveillance by Chinese systems, and some are concerned that Chinese commercial ships might be carrying equipment that could jam US military radar and communications in the event of a confrontation.
A year into the trade conflict the stakes have become clear: the United States faces a threat unprecedented in its history—a nuclear-armed adversary running a political system antithetical to the US constitutional republic, dedicated to replacing the rules-based trading order with its own mercantilist hegemony, which has major economic clout and global maritime domain awareness from a fleet of nearly 400 commercial vessels sailing the world’s oceans at all times as China’s ships of state. China doesn’t have the naval power to challenge the United States militarily, and likely won’t achieve naval parity any time soon. But in command of a global maritime network that it has only started to mobilize, China is already more of a menace to US national security and economic interests than the Soviet Union, and the ongoing trade tensions portend a geopolitical competition that is not likely to be resolved by a tariff deal alone.

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When “Trade Wars” End Badly

By Gordon G. Chang

“I think we’re going to be strategic partners,” said President Donald Trump on June 29 at his Osaka G-20 press conference, in response to a question from Olivia Qi Zhang, a reporter for Caixin, the Chinese news organization. “I think we can help each other. I think, in the end, we can—if the right deal is structured, we can be great for each other.”

In Osaka, Trump laid out the case for optimism about ties between China and the United States. And why should he not be hopeful? He had just made two important concessions to Beijing. First, the president did not, as he had threatened, exercise his authority under Section 301 of the Trade Act of 1974 and impose additional tariffs on $325 billion of Chinese goods. Second, he promised to allow sales of American products to Huawei Technologies despite its inclusion on the Commerce Department’s Entity List.

Huawei’s addition to the list, effective May 16, was close to a “death sentence” for the world’s largest manufacturer of telecommunications equipment. As a result of Commerce’s action, no American company, without prior approval from the Bureau of Industry and Security, may sell or license to Huawei products and technology covered by the US Export Administration Regulations.

Due to Trump’s favors to Beijing, almost all analysts expect some sort of trade deal with China. Yet agreement is by no means assured. After all, both sides at the end of April were close to inking a comprehensive pact—Beijing and Washington were “95 percent there” according to the president—but in the beginning of May, Chinese trade negotiators withdrew commitments across the board, angering Trump and leading him to impose Section 301 tariffs on $200 billion of Chinese goods.

In reality, a trade deal will be difficult to reach, especially because Chinese ruler Xi Jinping is pushing China back to a state-dominated economic model, while Washington demands a more open one, the architecture Beijing promised when it acceded to the World Trade Organization in December 2001. Xi, however, apparently believes he will not be able to realize his outsized ambitions unless he can shut off China while, at the same time, obtaining access to other markets. Beijing and Washington are promoting two irreconcilable visions of that country’s future.

If this were not bad enough, Xi has, for reasons relating to Communist Party politics, raised the stakes by elevating commercial disputes into questions of national sovereignty. China’s response to Trump’s tariffs has been to impose tariffs of its own on US goods and go on a rhetorical bender. In May, state media issued a stream of belligerent, hostile, and warlike statements. For instance, the authoritative People’s Daily carried a May 13 piece by a sister publication that declared a “people’s war” on the United States. The official Xinhua News Agency on May 25 ran a commentary stating that China’s economic system is a “core interest” that the United States is attacking. In Communist Party lingo, a “core interest” is nonnegotiable and can be defended with force.
The official media blast makes it almost appear that Xi Jinping does not want a trade deal. Yet whether there ultimately is one or not, American companies are beginning to move factories from China. For one thing, Xi is squeezing foreign businesses out with discriminatory policies favoring state enterprises.

Second, escalating trade friction is convincing the business community that disagreements will continue for a long time. As Joseph Foudy of New York University Stern Business School told CNN, it is not the additional tariffs that are motivating companies to exit China. “It’s the uncertainty that drives you to look abroad because you can’t put a price on that,” he said.

Despite what Chinese officials call “decoupling,” there will still be a high volume of trade between the two countries. Many, therefore, think economic ties will continue to stabilize relations. Trade and investment have often been called the “ballast” of Sino-US ties.

Perhaps they will no longer be. “Does trade increase or decrease the likelihood of conflict?” Samuel Huntington, the great Harvard political scientist, asked in his landmark work, The Clash of Civilizations and the Remaking of World Order. “The assumption that it reduces the probability of war between nations is, at a minimum, not proven, and much evidence exists to the contrary.”

As many have now pointed out, high levels of trade in the first years of the last century did not prevent the First World War. As Huntington, building on the work of others, pointed out, what is important is expectation. “Economic interdependence fosters peace,” he wrote, “only ‘when states expect that high trade levels will continue into the foreseeable future.’” If, however, trade partners “do not expect high levels of interdependence to continue, war is likely to result.”

Of course, war does not inevitably result when countries believe they will delink their economies. Yet the threshold for the use of force will drop when Americans believe China poses an existential threat.

Beijing, unfortunately, continually provides evidence that it is America’s enemy. In April of last year, for instance, the Chinese military, from its base in Djibouti, lasered a C-130 Hercules cargo plane, causing eye injuries to two military pilots. American planes are continually lasered in the East China Sea by Chinese forces. Furthermore, last year sonic waves caused brain injuries to American diplomats at the Guangzhou consulate. Because the Communist Party runs a surveillance state, Chinese officials either were the perpetrators of this crime or complicit in it. Soon, Americans will ask why they should trade with a state that uses the proceeds of commerce to harm their service personnel and diplomats. Beijing is leaving its most important trading partner no choice.

So what will be the result of the US-China trade war? Commerce and investment between the United States and China will decline, friction between the two countries will soar, and people will reread The Clash of Civilizations.

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Demystifying Sino-US Decoupling

By Michael R. Auslin

“He’s a New York real estate developer,” a nonpolitically involved acquaintance argues, explaining that President Donald Trump knows that any deal as complex as the one he is trying to negotiate with China over trade will take time, “even years.” That explanation may be as valid as any of the ostensibly more informed takes by professional policy watchers. It also is a useful caution against placing artificial, media-driven timetables on what is turning into the most significant policy showdown between Washington and Beijing since the normalization of diplomatic ties forty years ago.

Negotiations between American and Chinese officials are a drawn-out affair because Trump has zeroed in on a problem a generation in the making. At one level, Trump’s trade war is upending four decades of unequal US-China economic relations that have helped fuel China’s modernization in the post-Mao Zedong era. Given that, at least since the death of Mao, the Chinese Communist Party (CCP) has based its legitimacy on Chinese economic development, any threat to continued growth carries political implications that cut to the heart of CCP rule. It is hard to think of any other issue that has the potential to undermine the CCP’s overall national strategy.

At a higher level, the trade war is over the soul of the global trade regime, with Trump acting on his election-trail promises to reconstruct the international economic architecture that he believes has devastated the American heartland. With the world’s two largest economies sparring over trade, whatever agreement they come up with will have repercussions across the globe. Hence, Xi Jinping’s claim to the World Economic Forum at Davos in January 2017 that China was the new guardian of free trade and the international order.

What Beijing really fears is the decoupling of the United States and China, on both the economic and political fronts. Chinese scholars and officials claim that Trump’s real goal is to contain and weaken China by crippling its economy. Tariffs that lead to lowered exports and a decoupling that sees supply chains and manufacturing shift away from China is the CCP’s great fear. While it is hard to imagine a complete decoupling, given the interconnected nature of global supply and production, economic figures already show some manufacturing moving out of China in response to higher costs, which is something that has been brewing for years, given the maturation of the Chinese economy. Yet Beijing believes that Trump is attempting to accelerate this process, even if it means imposing pain on domestic US producers.

Such economic decoupling means greater isolation, to Chinese officials. While they have opened up a new geo-economic front with the One Belt One Road initiative to link Eurasia to China, the specter of China and America drifting apart is, perhaps counterintuitively, of great fear to the CCP. Much of Chinese strategy since 1979 was to keep the United States as close as possible, giving it an “ownership stake” in China’s success, whether economic or political. Washington obliged by fully integrating Beijing into the global system, whether at the United Nations and World Trade Organization, or through high-level Sino-US diplomatic exchanges. While the American goal was to get Beijing to buy into what is termed the “rules-based international order,”
the Chinese saw it as a way to circumvent pressure Washington might put on Beijing’s foreign and even domestic policies, while abetting the CCP’s goals of rapidly modernizing China’s economy.

Hence, the worry in Beijing that, as it faces a naturally slowing economy, as it responds to increased domestic unrest whether in Xinjiang or Wuhan, and as it looks out at a more activist Japan and India, that it now also faces a political decoupling from the United States that will result in less favorable US policies. The Trump administration’s push against Huawei, moderately blunted but not repealed; its increased activity in the South China Sea; and its pushback against endemic Chinese cyber espionage and attacks, all add up for Beijing to a period of intensified Sino-US competition.

The current trade tensions are thus both a major issue on their own, as well as part of a much larger reordering of Sino-US relations. The current disequilibrium is likely to continue regardless of whether Trump comes to an agreement with Chinese president Xi Jinping over trade or is defeated in reelection in 2020. Large segments of both US political parties are dissatisfied with relations with China and are demanding change. The bitter trade dispute has already developed a feedback mechanism into diplomatic relations, increasing tensions and resulting in greater jockeying for position around Asia. Above all, Chinese officials and scholars are warning that Trump’s protectionism and a war of civilizations risk major conflict. In attempting preemptively to place blame on the White House for destabilizing the world, Beijing is signaling the degree to which it fears that today’s tensions will lead to a weaker, poorer, and more isolated China.

**POLL: What are the likely results of current US-China trade tensions?**

- Both sides will meekly and reciprocally back off.
- The trade war will shortly end with mild Chinese concessions.
- Trump will radically redefine trade in America’s favor.
- Tensions will escalate into a destructive, full-bore trade war.
- Commercial tensions will lead to military incidents and possible war.

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Discussion Questions

1. Since its capitalist reforms, has China ever given concessions to any trading partner?

2. Will growing tensions make China’s Asian neighbors more or less friendly to Beijing?

3. To what degree does China have the ability to stir up trouble through surrogates like North Korea and Iran?

4. Is there now a new informal alliance of China, Russia, Iran, Turkey, and North Korea?
Suggestions for Further Reading

- Andy Rothman, “China’s accession to WTO has been a boon, not an error,” *Financial Times* (February 15, 2018). [https://www.ft.com/content/9ebf9e36-1271-11e8-940e-08320fc2a277]
Military History in Contemporary Conflict

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Working Group on the Role of Military History in Contemporary Conflict

The Working Group on the Role of Military History in Contemporary Conflict examines how knowledge of past military operations can influence contemporary public policy decisions concerning current conflicts. The careful study of military history offers a way of analyzing modern war and peace that is often underappreciated in this age of technological determinism. Yet the result leads to a more in-depth and dispassionate understanding of contemporary wars, one that explains how particular military successes and failures of the past can be often germane, sometimes misunderstood, or occasionally irrelevant in the context of the present.

Strategika

Strategika is a journal that analyzes ongoing issues of national security in light of conflicts of the past—the efforts of the Military History Working Group of historians, analysts, and military personnel focusing on military history and contemporary conflict. Our board of scholars shares no ideological consensus other than a general acknowledgment that human nature is largely unchanging. Consequently, the study of past wars can offer us tragic guidance about present conflicts—a preferable approach to the more popular therapeutic assumption that contemporary efforts to ensure the perfectibility of mankind eventually will lead to eternal peace. New technologies, methodologies, and protocols come and go; the larger tactical and strategic assumptions that guide them remain mostly the same—a fact discernable only through the study of history.