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THE UNITED STATES OF AMERICA AND CHINA'S TRADE AND ECONOMIC RELATIONSHIP: A RISK MANAGEMENT SOLUTION BASED APPROACH

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Abstract: **This research paper examines the U.S. -China financial relationship which has reached a important juncture. During the last year, the U.S imposed tariffs on $250 billion worth on Chinese imports and China has retaliated, raising tariffs on U.S. exports. At the G-20 leaders' summit in November 2018, Presidents Trump and Xi agreed to remedy the trade dispute within 90 days—through March 1, 2019, even though this cut-off date has been lately extended.**

The U.S. worries that underpin these bilateral tensions stem from unique practices endemic to China's financial model that systematically tilt the field to favor of Chinese corporations regionally and globally. Development on specific trade issues would require China to conform with its world trade organization (WTO) commitments and to make sure reforms will touch on areas of state control over the economy.

In addition, new trade rules are needed to address China's economic practices not covered by its WTO commitments, including in areas such as state-owned enterprises (SOEs), certain subsidies, and digital trade. These issues also come at a time of increasing U.S. concern over the national security risks China presents, particularly with respect to technology access.

Despite the challenges the U.S. has had at the WTO, the WTO should be central to resolving U.S.-China trade tensions. From this perspective, we outline a multipronged strategy, including bilateral, multilateral, and unilateral actions, as well as working with allies, that together would constitute positive next steps for this critical economic relationship. In taking this multifaceted approach, the U.S. also needs to stay true to its values and not accept short-term gains or "fig leaf" deals. In particular, creating a managed trade relationship with China would not be a constructive outcome. The resulting deal should address the real issues at hand in a free market manner and strengthen the multilateral global trading system and rule of law that the U.S. has championed in the post-World War II era.

All of these matters underscore the complexity of U.S.-China bilateral negotiations as well as the stakes at play. Resolving U.S.-China differences in a meaningful way will take time.

Keywords: **U.S. -China financial, world trade organization (WTO), Economic Relationship.**

1. INTRODUCTION

The state of the two super power's bilateral economic engagement

In order to assess what might constitute a sustainable economic relationship going forward, it is important to be clear about the costs and benefits of U.S. trade and investment with China.

The U.S.-China economic relationship delivers more benefits to the U.S. than is commonly understood. For example, recent data shows that U.S. exports to China support around 1.8 million jobs in sectors such as services, agriculture, and capital goods. However, trade with China has also led to job destruction in some U.S. industries—particularly low wage manufacturing. Despite these costs, the frequent focus by the administration on the bilateral deficit is not a meaningful yardstick for assessing U.S.-China trade or its impact on employment. The U.S. trade deficit is less a product of restrictions on U.S. imports than it is a reflection of a low U.S. domestic savings rate, which requires overseas capital to fund U.S. domestic investment needs and the growth in U.S. government debt. In addition, the trade deficit does not account for the activities of affiliates of U.S. and Chinese companies in each respective market, a calculus that shows the U.S. selling more to China than vice versa.

Nevertheless, the economic costs of the bilateral economic relationship are very real. China's economic practices now risk harming the U.S. service and knowledge economy. As identified in the United States Trade Representative (USTR) Section 301 report, intellectual property (IP) theft and forced technology transfer and other Chinese unfair trade practices threaten high-wage jobs and high-value-added manufacturing in the U.S. The role of the state in effectuating these policies with larger aims of supplanting U.S. leadership in high-tech industries makes these Chinese policies all the more concerning.

Why China's monetary risk model matters

Despite the rapid growth in its economy and acceptance of a role for competition and markets, the Chinese Communist Party (CCP) remains firmly in control of China's economy. China is not the first country with an economic model premised on state control and coordination between the government and business on economic and trade priorities. Elements of all these systems were, and continue to be, present in places like Japan, with the keiretsu, or South Korea, with its chaebols. Yet China's economic model is different from both Japan and Korea. In addition, due to its sheer size, how China grows will affect the rest of the world in ways that even Japan's economy at its economic height did not.

China's economic model has a range of growing implications for the U.S. and globally. First, the move towards self-sufficiency in emerging technologies is inconsistent with a trading system based on comparative advantage. Second, use of SOEs, their access to subsidies, and limited rule of law in China support state companies within China and globally. Third, China's use of industrial policy to pick winners is expected to lead to excess production and dumping overseas. This has already occurred, for instance, in steel and solar photovoltaic (PV) with negative impacts for U.S. and global industries, and is expected to occur in more advanced industries identified in China's recent industrial policies, such as robotics, high-speed rail production, new energy vehicles, and batteries.

The effect at the WTO

While President Xi continually affirms China's commitment to the multilateral rules-based trading framework, China continues to renege on its WTO commitments. Moreover, China's economic model makes it difficult to use the WTO and its dispute settlement system to challenge noncompliance. For instance, state control over public and private businesses makes it difficult to distinguish between what is a public body and what is private, thereby making unclear whether the there is a rule or regulation issued by a public entity that is subject to WTO rules. In addition, the state's role in the judicial and administrative system, including the use of informal notices and verbal demands on foreign businesses, undermines the ability to show that a WTO-inconsistent measure exists. More broadly, China's industrial policy—which distorts the playing field in favor of Chinese companies—is at odds with most WTO members' market-based systems.

Given these challenges, there is a real question as to the capacity of the WTO to respond to the China challenge. While the WTO is not able to address all the issues that China poses, in the context of a comprehensive approach to the China challenge, the WTO remains central, contingent on strong U.S. leadership. The WTO is the only global set of trade rules that both reflects core U.S. values, such as non-discrimination, transparency, and rule of law, and forms a baseline on which to build global support to critique and push back against Chinese economic practices.

Making development in U.S.-China economic relations

In looking for collectively useful outcomes, the U.S. will have to take a comprehensive method to the negotiations based on market-oriented answers, which will improve the worldwide buying and selling structure and rule of law.

2. BILATERAL NEGOTIATIONS

U.S.-China bilateral outcomes need to be verifiable, enforceable, and market-based—not simply a restatement of prior Chinese commitments such as to do better on IP protection and enforcement or forced technology transfer, or to buy more U.S. products. The bilateral track should include commitments from China to implement all of its WTO commitments. Additional WTO-plus commitments should be negotiated in areas such as SOEs, cross-border data flows, and determining the application of nonmarket economy (NME) status for trade remedy purposes. Where feasible, enforcement should be through the WTO dispute settlement mechanism, and recourse to arbitration under Article 25 of the Dispute Settlement Understanding (DSU) could be used to produce speedier results.

Given that the tariffs imposed to date by the U.S. and China are not WTO consistent, as discussed below, any U.S.-China deal should aim to bring tariffs back to their WTO-bound levels when specific benchmarks are met, but with scope for tariff snapbacks in the event of noncompliance. The U.S. and China should make such a deal WTO consistent by seeking a WTO waiver. Such an approach is a pragmatic compromise that recognizes that the U.S. and China will likely focus on bilateral negotiations to address their trade issues, while minimizing the harm to the WTO as an institution.

The U.S. and China should also renew efforts to complete a comprehensive bilateral investment treaty (BIT) with an aggressive nine-month schedule.

A bilateral deal should avoid commitments by China to increase purchases of U.S. exports, and reducing the bilateral trade deficit should not guide the negotiations or determine success. Increased U.S. exports, whether to China or elsewhere, need to be in response to market forces and not undercut broader U.S. demands for less state intervention. Such an arrangement would be inconsistent with U.S. values, adopt a managed trade framework more akin to the Chinese model, would likely be WTO inconsistent, and could disadvantage U.S. allies

The action position for the WTO

The WTO is a set of globally agreed upon trade rules that provide a basis for identifying where China fails to comply with existing commitments. The U.S. could then also identify where Chinese practices are of concern, but not disciplined by WTO rules, to justify where bilateral or unilateral action may be necessary.

In terms of what the U.S. could seek to pursue at the WTO:

■ The U.S. should work with China to agree to an in-depth review at the WTO of China’s compliance with its WTO commitments.

■ The U.S. should work through the WTO to ensure that China gives a full accounting of its SOE activities and subsidies as required of any WTO member and pursuant to its Protocol of Accession.

■ The U.S. should work with allies and China to reintroduce the China specific safeguard as well as craft an agreement with China regarding its ongoing use of NME methodology until such time that China is able to substantiate that it has become a market economy.7 Progress on this issue could be the result of a negotiated settlement of the WTO case that China has brought against the EU and U.S. regarding their continued use of NME methodology in trade remedy cases.

■ The U.S. should work to reform the WTO dispute settlement system to ensure quicker dispute settlement proceedings, including potential injunctive relief for unfair trade practices, would be an institutional change that could be useful vis-à-vis China

The U.S. and China should use a bilateral deal or a BIT as the basis for re-energizing the negotiation of new rules at the WTO on areas such as technology transfer, SOEs, and digital trade.

Work with U.S. allies

A key part of the U.S. strategy with respect to the China challenge needs to include new trade agreements with allies, which raise the standards for trade. This strategy would provide benefits to the parties to such free trade agreements (FTAs) and create economic costs to China from nonparticipation, which should further encourage China to reform its economy and trade practices with the aim of joining the new trade agreements.

The Trans-Pacific Partnership (TPP), from which the U.S. withdrew in 2017, included important new rules in areas that matter for the U.S. such as on SOEs, IP, digital trade, and transparency and due process in the making of regulations affecting trade. With China outside the trading block, TPP would have created costs for China. According to one estimate, TPP could have decreased Chinese income by $40 billion annually and this would have grown as more countries joined the agreement. Taken together, TPP would have been an important part of the "comprehensive toolkit" USTR refers to in creating pressure on China to reform. The TPP has now been reconstituted without the U.S. as the Comprehensive and Progressive TPP (CPTPP) and most of the rules for addressing U.S. concerns with Chinese trade practices remain. The importance of the CPTPP for addressing the China challenge warrants the U.S. to reconsider its position on the agreement and rejoin.

In the event that bilateral FTAs remain the focus for the time being, the U.S. should aim to conclude agreements with its strategic allies in the Asia-Pacific region and beyond.

Unilateral U.S. motion

How the U.S. fares in its competition with China will ultimately be determined by actions that the U.S. takes at home. Apart from focusing on its own competitiveness through domestic policies, which are beyond the scope of this policy brief, the U.S. should thoughtfully control access to U.S. technologies through foreign investment and export controls, and effectively use WTO-consistent tariff policies to minimize the harm from Chinese economic practices on U.S. businesses.

The U.S. has already made progress domestically on addressing technology transfer issues with the enactment of the Foreign Investment Risk Review Modernization Act (FIRRMA), which included the Export Control Reform Act (ECRA) of 2018. While companies now largely decide which technologies to transfer overseas, the careful implementation of FIRRMA/ECRA is critical to making this a matter for U.S. policy and for considering the national security costs that may not be properly included in private sector decisions regarding the transfer of technology to China.

FIRRMA/ECRA also recognizes the importance of working with allies to strengthen multilateral export control regimes and to prevent diversion through U.S. allies in attempts to avoid FIRRMA

The U.S. will need to convince other governments to adopt similar investment and technology export restrictions in order for these U.S. reforms to be most effective. U.S. restrictions on access to U.S. technology will be less effective and hurt U.S. competitiveness if similar technology is available from the EU or Japan.

Making progress on China's compliance with its WTO commitments will be most effective where the U.S. is also complying with its WTO commitments. This would require the U.S. to calibrate its unilateral use of tariffs, which have undermined the WTO. Instead, the U.S. should expand its use of trade remedy measures—anti-dumping and countervailing duties—that are consistent with U.S. WTO obligations and provide recourse to U.S. business for China's unfair trade practices.

The U.S.–China economic relationship has reached a critical juncture. The last year has seen tit-for-tat tariff escalation. So far, $250 billion worth of U.S. imports of Chinese products have been hit with tariffs ranging from 10-25 percent and President Donald Trump is threatening to increase existing tariffs and to place additional tariffs on all imports from China. China has likewise levied tariffs on the equivalent amount of U.S. imports and has threatened to impose more. This trade war has roiled financial markets and contributed to slowing global growth. At the G-20 leaders' summit in November 2018, Presidents Trump and Xi agreed to resolve the trade dispute within 90 days—by March 1, 2019, though this deadline has recently been extended.

The U.S. concerns that have escalated these bilateral tensions stem from specific trade practices endemic to China's economic model that systematically tilt the playing field in favor of Chinese companies domestically and globally. Progress on specific trade issues will require China to comply with its WTO commitments and to make certain reforms that will likely touch on areas of state control over the economy. In addition, new trade rules are needed to address China's economic practices not covered by its WTO commitments, including in areas such as SOEs, certain subsidies, and digital trade. These issues also come at a time of increasing concerns over the national security risks China presents, particularly with respect to technology access. All of these matters underscore the complexity of U.S.-China bilateral negotiations as well as the stakes at play. Resolving U.S.-China differences in a meaningful way will take time.

This policy brief assesses the state of the U.S.-China trade relationship by looking at the economic impact for the U.S. The policy brief then looks at why the Chinese economic model is so concerning. The brief then explains why, despite the challenges the U.S. has had at the WTO, the WTO should be central to resolving U.S.-China trade tensions. We outline a multipronged strategy, including bilateral, multilateral, unilateral actions as well as working with allies that together would constitute positive next steps for this critical economic relationship. In taking this multifaceted approach, the U.S. should stay true to its values and not be tempted to accept short-term gains or "fig leaf" deals. Creating a managed trade relationship with China would not be a constructive outcome. Instead, the U.S. should work with China to agree on long term solutions. The resulting deal should address the real issues at hand in a free market manner and strengthen the multilateral global trading system and rule of law that the U.S. has championed in the post-World War II era.

Assessing the U.S.-China relationship: Benefits and costs of the world's largest economic relationship

Since China's accession to the WTO in 2001, U.S. trade with China has increased from $125 billion to over $700 billion in 2017. In this same period, China's economy has quadrupled in size, from the fourth largest economy in 2001 to the world's second largest today. China accounts for 16 percent of global activity and 40-50 percent of global marginal growth. In addition, the world's largest middle class now lives in China, and four of the world's top 10 banks are Chinese, including the first and second largest banks. China also has the largest e-commerce market. Over this period, the U.S. has supported China's global integration with the expectation that as China benefited from the international economic system, including WTO membership, it would become a responsible stakeholder—where China would work with the United States "to sustain the international system that has enabled its success."

However, this U.S. view of China has progressively evolved into seeing China less as a partner and more as a competitor, culminating in the positions taken by the Trump administration. The trade and investment front is where some of the most dramatic shifts in U.S. policy towards China have manifested. For instance, the U.S. 2017 National Security Strategy states that "China and Russia challenge American power, influence, and interests, attempting to erode American security and prosperity. They are determined to make economies less free and less fair, to grow their militaries, and to control information and data to repress their societies and expand their influence." The same National Security Strategy called for the U.S. to rethink the policies over the past two decades, "policies based on the assumption that engagement with rivals and their inclusion in international institutions and global commerce would turn them into benign actors and trustworthy partners. For the most part, this premise turned out to be false."

In order to decide what type of trade and investment relations the U.S. and China should have going forward, it is important to step back and be clear about the current state of the bilateral economic relationship.

Benefits and cost

International trade increases economic productivity, reallocating jobs to more efficient industries. In the case of U.S.-China trade, there has been job creation in some areas of the U.S. economy such as agriculture and services, and job destruction in some sectors—particularly low wage manufacturing. For instance, between 1995-2001, U.S. exports overall are estimated to have created 6.6 million jobs and recent data shows U.S. exports to China support around 1.8 million jobs in sectors such as services, agriculture, and capital goods. U.S. consumers have also gained from trade with China. From 2000 to 2007, the impact of lower-priced imports from China produced an economic gain of $202 billion for the U.S.—equivalent to $101,250 per job lost in manufacturing during this period.

Yet, trade with China has led to job losses in the U.S. manufacturing sector. From 1999 to 2011, 560,000 manufacturing jobs were lost due to direct competition with imports from China.26 Taking into account upstream effects—job losses in industries that supplied to those industries facing direct competition from China—there were 2 million job losses in the manufacturing and non-manufacturing sectors. This data, however, likely overstates the job losses as it fails to account for the extent to which U.S. imports from China include U.S. value add. China remains a locus of significant amounts of "processing trade" critical to global value chains, whereby low value-added product assembly using inputs from the U.S. and elsewhere are then exported to the U.S. and globally, while high-value inputs such as research and development, design, distribution, retail, and so on remain outside China. For instance, each iPhone imported into the U.S. from China is recorded as a $240 import, but China's value add to the iPhone is only around $8.50 or 3.6 percent of the total, while the imported U.S. value added in the iPhone is worth around $70.29 As this example demonstrates, a proper accounting of U.S. trade with China would better take into account U.S. value embedded in imports from China and reduce the impact of imports from China on U.S. manufacturing jobs by over 32 percent. Moreover, the initial China shock to the U.S. economy is largely complete and trade with China is having fewer negative effects on U.S. manufacturing. Evidence of firm reorganization and innovation shows that U.S. business has been more adept at competing with imports from China. In fact, since 2010, the U.S. has added over 1.2 million manufacturing jobs

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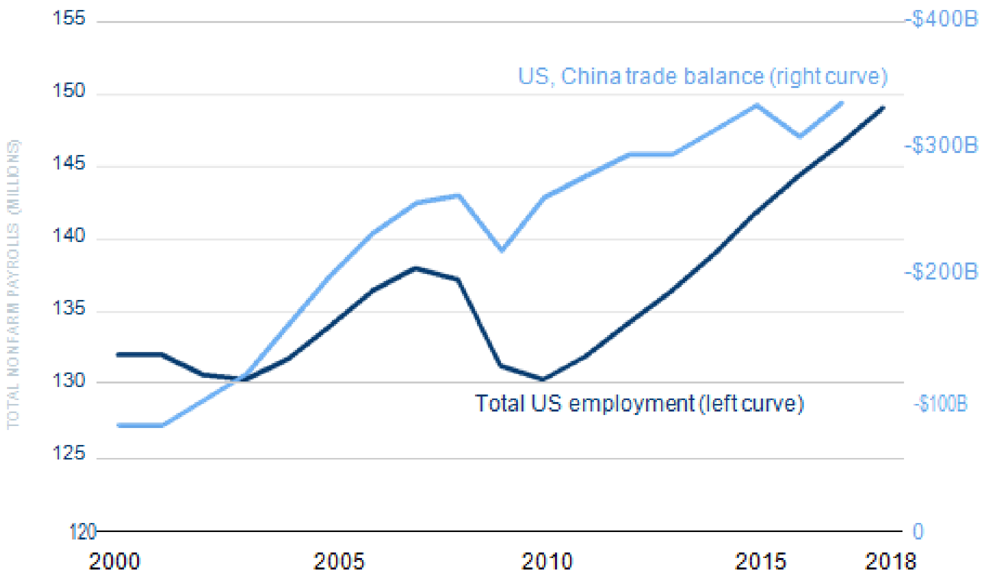
It is also the case that the U.S.-China deficit is not a meaningful yardstick for assessing the health of the relation or its impact on U.S. employment, despite being a focus for the Trump administration. Figure 1 shows the bilateral deficit in goods and services has grown from $81 billion in 2001 to $336 billion in 2017, increasing from just over 20 percent of the U.S. trade deficit in 2011 to over 60 percent today

Figure A. U.S. trade deficit with China

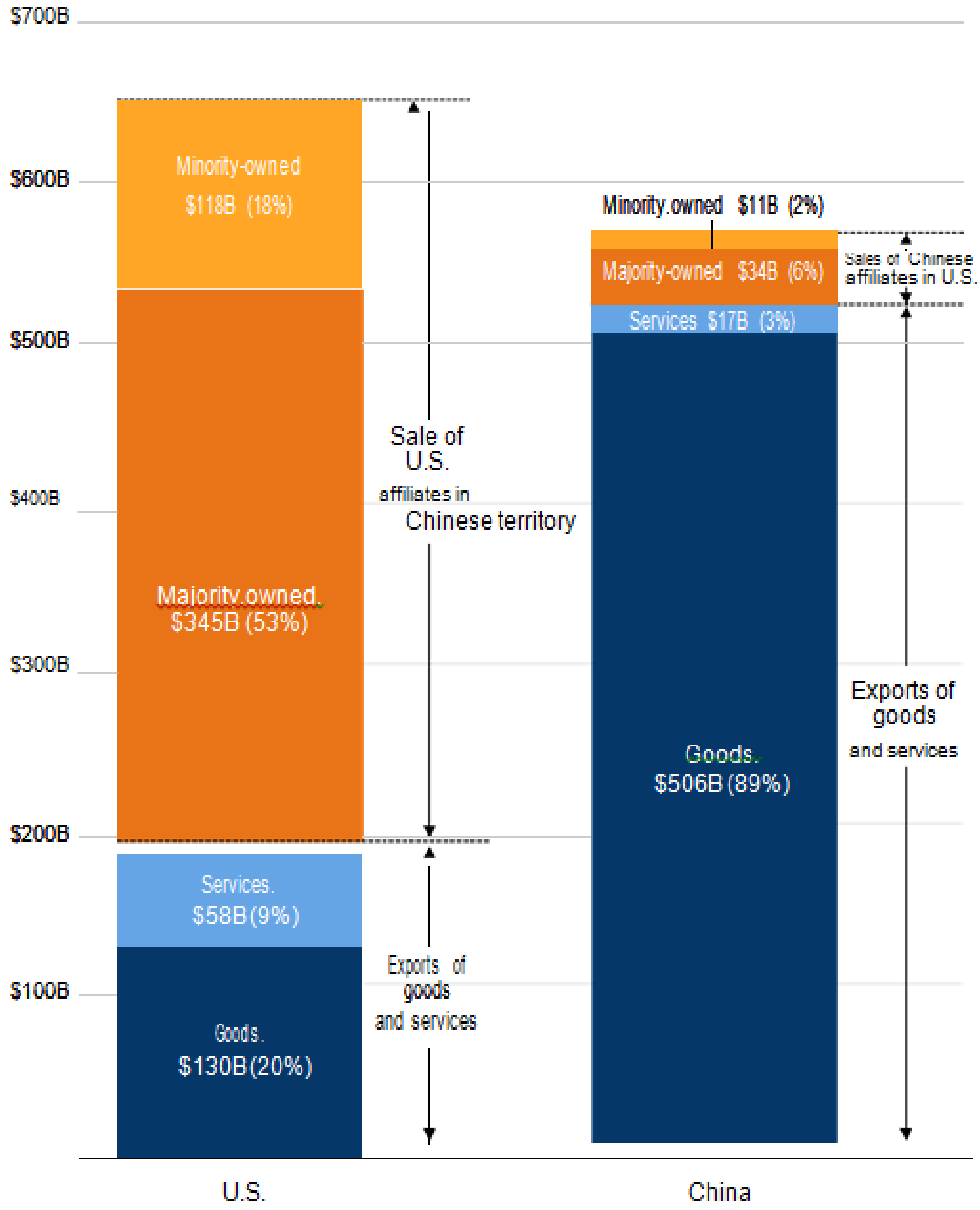
The bilateral trade deficit needs to be assessed in light of the overall trade deficit which is less a product of restrictions on U.S. exports than it is a reflection of a low U.S. domestic savings rate which requires overseas capital to fund U.S. domestic investment needs and the growth in U.S. government debt.34 Efforts to reduce the U.S.-China trade deficit without addressing the saving-investment gap, will merely change the composition of the U.S. trade deficit, leaving the overall trade deficit unchanged

Figure B. Relationship between employment and deficit trade with China



Seeing the U.S. trade deficit as a drain on the U.S. economy is also at odds with the facts. During times of strong economic growth and full employment, the U.S. economy has seen growing trade deficits, since capital inflow from overseas is required to finance increased domestic investment and consumption. In addition, the trade deficit has decreased during periods of economic contraction and rising unemployment. Notably, as Figure 2 demonstrates, there is actually a strong correlation between increases in the U.S. trade deficit and employment.

Figure C. Trade and business activities of Allies of U.S. and Chinese firms in each other's markets



Nevertheless, Chinese economic practices are now increasingly targeting the heart of the U.S. service and knowledge economy. IP theft, forced technology transfer, and other Chinese unfair trade practices now threaten high-wage jobs and high-value added manufacturing in the United States. U.S. concerns with China's economic practices are particularly focused now on Chinese efforts to acquire U.S. technology and IP. According to one estimate, trade in counterfeit goods, pirated software, and trade secrets in China costs the U.S. between $225-$600 billion annually—with the large range reflecting significant uncertainty as to the cost of trade secret theft for the U.S. economy. These figures do not take into account most costs of patent infringements as well as second order effects from IP theft, such as additional costs to companies of protecting IP, disincentives for investment, reduced innovation, and employment effects on U.S. skilled labor. While not all these costs are caused by China, it is the most significant infringer of IP rights globally.

In March 2018, the USTR issued a report under Section 301 detailing how these Chinese practices affect U.S. IP and technology. In a follow-up report in November 2018, USTR assessed whether China had changed any of its practices, finding progress in some areas but concluding overall that China's attempts to access and acquire U.S. technology remained.

In the Section 301 report, USTR focused on four Chinese practices:

1. China's technology transfer regime, including conditioning access to investment opportunities on technology transfer, applying the licensing and administrative process in an arbitrary, non-transparent manner, and conditioning government procurement on technology transfer; 2. Restrictions on terms under which U.S. companies can license their technology within China; 3. Chinese government directed outbound investment into U.S. companies in order to acquire technology; and 4. Unauthorized cyber intrusions into U.S. companies.

The Section 301 report also discussed other technology issues, including Chinese restrictions on data flows, data localization requirements by critical infrastructure providers, encryption regulations, and inadequate IP protection.

Access to U.S. technology also raises national security concerns. As the U.S. Department of Defense has noted, many of the key technologies in which China is seeking to obtain global leadership are integral to American economic growth as well as the ability of the U.S. to maintain its military advantage

3. WHY CHINA'S FINANCIAL VISION MATTERS

Despite the rapid growth in its economy and acceptance of a role for competition and markets, the CCP remains firmly in control. At its 19th Party Congress, China described its economy as "socialism with Chinese characteristics for a new era." The state sets economic goals and allocates resources to achieve them through industrial policy and providing platforms for SOEs. China is not the first country with an economic model premised on state control and coordination between the government and business on economic and trade priorities. Elements of all these systems were, and continue to be, present in places like Japan, with the keiretsu, or South Korea, with its chaebols. Yet the impact of China's economy is different from both Japan and Korea. Due to its sheer size—as the world's second largest economy—how China grows will affect the rest of the world in ways that even Japan's economy at its economic height did not.

China's economic model has a range of growing economic implications for the U.S. and globally. First, the move towards self-sufficiency in emerging technologies is inconsistent with a trading system based on comparative advantage. Second, use of SOEs, their access to subsidies and limited rule of law in China support state companies within China and globally. Third, China's use of industrial policy to pick winners is expected to lead to excess production and dumping overseas. This has already occurred for instance in steel and solar PV with negative impacts for U.S. and global industries in terms of output and innovation, and is expected to occur in more advanced industries identified in China's recent industrial policies, such as robotics, high-speed rail production, new energy vehicles, and batteries

An ongoing reliance on planning and industrial policy to achieve goals identified by the state China has now turned the focus of its industrial policies to the pursuit of an innovation driven economy. This includes industrial policies such as the National Medium and Long-Term Science and Technology Development Plan Outline (2006-2020) (MLP) which calls for China to become an innovation-oriented society by the year 2020 and a world leader in science and technology (S&T) by 2050, based on developing capabilities for indigenous innovation. The "Made in China 2025" initiative launched in 2015 is a 10-year plan for China to achieve 70 percent self-sufficiency in strategic technologies such as advance information technology, robotics, aircraft, new energy vehicles, new material, and biotechnology. Similar industrial policies are also being implemented at the sub-central government level

Reliance on SOEs as a tool of state economic policy When it comes to implementation of its industrial policy, China largely relies on SOEs and control over key inputs including land, labor, and finance to achieve its objectives. The activities of SOEs are not governed by market forces or commercial standards. The role of SOEs in the Chinese economy only continues to grow in importance under President Xi47 and China's government has also been crowding-out private enterprise and taking even larger stakes in private companies.48 While assessing the extent of the public sector is challenging given the various and often opaque ways that the state controls companies, one estimate is that the public share of fixed investment in 2016 was around 60 percent, compared to official data of 35 percent.49 SOEs tend also to benefit from subsidies and other state support. For instance, China's largest oil companies—CNOOC, Petro China, and Sinopec—all benefit from state financial support from state-owned banks. Government support also extends to supporting Chinese firms operating globally. The identification by the state of food security as a strategic priority led state-owned banks to guarantee ChemChina's acquisition of Swiss firm Syngenta and its biotech assets. Private firms such as Huawei are seeking to dominate the development of 5G networks globally with support from the China Development Bank.

A key mechanism for control of SOEs is the State-owned Asset Supervision and Administration Commission of the State Council (SASAC). SASAC has a stake in more than half of the Chinese companies on the Fortune Global 500 List. This includes SOEs with returns on capital far lower than those generated by private firms (sometimes half as less). As Harvard Law Professor Mark Wu explains, the equivalent of SASAC in America would be to imagine a single U.S. government agency controlling GE, GM, Ford, Boeing, U.S. Steel, DuPont, AT&T, Verizon, Honeywell, and United Technologies, with such an entity empowered to hire and fire management, and to deploy and transfer resources across companies.

Access to finance by state-owned or controlled banks has also been a key tool of economic policy. As Wright and Rosen observe, "controlling the flow of credit has been virtually the raison d'etre of China's political system for almost half a century." The state has used credit growth to fuel economic expansion and limit any economic recession so far. Control over access to finance is exercised in China through Central Huijin Investment Ltd. (a subsidiary of China's sovereign wealth fund, the China Investment Corporation), which has a controlling stake in China's largest four banks as well as a majority stake in smaller second-tier commercial banks. Chinese banks account for over 80 percent of all assets in the Chinese financial system, which at $38.4 trillion is three times the size of China's GDP in 2017. For a point of comparison, the existence of an equivalent to Central Huijin Investment Ltd. in the U.S. would be like the U.S. Treasury controlling JPMorgan Chase, Bank of America, Citibank, and Wells Fargo

The CCP also controls SOEs through the Central Organization Department which has the power to appoint the head and management of SOEs, overriding the corporate function of boards. In fact, the heads of SOEs are all CCP members and carry a CCP rank commensurate with their role. In addition, both SOEs and private companies must establish a Party Committee comprising three CCP members. While its usually unclear how these Party Committees work or their role, they create an appearance of ongoing CCP influence over companies.

The operation of SOEs is also supported by a complex range of preferences, national standards, cyber theft, and use of government procurement and regulation to ensure that private and foreign traders' and investors' ability to compete is curtailed.

The development of regulations and standards is another tool of state control used to benefit SOEs over private and foreign investors and traders. As rule of law in China often means the fiat of government officials, domestic courts are usually unwilling to overturn administrative decisions or to sanction government and party officials who breach the law. Central control is further reinforced through the role of guanxi (i.e., the system of social networks and influential relationships that facilitate business and other dealings) in the judicial system. Compounding this is the prevalence of corruption and informality as alternative means of settling disputes.

An ongoing reliance on planning and industrial coverage to gain dreams diagnosed by using the country China has now became the focus of its business rules to the pursuit of an innovation driven financial system. This includes commercial policies such as the country wide Medium and long-time period technology and technology improvement Plan outline (2006-2020) (MLP) which calls for China to grow to be an innovation-orientated society via the year 2020 and a global leader in technological know-how and technology (S&T) via 2050, based totally on growing skills for indigenous innovation. The "Made in China 2025" initiative launched in 2015 is a 10-year plan for China to achieve 70% self-sufficiency in strategic technologies along with increase statistics technology, robotics, aircraft, new energy motors, new fabric, and biotechnology. Comparable industrial guidelines are also being carried out at the sub-critical authorities stage.

Reliance on SOEs as a device of nation financial policy in terms of implementation of its industrial policy, China in large part relies on SOEs and control over key inputs consisting of land, labor, and finance to achieve its objectives. The sports of SOEs aren't ruled by means of marketplace forces or industrial requirements. The position of SOEs within the China's economic system most effective keeps to grow in significance below President Xi and China's government has additionally been crowding-out personal agency and taking even large stakes in private businesses at the same time as assessing the quantity of the public quarter is tough given the diverse and often opaque approaches that the nation controls organizations, one estimate is that the public proportion of fixed funding in 2016 become round 60 percent, compared to respectable statistics of 35%. SOEs generally tend also to advantage from subsidies and other country support for instance, China's largest oil organizations—CNOOC, Petro China, and Sinopec—all benefit from kingdom monetary assist from state-owned banks. Government assistance additionally extends to supporting Chinese firms working globally.

The identification by using the kingdom of meals protection as a strategic precedence led nation-owned banks to assure ChemChina's acquisition of Swiss company Syngenta and its biotech assets. personal companies which includes Huawei are searching for to dominate the development of 5G networks globally with guide from the China development financial institution.

A key mechanism for manage of SOEs is the country-owned Asset Supervision and management commission of the state Council (SASAC). SASAC has a stake in more than half of the Chinese businesses on the Fortune global 500 list. This includes SOEs with returns on capital some distance lower than those generated through personal corporations (on occasion half as much less).fifty one As Harvard law Professor Mark Wu explains, the equivalent of SASAC in America might be to imagine a unmarried U.S. government employer controlling GE, GM, Ford, Boeing, U.S. metal, DuPont, AT&T, Verizon, Honeywell, and United technology, with such an entity empowered to lease and hearth control, and to installation and switch resources throughout companies get Access to finance by means of nation-owned or managed banks has additionally been a key tool of financial coverage. As Wright and Rosen look at, "controlling the waft of credit has been really the reason d'être of China's political machine for nearly half of a century." The kingdom has used credit score boom to gas monetary expansion and limit any monetary recession so far control over access to finance is exercised in China thru critical Huijin investment Ltd. (a subsidiary of China's sovereign wealth fund, the China funding organization), which has a controlling stake in China's biggest 4 banks in addition to a majority stake in smaller second-tier industrial banks.

Chinese banks account for over eighty percentage of all property within the Chinese economic gadget, which at $38.four trillion is 3 instances the size of China's GDP in 2017.fifty four For a point of comparison, the life of an equivalent to significant Huijin investment Ltd. inside the U.S. could be just like the U.S. Treasury controlling JPMorgan Chase, bank of the us, Citibank, and Wells Fargo.

The CCP additionally controls SOEs thru the vital enterprise department which has the strength to hire the pinnacle and management of SOEs, overriding the corporate feature of forums. In fact, the heads of SOEs are all CCP contributors and bring a CCP rank commensurate with their function. in addition, both SOEs and personal companies need to set up a celebration Committee comprising three CCP individuals even as its commonly unclear how those celebration Committees paintings or their function, they invent an look of ongoing CCP have an effect on over organizations.

The operation of SOEs is also supported by means of a complicated range of possibilities, countrywide standards, cyber theft, and use of presidency procurement and regulation to make certain those non-public and overseas traders' and buyers' potential to compete is curtailed.

The improvement of policies and standards is some other device of nation control used to advantage SOEs over non-public and foreign traders and investors. As rule of regulation in China frequently manner the fiat of government officers, domestic courts are usually unwilling to overturn administrative decisions or to sanction authorities and birthday celebration officers who breach the regulation critical manage is in addition strengthened through the role of guanxi (i.e., the machine of social networks and influential relationships that facilitate enterprise and other dealings) inside the judicial machine.

Compounding this is the height of corruption and informality as opportunity way of settling disputes.

The significance of the WTO to resolving U.S.-China trade tension

China's economic system places a number of acute stresses on the WTO. China undertook significant commitments as part of its WTO accession in 2001, yet developments in the Chinese economic system make it increasingly difficult to enforce its WTO commitments. In addition, China's economic model presents new challenges not anticipated at the time of its accession. This comes at a time of skepticism of the capacity of the WTO as an institution—both in terms of the rules and the dispute settlement system—to deal with the magnitude of the China challenge. The last multilateral trade round, the Doha Development Agenda, was shelved after over ten years of negotiations. Attempts at concluding various plurilateral agreements in areas such as services and environmental goods have stalled, among other things.

While President Xi continually affirms China's commitment to the multilateral rules-based trading framework, China continues to renege on its WTO commitments. Moreover, China's economic model makes it difficult to use the WTO and its dispute settlement system to challenge non-compliance. For instance, state control over public and private businesses makes unclear what is a public body and what is private. In addition, the state's role in the judicial and administrative system, including use of informal notices and verbal demands, undermines the ability to show that a WTO inconsistent measure exists. More broadly, China's industrial policy—which distort the playing field in favor of Chinese companies—is at odds with most WTO members' market-based systems.

Given these challenges, there is a real question as to the capacity of the WTO to respond to the China challenge. While the WTO is not able to address all the issues that China poses, in the context of a comprehensive approach to the China challenge, the WTO remains central. The WTO is the only global set of trade rules, which both reflect core U.S. values, such as non-discrimination, transparency and rule of law, and form a baseline on which to build global support to critique and push back against Chinese economic practices. As a recent RAND report noted, the key challenge to the U.S. may come from efforts by China to elevate the viability and legitimacy of its authoritarian model and "[gain] veto authority over other nations' economic, diplomatic and security decisions." Then efforts to bolster the value of largely U.S.-generated rules, norms, and international institutions will be a key common point of reference and baseline for the U.S. and other countries seeking to counter China's economic and governance models. Thus, despite the organization's challenges, the WTO can continue to play a key role in addressing the China challenge if the U.S. provides leadership for such a path forward.

In this light, any outcome in U.S.-China bilateral trade negotiations that achieves short-term wins, such as more trade with China, but does so in ways that undermine WTO legitimacy, would come at an enormous strategic cost. As discussed below, positive, long-term outcomes for the U.S.-China relationship should support and strengthen the WTO and the rules based system.

Making progress in U.S.-China trade relations

The current abiding challenge for U.S.-China relations is to avoid fostering a relationship shaped only by competition and to identify where mutually beneficial outcomes are possible. The trade and investment front is one area where such progress may be possible. As the U.S. Department of Defense has noted, while China is a key long-term strategic competitor, "competition does not mean conflict is inevitable, or preclude cooperation with China on areas of mutual interests." USTR affirmed this scope for mutually beneficial cooperation with China on trade, stating that its goal is for "a trade relationship with China that is fair, reciprocal, and balanced," stressing that the reforms the U.S. is requesting of China will benefit China as well as build a stronger global economy.

In seeking mutually beneficial outcomes, the U.S. should take a comprehensive approach to the negotiations, using a combination of actions the U.S. could undertake through bilateral negotiations with China, multilaterally through the WTO, and working with allies outside the WTO, as well unilateral actions.

In taking this multifaceted strategy, the U.S. should aim for long-term, market-orientated solutions, while also strengthening the global trading system and rule of law.

Bilateral negotiations

U.S.-China bilateral outcomes need to be verifiable, enforceable, and market-based—not simply a restatement of prior Chinese commitments such as to do better on IP protection and enforcement or forced technology transfer or to buy more U.S. products. The bilateral track should include assurances from China to implement all of its WTO commitments and commitments to additional WTO plus reform as well as renewed efforts to complete a comprehensive BIT. Where feasible, enforcement should be through the WTO dispute settlement mechanism and recourse to arbitration under Article 25 of the DSU could be used to produce speedier results.

Assurances by China to live up to its WTO commitments

In its WTO Protocol of Accession in 2001, China made commitments to the fundamental principles of the international trading system as well as a whole host of specific commitments. Indeed, China has taken WTO commitments in a number of areas that if implemented fully would go some way to addressing U.S. concerns, including with respect to technology transfer, IP protection, and use of subsidies. Yet, and as noted above, China's implementation of its WTO commitments has been, at best, mixed. The U.S. should prioritize China's reaffirmation of its WTO commitments in the context of bilateral talks. The U.S. and China should also resolve continued application of NME methodology to China for purposes of anti-dumping and countervailing duty (CVD) trade remedy actions. In addition, the bilateral deal should seek to address Chinese economic practices not covered by WTO commitments and that have major impacts on the U.S. economy, such as SOEs and access to subsidies.

Having a mechanism to ensure compliance will be critical to concretize these commitments. The U.S. and China could agree to resort to Article 25 of the WTO DSU for noncompliance with any bilateral deal struck which allows for "expeditious arbitration within the WTO as an alternative means of dispute settlement…that concern issues that are clearly defined by both parties." Article 25 requires WTO members using this mechanism to provide all WTO members with notice and, with a favorable arbitral award, would allow the U.S. access to retaliation through the WTO DSU (including with tariffs or suspending other market access the U.S. gave China through the WTO), were China to not comply with commitments. An arbitration mechanism could also be used for any WTO plus commitments to which China agrees. In addition to raising tariffs in the event of non-compliance, the U.S. should consider Office of Foreign Assets Control (OFAC) financial sanctions or travel bans against Chinese persons and companies who steal U.S. technology.

Given that the tariffs which have been imposed to date by the U.S. and China are not WTO consistent, such any U.S.-China bilateral deal should aim to bring tariffs back to their WTO bound levels when specific benchmarks are met, but with scope for tariff snap-backs in the event of non-compliance. The U.S. and China should seek to make such a deal WTO consistent by seeking a WTO waiver. Such an approach is a pragmatic compromise that recognizes that the U.S. and China will likely focus on bilateral negotiations to address their trade issues, while minimizing the harm to the WTO as an institution.

Negotiate a BIT

The U.S. and China should reinvigorate BIT negotiations, as has recently been suggested by the U.S. Chamber of Commerce and Am Cham China. The countries began negotiating a BIT in 2008 with limited progress. The U.S. and China should revisit this effort and set an aggressive timeline of nine months to complete the agreement. Pursuing a high quality BIT would serve several core U.S. interests. First, it would provide the U.S. with an opportunity to shape rules that could address China's key trade and investment practices the U.S. finds so objectionable. Second, a BIT would further a rules-based approach to dealing with China. Third, it would develop another mechanism for the U.S. to hold China accountable through enforcement measures, as a BIT could include a state-to-state as well as an investor-state dispute settlement mechanism

What should no longer be a focal point for the U.S. in bilateral negotiations

It is also worth noting what should not guide the negotiations or determine success: namely commitments by China to increase purchases of U.S. exports and a reduction in the bilateral trade deficit.

Without a doubt, U.S. business, farmers, and ranchers aim to export more to China. However, increased U.S. exports, whether to China or elsewhere, need to be in response to market forces and not undercut broader U.S. demands for less state intervention. Such an arrangement would be inconsistent with U.S. values and adopt a managed trade framework, more akin to the Chinese model. In the short-term, a large increase in exports to China would also likely mean the U.S. exporting less to other countries. China agreeing to purchase more U.S. goods would also likely violate China's most favored nation (MFN) WTO commitment, as a decision to buy more U.S. energy or agriculture exports would mean purchasing less from other countries. Such an outcome would also disadvantage U.S. allies.

The U.S. should also not make reducing the bilateral deficit a focus of the negotiations. For the reasons outlined above, the U.S. should focus on pushing for economic reform and more market access.

The function for the WTO

Despite the challenges the organization has had over the past few years, the WTO should play a central role in framing the issues at play in the U.S.-China trade dispute. As noted, the WTO is the only multilateral set of agreed upon rules and norms of behavior for assessing the impact of the Chinese economic model on international trade. Seeing the WTO in this way allows the U.S. to identify where China fails to comply with existing commitments as well as demonstrate where WTO rules are unable to discipline Chinese trade practice and where bilateral or unilateral action may be necessary. The administration made an important step in this direction in its recent report on China's compliance with its WTO commitments. In that report the Administration advanced a broad claim that China made "representations that it was committed to increasing the market-orientation of its economy and trading system, reforming state-owned enterprises so that they operate independently and in accordance with market principles and introducing a pricing system that reflects supply and demand." Here, the administration is going beyond legal claims per se to express that China has not fulfilled "the expectations of Members" by acting inconsistently with the expectations that come with WTO membership.

As noted earlier, China reiterating its commitment to comply with its WTO Protocol of Accession should be a bilateral priority and its enforcement (outside a BIT) should be done through the WTO dispute settlement system. The U.S should also develop a broader portfolio of WTO cases against China on the issues of technology transfer, IP, and SOEs especially since, in most cases where China has lost a WTO cases, it has usually complied. Though USTR claims that 23 WTO cases have been brought against China, so far Trump's USTR has initiated only one case against China and continues to litigate a few more started under the Obama administration. A former American WTO Appellate Body member has made the case that a range of Chinese practices of particular concern to the U.S., such as access to trade secret, forced technology transfer, lack of IP enforcement, and Chinese subsidies to SOEs could be litigated at the WTO.

There are further areas where the U.S. and allies should seek to work within the WTO. This is not to underestimate the challenges of making progress in the WTO given the diverse membership and institutional challenges. The U.S. and China would need to have the political will to make progress on some of their bilateral issues in the WTO context. Taking a more multilateral approach to some of the bilateral trade issues could also give President Xi political cover to make commitments which he would not be able to undertake unilaterally.

In terms of what the U.S. could seek to pursue at the WTO, first, the U.S. should work with China to agree to an in-depth review at the WTO of China's compliance with its WTO accession agreement. Second, the U.S. should work through the WTO to ensure that China actually gives a full accounting of its SOE activities and subsidies as required of any WTO member and pursuant to its Protocol of Accession. Third, the U.S. should work with allies and China to reintroduce the China specific safeguard as well as craft an agreement with China regarding the ongoing use of NME methodology until such time that China is able to substantiate that it has become a market economy. Progress on the NME issue could be the result of a negotiated settlement of the WTO case that China has brought against the EU and U.S. regarding their continued use of NME methodology in trade remedy cases. Fourth, working to reform the WTO dispute settlement system to ensure quicker dispute settlement proceedings, including potential injunctive relief for unfair trade practices, would be an institutional change that would be useful vis-à-vis China.78 Fifth, the U.S. should use a bilateral deal with China or a BIT as the basis for re-energizing the negotiation of new rules at the WTO on areas such as technology transfer, SOEs, and digital trade.

Work with U.S. allies

A key part of the U.S. strategy with respect to the China challenge should be to have a forward-looking trade policy to conclude free trade agreements (FTAs) with allies that raise the standards for trade. Apart from the economic benefits for the U.S. FTA partners, such agreements would create economic costs to China, which could encourage China to reform its economy and trade practices.

The key U.S. rationales for negotiating the TPP, from which President Trump withdrew the U.S. in January 2017, were just that. The TPP was a high-standard agreement that would have expanded trade amongst the TPP parties, many of which are also U.S. allies, such as Japan, and important trading partners for China. The TPP included important new rules in areas that matter for the U.S. such as on SOEs, digital trade, and transparency and due process in the making of regulations affecting trade. With China outside the trading block, TPP would have created costs for China. According to one estimate, TPP would have decreased Chinese income by $40 billion annually and this would have grown as more countries joined the agreement.79 Taken together, TPP would have been an important part of the "comprehensive toolkit" USTR refers to in creating pressure on China to reform. The TPP has now been reconstituted without the U.S. as the CPTPP and most of the rules for addressing U.S. concerns with Chinese trade practices, remain. The importance of the CPTPP for addressing the China challenge warrants the U.S. to reconsider its position on the agreement and re-join.

In the event that bilateral FTAs remain the focus for the time being, the U.S. should aim to conclude bilateral agreements with its strategic allies in the Asia-Pacific region, such as Japan, Thailand, Vietnam, Malaysia, and other countries counted among China's largest trading partners.80 While the current focus of the Trump administration on bilateral FTAs is no substitute for larger regional or plurilateral trade agreements and would be time-consuming and challenging to negotiate, high standard bilateral FTAs would provide these countries with preferential access to the U.S. and include new rules in areas such as SOEs and digital trade. Such FTAs would also provide a basis for the U.S. to ensure that its FTA partners reform their economies and trade practices in ways consistent with U.S. interests and values. The U.S. has already begun "trilateral talks" with the Japan and EU that include topics such as technology transfer, the role of SOEs, and subsidies, and outcomes here could be included in bilateral FTAs with these partners.

Unilateral U.S. movement

How the U.S. fairs in its competition with China will ultimately be determined by actions that the U.S. takes at home. Apart from focusing on its own competitiveness through domestic policies, which are beyond the scope of this policy brief, the U.S. should thoughtfully control access to U.S. technologies through foreign investment and export controls, and use WTO-consistent tariff policies to minimize the harm from Chinese economic practices on U.S. businesses.

Take domestic motion to deal with China's era transfer necessities

The U.S. has already made progress domestically on addressing technology transfer issues with the enactment of the Foreign Investment Risk Review Modernization Act (FIRRMA), which included the Export Control Reform Act (ECRA) of 2018. While prima facie country-neutral, FIRRMA/ECRA was intended to address concerns over Chinese investment into the U.S. in "critical technologies," defined as "emerging" and "foundational" technologies, as well as create, through the U.S. export control system, controls over the export of such technologies. Notably, the legislation expands the Committee on Foreign Investment in the United States (CFIUS) review process to all "non-passive" foreign investments in companies that deal with critical technology, "critical infrastructure," or sensitive personal data of United States citizens that may be exploited in a manner that threatens national security, among other things. The legislation also requires the U.S. to regulate exports of "emerging" or "foundational" technologies essential to national security that do not fall under U.S. export controls—expanding on the current technologies subject to export controls. While what constitutes such technologies has yet to be determined, the technologies currently targeted for review include additive manufacturing, autonomous vehicles, advanced battery, biotechnology, gene editing, and superconducting technology.

How the U.S. implements FIRRMA/ECRA will be key to whether concerns over technology transfer to China are addressed adequately. Company decisions as to which technologies to transfer overseas tend to be short-term, risk-based decisions driven by costs, actions of competitors, and returns to shareholders. Companies may not always make optimal decisions due to information asymmetries—where the opportunities of being in China are often high and more easily quantifiable, given the size of Chinese market, while the downside risks are harder to assess. There may also be a mismatch between the business assessment of the risks of technology transfer and theft and the national security costs to the U.S. Individual company decisions to transfer technology may be rational, but the collective outcome where China uses IP and know-how gained across multiple foreign investments to gain control or leadership in a particular a technology sector can create additional national security risks. The implementation of FIRRMA/ECRA is important for addressing this collective action problem and for considering the national security costs that may not be properly included in private sector decisions regarding the transfer of technology to China. The export controls that ultimately result from the FIRRMA/ECRA process could also help U.S. companies push back against ongoing Chinese demands for technology transfer. The implementation of FIRRMA should be carefully targeted and not designed to stifle inbound or outbound investment by making clear that there are significant sectors where Chinese investment is welcome. This is consistent with the importance of having a targeted response to the threat that has been identified—avoiding unnecessary economic costs for the U.S. and leaving room for ongoing mutually beneficial economic relations with China.

FIRRMA/ECRA also recognizes the importance of working with allies to strengthen multilateral export control regimes and prevent diversion through U.S. allies in attempts to avoid FIRRMA review. The U.S. will need to convince other governments to adopt similar investment and technology export restrictions in order for these U.S. reforms to be most effective. U.S. restrictions on access to U.S. technology will be less effective and hurt U.S. competitiveness if similar technology is available from the EU or Japan. Here, progress has already begun as Germany, France, and the U.K. have also tightened review of foreign investments on national security grounds and the EU has established a mechanism for cooperation and sharing and information amongst the Commission and Member States on investment from counties that may affect security or public order.

Trade remedial actions

Making progress on China's compliance with its WTO commitments will be most effective where the U.S. is also complying with its WTO commitments. This would require the U.S. to calibrate its unilateral use of tariffs, which have undermined the WTO. Instead, the U.S. should expand its use of trade remedy measures—anti-dumping and countervailing duties—that are consistent with U.S. WTO obligations and provide recourse to U.S. business for China's unfair trade practices.

4. CONCLUSION

U.S.-China economic relations are at an important crossroads. Developing a durable basis for mutually beneficial economic relations will require benefits for both economies while upholding U.S. values of market-based solutions and reaffirming the importance of the rules based international economic architecture. Failure for the U.S. and China to find ways to resolve their differences will strengthen the hand of those arguing for U.S. disengagement from China, with all the costs that would entail for both countries.

As outlined in this policy brief, the U.S. and China have a complex economic relationship, which has borne benefits and costs for the U.S. While many U.S. producers and consumers have reaped billions of dollars of gains from the relationship, concentrated employment effects in manufacturing have been acute and concerns over Chinese IP theft and forced technology transfer now threaten U.S. knowledge-based industries. What makes these emerging concerns all the more problematic is the role of the state in the Chinese economy, which systematically tilts the playing field in favor of Chinese businesses domestically and globally. Furthermore, China's use of industrial policy, and control over SOEs and the provision of pervasive subsidies has become of even greater concern for the U.S. as China has focused its attentions on dominating certain technologies and supplanting U.S. leadership. Alongside ongoing cyber theft of U.S. technology and IP, these economic practices also raise U.S. national security concerns.

The Chinese economic model has also revealed the limits of the WTO. Combined with other challenges the institution has faced, the effects of China on the world trading system have undermined U.S. faith in the institution. However, while the WTO is not able address all the issues that China poses, it remains central as the only global set of trade rules which both reflect core U.S. values, such as non-discrimination, transparency and rule of law, and provide a forum to discipline Chinese economic practices.

To address the challenges China poses, this brief argues that the U.S. should thus undertake a comprehensive strategy including bilateral, multilateral, unilateral actions, and work with allies. Bilateral negotiations should be the key forum for making progress. Here, the challenges are both agreeing on a substantive agenda and developing mechanisms that create incentives for Chinese compliance. Mere reaffirmation by China of commitments already made is insufficient. The U.S. and China should consider using WTO arbitration as an enforcement mechanism and seek a WTO waiver of any bilateral deal that includes WTO inconsistent measures, such as tariff snapbacks or WTO plus commitments, to maximize compliance and minimize impacts on the rules based system. The U.S. and China should renew efforts to complete a comprehensive bilateral investment treaty (BIT) with an aggressive nine-month schedule. It is also important that the U.S. not simply agree to Chinese offers to buy more exports. This strategy would yield short-term gains but would require the U.S. to co-opt managed trade with China, at the cost of the U.S. commitment to WTO consistent, market-based international trade outcomes.

At the WTO, the U.S. should work through the institution to expose where China's economic practices depart from its WTO commitments and where possible, the U.S. should increase its use of WTO dispute settlement to challenge China's WTO non-compliance. The U.S. should work with its allies and China to reintroduce the China specific safeguard and ensure China's continued treatment as a non-market economy for trade remedy purposes. In addition, China and the U.S. should commit to use any bilateral deal as a launching point to make rapid and comprehensive progress on new trade rules at the WTO in areas, such as reformed dispute settlement, technology transfer, SOEs, and digital trade.

The U.S. should not take on these ambitious plans alone. It needs to work closely with allies to develop new trade rules and to create incentives for China to reform its economy and trade practices. Joining the CPTPP would be the quickest way to reinforce a range of new trade rules important to the U.S., including on IP protection, SOE reform, and digital trade. Expanding CPTPP membership would increase the costs to China for non-participation, creating an incentive for

China to reform. If re-entry into the CPTPP proves elusive, the U.S. should undertake an ambitious bilateral FTA policy to achieve similar ends.

Finally, the U.S. has a number of unilateral actions it should also explore to better deal with the challenges China presents. Targeted use of the foreign investment review process and export controls will be an important response to China's quest for U.S. technology. Heightened use of WTO-consistent trade remedy tariffs should also be in the U.S. toolkit.

If the current level of U.S.-China trade tensions remain for an extended period of time, bilateral trade and investment are likely to decrease, which would be a lose-lose for both sides. The U.S. and China have a historical opportunity to level the playing field between the world's two largest economies to ensure not only growth and prosperity for both countries but the world economy and the global trading system.

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