CHINA-US TRADE RELATIONS: WHAT UNDERLIES THE LATEST TENSION?

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Executive Summary

1. China-US economic relations have deteriorated sharply since early 2018. Beginning in June, trade tension had further escalated. At present, the world's two largest economies are engaged in a serious trade debate that could evolve into an all-out trade war.

2. In its economic ties with China, the United States is frustrated by first, the large and expanding bilateral trade imbalance, considered harmful to US jobs and economic well-being.

3. Second, the concern that the United States is losing its comparative advantage over China in various advanced technology-intensive sectors. Nearly half of China's exports to the United States now are those of "machinery and electrical products".

4. Third, the slow progress in China's reforms and economic liberalisation in recent years as perceived by the American government and businesses. In particular, the Trump administration is convinced that the strong involvement of the state in the economy is central to both the persistent trade imbalance and China's rapid catching up in advanced technology.

5. Chinese government policies are accused of being mercantilist. Measures including import tariffs and cheap financing provision have been used to promote exports.

6. There is also the belief that the development of China's high-tech industries is sustained by various state-sanctioned policies. Forced technology transfer from foreign multinationals and poor intellectual property rights protection are cited as examples. The *Made in China 2025* has also unnerved the Americans with its aim to enhance the development of indigenous technologies in key sectors.

7. The United States is seemingly using trade imbalance as a pretext to pressure China to make serious changes to how the government manages the economy. This presents great challenges to both sides.

8. Addressing bilateral trade imbalances through trade-related measures is almost impossible when global supply chains and regional production networks have become essential features of world trade.

9. Conversely, escalating trade tensions between China and the United States will have serious negative spillovers to the rest of the world. Uncertainties concerning bilateral economic ties have become a key risk for the world economy.