CHINA-US TRADE WAR:
A MODERN VERSION OF
THE THUCYDIDES TRAP

XING Yuqing

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Executive Summary

1. The ongoing China-US trade war is not a military conflict, but one that is similar to the "Thucydides Trap" concept in terms of the competition for economic dominance in the world. It is a rational US response to challenge China's rising economic power.

2. The Trump administration expects to use the trade war to rewrite trade rules, force China to further open its market to American firms, and abandon the practices distorting the competition between American and Chinese firms to allow the United States to compete with China on a level playing field.

3. The trade war has entered a tit-for-tat mode. On 3 April 2018, the Office of the US Trade Representative listed $50 billion Chinese goods for 25% tariff; on 17 September, a 10% tariff on another $200 billion Chinese goods was imposed. The Chinese government vowed to slap $110 billion of American goods with the same levy. The two countries are unlikely to arrive at a compromised agreement anytime soon.

4. The Trump administration claimed that the trade with China is without reciprocity. It accused China of forcing American companies to transfer technology to Chinese firms and distorting market competition with industry policy and massive subsidies. The 301 investigation report on China cited cases that support the claims.

5. The Chinese government refuted all the allegations, insisting that it has no obligation to adopt reciprocal tariffs as it is a developing country under World Trade Organisation rules. It argues that "Market for Technology" practices are not "forced technology transfer", and industry policy and government subsidies are essential for China to catch-up with advanced countries in technology innovations.

6. China's "unfair practices" have existed since its opening up. The huge trade deficit, massive loss of US manufacturing jobs and rising income disparity, which the imports from China are partially responsible for, have negatively impacted the view of the US government on trade with China after Trump's election.

7. The China-US trade war is asymmetric and China will certainly be the bigger loser. The trade war has shaken the confidence of Chinese investors. The index of Shanghai stock exchange broke the resilience of 3,000, down more than 20% since the peak in late January of 2018. Chinese yuan also suffered.

8. Foreign investors may be forced to leave China in order to avoid the tariff. Foreign investor firms using China as an export base for the US market may cut their orders in the Chinese factories or relocate the production facilities out China. A few Japanese firms have moved their Chinese factories back to Japan.

9. It is in the best interest of China to end the trade war soon. Negotiation not retaliation is the solution of the trade war. China has benefitted more than the United States from the existing trade system. China could now further open its domestic market.

10. EU and Japan are important markets of Chinese exports. The China-EU FTA and China-Japan-Korea FTA may give China a leverage to counterbalance the pressure of the United States. China should be ready to offer significant concessions in opening its domestic market and embracing “not made in China”.