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U.S.-China Trade and Economic Relations: Overview

As U.S.-China economic ties have grown, so have U.S. concerns about China's trade and investment practices, including the state's increasingly direct and powerful role in the economy and policies requiring many U.S. firms to disclose sensitive proprietary information to operate in China. Beijing's slowness to acknowledge and address priority U.S. concerns while Chinese firms expand offshore has highlighted uneven levels of market openness, divergent approaches to global rules, and significant differences in the operating conditions and tenets of the U.S. and Chinese economic systems, including clear separation of government and business interests, protections of freedom of information and expression, privacy and intellectual property (IP), and the impartial rule of law. Feeding U.S. concerns are an uptick in reports of Chinese corporate espionage, Beijing's tightening of information controls (and pressure on U.S. firms to abide by these controls), tit-for-tat retaliation, and industrial policies incentivizing the transfer of U.S. IP to the government and military.

To address these issues, the Trump Administration has undertaken policy actions that include invoking Section 301 of the Trade Act of 1974 (19 U.S.C. §2411) to target Chinese industrial policies and IP abuses, strengthening U.S. investment and export control authorities, and stepping up efforts to stem Chinese espionage. The Administration has sanctioned Chinese firms for violations of U.S. sanctions, theft of U.S. IP, ties to the Chinese military in dual-use sectors, and provision of surveillance technology to the authorities in the western Chinese region of Xinjiang. Supporters of the Administration's stance assess these actions will better position U.S. firms and advance U.S. economic interests. Others warn that frictions could reduce commercial flows and threaten U.S. growth. Some Members seek additional action to address China's coercion of U.S. firms, use of a "social credit system" to influence corporate behavior, and adoption of military-civil fusion policies that blur commercial and military distinctions.

Section 301

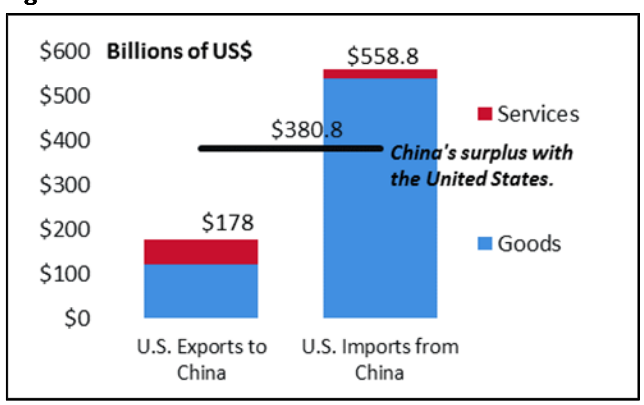
In March 2018, the U.S. Trade Representative (USTR) issued its investigation findings of Chinese policies related to technology transfer, IP, and innovation under Section 301 of the Trade Act of 1974. USTR concluded that four practices justified U.S. action: forced technology transfer requirements, cyber-enabled theft of U.S. IP and trade secrets, discriminatory and nonmarket licensing practices, and state-funded strategic acquisition of U.S. assets.

The United States and China signed a phase one trade agreement on January 15, 2020, to resolve some issues raised through Section 301. China committed to strengthen IP enforcement and improve access in agriculture and financial services—sectors important to the U.S. economy, but outside the 301 investigation's scope—leaving most U.S. concerns on IP, technology transfer, industrial policies, and state subsidies to phase two. Most Members assess the deal to be only a first step. U.S. businesses are warning that China is doubling down on industrial policies.

China committed to purchase at least $200 billion above a 2017 baseline amount of U.S. agriculture ($32 billion), energy ($52 billion), goods ($77.7 billion) and services ($37.9 billion) between January 2020 and December 2021, but stated that purchases will be market-based, suggesting amounts could be lower. Official Chinese and U.S. trade data will be used and the deal is silent on valuing purchases, opening potential disagreement on implementation.

Both sides delayed proposed December 15 tariffs. For U.S. tariffs enacted on September 1, 2019, the United States is to on February 14, 2020, cut the rate from 15% to 7.5%. China extended September tariff exemptions for autos, auto parts, pork, and soybeans, and may selectively exempt rather than cut tariffs. Other U.S. and Chinese tariffs enacted since March 2018 remain in effect. The United States has imposed increased 25% tariffs on three tranches of imports from China worth approximately $250 billion. China, in turn, raised tariffs (at rates ranging from 5% to 25%) on $110 billion worth of U.S. products.

Figure 1. U.S.-China Trade in 2018

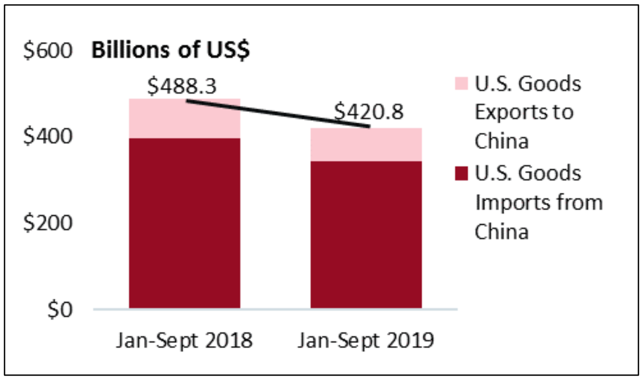


Source: CRS: data from U.S. Bureau of Economic Analysis (BEA).

Bilateral Trade and Investment

U.S.-China commercial ties expanded greatly over three decades. In 2018, China was, in terms of goods, the largest U.S. trading partner (with total trade at $660 billion), the third-largest U.S. export market (at $120 billion), and the largest source of U.S. imports (at $540 billion) (**Figure 1**). China is the second-largest foreign holder of U.S. Treasury securities (at $1.11 trillion as of June 2019). As the United States and China have increased tariffs since 2018, year-to-date (YTD) bilateral trade flows decreased in the first three quarters of 2019, with U.S. goods exports to China falling by 16%, while U.S. imports from China fell by 13%, according to official U.S. data **(Figure 2).**

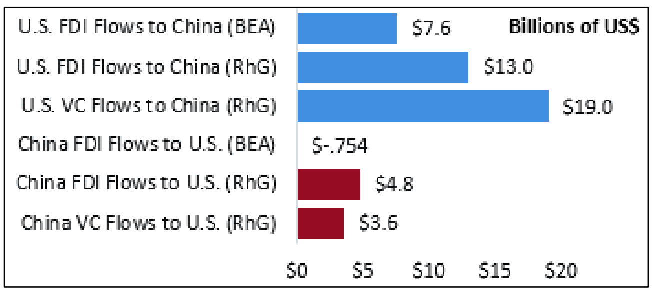
Figure 2. U.S.-China Trade in 2018 and 2019



Source: CRS: data from U.S. Bureau of Economic Analysis (BEA).

Foreign direct investment (FDI) flows in both directions have slowed since 2017. RhG estimates China FDI into the U.S. went from $45.5 billion in 2016 to $29.4 billion in 2017 and $4.8 billion in 2018, but announced deals show China's sustained interest in U.S. biotech, health, and technology sectors through commercial ties not captured in FDI data (e.g., venture capital, private equity, research and development, and open source technology platforms).

Figure 3. U.S.-China FDI Flows in 2018



Source: CRS with data from BEA and the Rhodium Group (RhG).

Notes: VC = Venture capital. BEA records net flows and may undercount FDI by not capturing all FDI via other countries, territories, or tax havens, or acquisitions made by U.S. affiliates of foreign firms. RhG records gross flows and attempts to identify FDI by Chinese firms regardless of where firms are based or sources of money for investment.

Trade Deficit. President Trump has raised concerns about U.S. trade imbalances with China. Some view the bilateral trade deficit as an indicator of Chinese trade barriers—including currency manipulation and Chinese policies and practices that discourage direct U.S. exports and incentivize manufacturing in China. Others view conventional data on the trade deficit as misleading because China's role as a point of assembly in global supply chains means Chinese export data includes the value of imported inputs from other markets. In August 2019, the United States formally labeled China a currency manipulator under the terms of the 1988 Trade Act, the first such designation in 25 years, and lifted the designation in January 2020 in response to China's currency commitments in the phase one trade deal.

Industrial Policies, Technology, and IP. To further its national development goals, China's government employs interrelated industrial policies that seek the transfer of foreign IP and knowhow to China in sectors in which the United States has strong comparative advantages. These policies, such as *Made in China 2025*, feature a heavy government role in directing and supporting Chinese business and include government-set targets, government-guided funds, subsidies, tax breaks, low-cost loans, trade and investment barriers, and discriminatory IP, procurement, and standards practices. U.S. companies are also concerned about China's cyber and data policies that require the disclosure of sensitive information. In 2018, the U.S. National Counterintelligence and Security Center warned that China's "expansive efforts in place to acquire U.S. technology to include sensitive trade secrets and proprietary information," if not addressed, "could erode America's long-term competitive economic advantage."

National Security. Congress and the Administration have responded to national security concerns about China's industrial policies and role in technology supply chains. Citing a "national emergency," the President in May 2019 issued Executive Order 13873, stating that U.S. purchases of information and communications technology (ICT) goods and services from "foreign adversaries" pose a national security risk and authorizing the federal government to ban ICT transactions deemed to pose an "undue risk." The U.S. Department of Commerce responded by adding Chinese firm Huawei and 68 of its non-U.S. affiliates to the Bureau of Industry and Security's Entity List, generally requiring an export license for the sale or transfer of U.S. technology, but has issued waivers. Efforts to tighten gaps in these policies are exposing U.S. interagency debates about the potential impact on U.S. technology firms. Legislation enacted in 2018 (P.L. 115-232) reforms U.S. foreign investment review and export control authorities. Some Members are concerned about the delay in establishing new controls on certain emerging and foundational technologies that are required to implement both the investment review and export control reforms.

Industrial Overcapacity. China is a top global steel and aluminum producer. In 2009, it issued 13 industry support plans allowing its firms to expand steel and aluminum capacity while much of the world dialed back. Assessing persistent global overcapacity, the United States in March 2018 announced tariffs on all aluminum (10%) and steel (25%) imports citing national security concerns (Section 232, Trade Expansion Act of 1962, PL 87-794). China responded by raising tariffs by 15% to 25% on $3 billion of U.S. exports and filing a World Trade Organization case.

Financial Markets. Some Members are concerned about China's access to U.S. capital markets. Responding to warnings by the Securities and Exchange Commission and the Public Company Accounting Oversight Board that they cannot inspect the work of auditing firms in China that examine U.S. listed firms, S. 1731 and H.R. 3124 would require Chinese firms that fail to meet U.S. auditing requirements to delist from U.S. exchanges. H.R. 2903 would bar the U.S. government's Thrift Savings Plan (TSP) from investing "in any entity in peer or near-peer competitor nations," a category that would include China.

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