China’s Economic Rise & Its Potential Implications on the World Economic Order as We Know It

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Note: The views expressed in this presentation do not represent those of the USITC or any of its individual Commissioners
Agenda

• How Fast is China Growing?
• Why Has it Grown so Fast?
• Is it a Rival or Partner to the U.S.?
• Implications of its Rise on the Global Economic Order
• Implications for the Policy Tools the U.S. Traditionally Uses to Address Unfair Trade Practices
1. How Fast is China Growing?
Real GDP Growth

Source: World Bank Development Indicators
GDP Per Capital
(in thousands $U.S.)

Source: IMF's World Economic Outlook (Apr 2019)
2. How Did China Grow So Fast?
2. How Did China Grow So Fast?

- Improved Resource Allocation (ended AG reliance)
- Careful, Experimental, and Nimble Planning
  - Opposing ideologies ok, “Growing Out of Plan” (Naughton)
- Became Global Manufacturing Hub
  - Assemble, Export, & Become GVC Glue
- ↑ FDI, “Learned” Technology, Now Leading Innovation?
- Expanded Outwards for Resources & Markets
Evolved From Agrarian Society

## Composition of China’s GDP

<table>
<thead>
<tr>
<th>Year</th>
<th>Agriculture (Primary)</th>
<th>Industry (Secondary)</th>
<th>Services (Tertiary)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1950</td>
<td>50%</td>
<td>21%</td>
<td>29%</td>
</tr>
<tr>
<td>1978</td>
<td>28%</td>
<td>48%</td>
<td>25%</td>
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<tr>
<td>2018</td>
<td>7%</td>
<td>41%</td>
<td>52%</td>
</tr>
</tbody>
</table>

Source: China’s National Bureau of Statistics (through CEIC)
**Careful Planning (Medium-Term)**

**Modest goals**

China’s GDP, % increase on a year earlier

<table>
<thead>
<tr>
<th></th>
<th>Actual</th>
<th>Five-year target</th>
<th>Five-year average</th>
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<tbody>
<tr>
<td>8th</td>
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<td>9th</td>
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<td>10th</td>
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<td>12th</td>
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</tbody>
</table>

**FIVE-YEAR PLANS:**

<table>
<thead>
<tr>
<th>Year</th>
<th>GDP 1991</th>
<th>GDP 95</th>
<th>GDP 2005</th>
<th>GDP 10</th>
<th>GDP 15</th>
</tr>
</thead>
<tbody>
<tr>
<td>1991</td>
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<td>95</td>
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<tr>
<td>2000</td>
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<td>05</td>
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<td>10</td>
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<tr>
<td>15*</td>
<td></td>
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</tbody>
</table>

Sources: National Bureau of Statistics; Thomson Reuters; IMF

*Forecast †Revised up from 6.0 to 8.5

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**GDP and per capita personal income**

- Annual GDP growth: 6.5% or above
- R&D spending: 2.5% of GDP

**Science and technology’s contribution to economic growth**

- 60% of the total population
- 45% of permanent urban residents
- 80% of big cities
- 50 million more than before

**High-speed railways in service**

**Energy consumption per unit of GDP**

**New urban jobs**

- 20 million

**Housing units rebuilt in rundown urban areas**

**Increase in average life expectancy**

1 year
Careful Planning (Long-Term)

Ten core industries set the basis of Made in China 2025

- Biomedicine & high-performance medical equipment
- Next-generation IT
- High-end computerized machines & robots
- Aviation & space equipment
- Maritime engineering equipment & high-tech ships
- Advanced railway transportation equipment
- Energy-saving & new energy vehicles
- Energy equipment
- Agricultural equipment
- New materials

Main steps

<table>
<thead>
<tr>
<th>Year</th>
<th>Milestones</th>
</tr>
</thead>
<tbody>
<tr>
<td>2025</td>
<td>Major manufacturing power</td>
</tr>
<tr>
<td>2035</td>
<td>Global manufacturing power</td>
</tr>
<tr>
<td>2049</td>
<td>Leading manufacturing superpower</td>
</tr>
</tbody>
</table>

Source: State Council
Growing Out of the Plan

China: Gross Value of Industrial Output & Urban Employment (% from State-Owned Firms)

Source: China’s National Bureau of Statistics
SOE Trade: Down But Not Out

From Hammer and Jones, “SOEs Play a Smaller, But Still Strategic, Role in China’s External Sector” Jan 2018
Built a Global Manufacturing Hub
Built a Global Manufacturing Hub

Share of World Trade
(Merchandise Exports + Imports)

Source: World Bank Development Indicators
Lead Innovation?

R&D Expenditures (in % of GDP)

Global Patent Applications (in % of Total)

From “The Mysterious Divergence in China’s Productivity and Innovation Patterns” (Bernard and Hammer, Aug 2019)
China's Belt and Road Initiative (BRI) is the most ambitious infrastructure plan in world history. Connecting Guangzhou to Venice by sea and Beijing to Brussels by land, this massive undertaking already involves 68 countries (including 24 in Europe) that comprise two-thirds of the global population. The BRI is a multi-pronged plan that reimagines global supply chains, technological connectivity, and military strategy.
3. Is China a Partner or Rival to U.S.?

**Partner**
- U.S. Consumer Welfare
- Major Investor
- Largest Consumer Growth Market
- Foreign Invested Enterprises
- Manufacturing Offshoring
- Global Value Chain Partner
- “Stable” Trade Partner

**Ambiguous**
- Trade Balance
- Currency Valuation
- Treasury Bonds
- Manufacturing: Jobs vs. Productivity/High-Tech Focus

**Rival**
- Unfair Competition in China (e.g. SOEs)
- Unfair Trade (e.g., AD, CVD)
- IP Infringement & Forced Tech Transfer
- Internationalization of FX
- Innovation Race
- Securing Global Resources
- FDI & Soft Power

**Manufacturing:** Jobs vs. Productivity/High-Tech Focus
The US-China merchandise trade balance reached $419 billion in 2018 (before real trade war effects kicked in).

Source: USITC Dataweb
…far surpassing other major trade partners.
FIEs are playing an important role in China’s exports to the U.S. ...
…FIEs also playing an important role in China’s imports from the U.S. ....
U.S. firms finding cost advantages in manufacturing, selling, and even doing R&D in China.
The majority of workers of U.S. affiliates in China are in the computer (semiconductor) sector.
U.S. imports from Asia remained fairly flat in past 2 decades...
..but their composition is totally different.
So companies no longer doing this, but importing directly from China.
Given lower final assembly costs in China, companies (e.g., Apple, Dell computers) are doing more final assembly in China.
China holds over $1 trillion $U.S. reserves (18.8% of total, and 4th highest after Japan, Cayman Islands, UK).

However, selloff would likely harm China more (needs stable investment).

Source: CRS (Morrison), "China-U.S. Trade Issues", July 30 2018

**China’s Holdings of U.S. Treasury Securities: 2002-2017**

($ in billions)

Source: U.S. Department of the Treasury.

Notes: Data are year-end and exclude Hong Kong and Macau, which are treated separately.
U.S. Manufacturing Jobs ↓, BUT Manufacturing Output & High-Tech Specialization ↑
IP Infringement from Chinese Entities: Real & Consequential

FIGURE ES.1 U.S. IP-intensive firms that reported IPR infringement in China accounted for 58.1 percent of the total sales of firms in the U.S. IP-intensive economy that were conducting business in China, 2009

<table>
<thead>
<tr>
<th>Total sales by U.S. IP-intensive firms ($7.3 trillion(^3) in 2009)</th>
</tr>
</thead>
<tbody>
<tr>
<td>By firms doing business in China ($5.9 trillion in 2009)</td>
</tr>
<tr>
<td>Reported IPR infringement in China (58.1%)</td>
</tr>
<tr>
<td>Did not report IPR infringement in China (41.8%)</td>
</tr>
<tr>
<td>By firms not doing business in China ($1.4 trillion)</td>
</tr>
</tbody>
</table>

TABLE ES.2 Summary of potential U.S. gains from IPR improvement in China (based on statistical and simulation analysis)

<table>
<thead>
<tr>
<th>Economic gains from statistical analysis</th>
</tr>
</thead>
<tbody>
<tr>
<td>Exports of goods and services to China</td>
</tr>
<tr>
<td>Goods</td>
</tr>
<tr>
<td>Services</td>
</tr>
<tr>
<td>Receipts of royalties and license fees from China</td>
</tr>
<tr>
<td>Other services</td>
</tr>
<tr>
<td>Sales of U.S. majority-owned affiliates in China</td>
</tr>
<tr>
<td>U.S. exports to affiliate firms in China (subtracted)(^b)</td>
</tr>
<tr>
<td><strong>Total increase in U.S. exports to China and sales to U.S. affiliates in China</strong>(^b)</td>
</tr>
<tr>
<td>Net income of affiliates (profits)(^c)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Economic gains from simulation analysis</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fixed employment scenario:(^d)</td>
</tr>
<tr>
<td>U.S. economic welfare</td>
</tr>
<tr>
<td>U.S. profits (as reflected by returns to capital)(^e)</td>
</tr>
<tr>
<td>U.S. net employment effect (in full-time equivalents or FTEs)</td>
</tr>
<tr>
<td>Illustrations of potential labor reallocation to more IP-intensive sectors (FTEs):</td>
</tr>
<tr>
<td>Education and related services</td>
</tr>
<tr>
<td>Recreational and other services (e.g., motion picture production, recorded music)</td>
</tr>
<tr>
<td>Business services</td>
</tr>
<tr>
<td>Software, paper products, and publishing</td>
</tr>
<tr>
<td>Flexible employment scenario:(^f)</td>
</tr>
<tr>
<td>U.S. economic welfare</td>
</tr>
<tr>
<td>U.S. profits (as reflected by returns to capital)(^e)</td>
</tr>
<tr>
<td>U.S. net employment effect (in FTEs)</td>
</tr>
</tbody>
</table>

Source: Compiled and estimated by the Commission.

Sources: Weighted responses to the USITC questionnaire; U.S. Bureau of Economic Analysis; U.S. Census Bureau.
Innovation Race?

R&D Expenditures (in % of GDP)

Global Patent Applications (in % of Total)

From “The Mysterious Divergence in China’s Productivity and Innovation Patterns” (Bernard and Hammer, Aug 2019)
4. Implications of China’s Rise on the Global Economic Order as We Know it
Most Economists Quibble Over When, Not If, China Will Surpass U.S. (Nominal) GDP

Figure 5 - GDP of emerging powers showing dramatic projected growth for India and China. Source: Goldman Sachs
High Tech Manufacturing: Not Just a U.S. Issue

Under Pressure: Industrialised countries will feel the heat of Made in China 2025
Vulnerability of select industrial countries to Made in China 2025

Made in China 2025 aims to substitute foreign imports
Targets for the domestic market share of selected Chinese industries (per cent)

Focus on advanced technologies
Key sectors targeted by Made in China 2025:
- New generation information technology
- High-end computerized machines and robots
- Space and aviation
- Maritime equipment and high-tech ships
- Advanced railway transportation equipment
- New energy and energy-saving vehicles
- Energy equipment
- Agricultural machines
- New materials
- Biopharma and high-tech medical devices
SOE Industrial Output Back on Rise

Note. The data are in year-to-date terms; “Foreign” includes investors from outside China and from Hong Kong, Macau and Taiwan.
Sources: National Bureau of Statistics; The Economist Intelligence Unit.
China: Lending By Enterprise Type
(in percent of total)

Source: China Banking Society and The State Strikes Back (Lardy, 2019)
Other Implications?
5. Implications for the Policy Tools the U.S. Traditionally Uses to Address Unfair Trade Practices
Share of U.S. Imports Subject to AD/CVD Orders

- China
- Rest of the World
- Total

Bown 2017
China’s represents a major share (more than 50%) of AD investigations.

* ROW indicates investigations that do not include Chinese firms, while China indicates investigations that include Chinese firms, but may also include ROW firms.

Source: USITC
China’s represents a major share (more than 50%) of CVD investigations.
...same is true for IP related investigations.
# US-China WTO Disputes, 2002-18

<table>
<thead>
<tr>
<th>Case Status</th>
<th>Complainant</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>United States</td>
</tr>
<tr>
<td>WTO Cases</td>
<td>23</td>
</tr>
<tr>
<td>Settled Early</td>
<td>9</td>
</tr>
<tr>
<td>Ruling for Complainant</td>
<td>10</td>
</tr>
<tr>
<td>Ruling for Respond</td>
<td>0</td>
</tr>
<tr>
<td>Split Decision</td>
<td>0</td>
</tr>
<tr>
<td>Pending</td>
<td>4</td>
</tr>
</tbody>
</table>
SECTION 301 OF TRADE ACT OF 1974

• **Section 301** establishes domestic procedures that allow US companies and unions to petition USTR to enforce US rights under international trade agreements and eliminate unfair foreign government trade practices that adversely affect US investment and exports of goods and services.

• USTR can self initiate

• USTR required to take appropriate action to remove foreign government policies or practices that violates a bilateral or multilateral trade agreement or are "unreasonable, unjustifiable, or discriminatory" and "burdens or restricts US commerce."
SECTION 301 (continued)

• If foreign unfair practices are not eliminated through successful WTO dispute settlement or negotiations, USTR can retaliate against the foreign country.

• Retaliation can take the form of suspending the benefits of trade concessions previously granted by the United States (i.e., tariffs) or other restrictions or fees on the trade of the offending nation.
Thank you!