

China Has Three Trump Cards to Win the US-China Trade War

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China is not afraid of the US on trade issues. It is better for the trade war not to happen since it will hurt both sides. But if the trade war happens, China will win. It may be an unexpected outcome even for US President Donald Trump who, like other US elites, believes the US has advantages.

According to the Office of the US Trade Representative, goods traded between China and the US totaled around \$659.8 billion last year. The US exported \$120.3 billion but imported \$539.5 billion. China makes \$419.2 billion more than the US.

It would seem that China has more to lose in a trade war. But that is not how it works.

Goods the US sold to China through the intermediary trade were not included. And what the US does not mention is its services trade surplus of 40.5 billion against China.

China does not deny the trade deficit with the US. But China's exports to the US are mostly (industrial) processing trade. Many of the commodities China produces belong to US enterprises.

For example, iPhones will be sold back to the US after they are produced by their original equipment manufacturers in Shenzhen and Zhengzhou. These are regarded as Chinese exports, but Chinese companies earn very little money from producing and processing them.

US President Donald Trump's sanctioning of ZTE Corp was equivalent to a warning strike on a battlefield. In addition to the traditional tariff war, the US aimed to seize China by the throat by putting restrictions on China's application of high-end chips.

Nevertheless, Trump realized later that the US would not dare to start a total trade war with China. US high-end chips are indeed the best in the world. Developing and producing such chips are very costly, so chipmakers have to sell them at a very high price to maintain high investment in research and development (R&D) and further create a virtuous circle in the industry. The Chinese market is the key.

The global sales of the chip market totaled \$468.8 billion in 2018, of which China imported over \$300 billion. If Trump totally blocks sales of high-end chips to China, a large number of US chip makers would have to face bankruptcy, which would bring huge damages to Wall Street as well.

In fact, a lack of high-end chips has almost no effect on China other than a mild slowdown in industrial upgrading. China can also seize this opportunity to develop its own high-end chips.

China has three trump cards to deal with the US on trade.

The first one is a total ban on the export of rare earths to the US.

Rare earths are the raw materials for non-ferrous metals, which are indispensable in chip-making. China's rare-earth production accounts for a majority of the world's total.

The US has its own rare-earth reserves but it would take years for the US to restore its own rare-earth industry to meet its needs for chip production. Even when the US finishes re-establishing the industry, China would have completed R&D on high-end chips and started to export its own products.

US national debt is the second card.

China holds more than \$1 trillion of US Treasury bonds. China made a great contribution to stabilizing the US economy by buying US debt during the financial crisis in 2008. The US would be miserable if China hits it when it is down.

The third card would be American companies' market in China.

US companies entered China at a very early time, right after China's reform and opening-up.

They reaped large profits in the Chinese market, higher than Chinese companies earned in the US market.

The US is anxious and arrogant. The growing nationalist sentiment of the US could be beneficial to China.

China will only lose compradors rather than ordinary workers if the US fails to win the Chinese market.

China could be more open in some industries, including insurance, finance, and healthcare, and make more efforts in respecting intellectual property rights.

China must rationalize its behavior with internationally accepted norms, such as globalization, free trade, and multilateralism, whereas the US is on its way to anti-globalization, protectionism, and unilateralism. *

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