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Prospects for China-U. S. Relations After "Phase 1 Trade Deal"

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Global Research, January 26, 2020

Region: Asia, USA
Theme: Global Economy

Last week the US and China finally signed phase 1 of their long awaited trade deal. Despite Trump's hyperbole financial markets reacted in a rather muted way to the 'deal of the century'. The continuing inflation in stock markets is due to the QE4 programme of the US Federal Reserve that's pumping hundreds of billions into the short term debt (repo) market and the purchasing of $60 billion of US Treasury debt every month.

Nearly 2 years after he launched the trade war with China has Trump finally got the deal he originally wanted? Definitely not.

The current deal does not address any of the major structural issues that the US wants China to make concessions over. Those thorny issues seem insurmountable unless China is willing to make major compromises over its national sovereignty reminiscent of the unequal treaties it was forced to sign with Western imperialism during the 19th and 20th centuries.

The second round of the trade war will be much more protracted and problematic and is likely to greatly exacerbate tensions between the two largest economies in the world pushing their relationship to breaking point.

Having said this, Trump has extracted a series of concessions from the Beijing government led by the misnamed Chinese Communist Party (CCP). Effectively, China has conceded the first round of the trade war to the US. giving Trump's re-election prospects a major boost.

This begs the question: why has China signed a trade deal, that makes so many concessions, with a country that is unrelentingly aggressive towards it?

The phase 1 trade deal will also create domestic problems for the CCP leadership which has played the nationalist card for all its worth over the last year and ramped up its anti-American propaganda claiming that it would,"fight to the end". The CCP leadership is in danger of boxing itself into a corner having raised public expectations that it would resist any trade deal which stifled China's economic prospects.

The Chinese population has a long historical memory of concessions made by past governments to the West. It will be interesting to see how the Chinese people react to the compromises made by their government in the 'phase one' trade deal at a time of slowing economic growth. In 2019 China's economy grew at its slowest pace in three decades. This is a major concern to the government which is acutely aware that slowing economic growth poses a threat to social stability and the continued rule of the one party state.

Vincent Kolo a journalist based in China makes the observation that the trade deal:

> "… is very likely to be panned as an "unequal treaty" and an American victory by netizens in China. China's state media has been unusually defensive and restrictive with its coverage of the deal. The normally bombastic Global Times (a government mouthpiece), which in December insisted the rolling back of all US tariffs was the bottom line for reaching a phase one agreement, ran an editorial after the deal was signed admonishing its readers that debating "about who had lost or gained is shallow."

"We urge individuals and forces to exercise some restraint in their nit-picking of the agreement and bad-mouthing future trade negotiations," it wrote.

Can President Xi's government successfully sell the trade deal as an achievement that will benefit China's economy? Time will tell. Let us look at the series of concessions that China made to the United States before considering the domestic and geo-political implications of this trade deal.

Concessions made by China in the 'Phase One' trade deal

The mainstream media has widely reported the $200 billion of agricultrual goods, manufactured goods, energy products and services that China has agreed to purchase during the 2020-2021 period.

The ability of China to purchase this amount of American imports has been questioned by many financial experts, never mind the fact that the EU is threatening WTO legal action stating that the phase 1 deal violates free trade.

Under the terms of the phase 1 deal China's exporters will still be suffering under $360 billion worth of US tariffs that cover two thirds of all goods that Americans buy from China. Conversely, these tariffs will also hurt American shoppers who will pay more for their consumer goods and cut into the profits of many US importers.

If we get into the meat of the 96 page agreement we shall see how the concessions that China has made go much further than these headline catching figures.

Counterfeiting, copyright and intellectual property theft

One of the earliest sections of the agreement deals with counterfeiting, copyright and intellectual property theft for which China has received a bad reputation. The agreement specifies that China will take a whole host of measures to deal with these issues. These measures range from a substantial increase in the number of customs personnel and raising legal penalties to significantly increasing the number of enforcement actions. The agreement puts no obligations on the United States as it merely acknowledges that existing U.S. measures afford effective enforcement.

Agricultural goods

In the politically charged section on trade in agricultural goods we see how the U.S. has successfully pressured China to lower food standards in many areas. In section 3-9 China is now committed to adopting maximum residue limits for growth hormones zeranol, trenbolone acetate, and melangesterol acetate in American beef. These growth hormones in beef have been banned by the EU as potential risks to human health.

China has agree to lift its ban on American pet food containing ruminant ingredients and agrees to no longer carry out Polymerase Chain Reaction (PCR) testing (i.e. DNA testing) on all U.S. pet food products containing ruminant ingredients. However, one recent scientific study into the importance of PCR testing in food safety noted that there is a:

"complex widespread disease of the small grains (wheat, maize, or barley) … *Fusarium* head blight (FHB) produced by the *Fusarium* sp. infection. Besides the considerable loss of yield, it has the ability to produce mycotoxins which are harmful to human and animal consumer.''

More controversially, is the agreement regarding Agricultural Biotechnology. According to section 3-20 China has a year in which to produce an assessment procedure for approval of American food derived from genetically modified microorganisms.

This could prove difficult for the Chinese government which has failed to persuade its people of the merits of GMO foods. In a country plagued by food scandals that have produced violent protests it is no surprise that a nationwide survey in 2018 revealed that 46.7% of people disapproved of GMO food. This is despite government propaganda campaigns telling people that GMO food is safe to eat.

The Chinese government, nervous of public feeling on this emotive issue, has even allowed government organizations to issue duelling official narratives on the safety of GMO food. According to Eugene K.Chow of The Diplomat there is, 'anti-GMO fervour, spread by everyone from popular TV personalities to Maoists and NGOs like Greenpeace.'

Besides this public distrust of GMO food China has its own soybean industry. Its largest producer is based in the north east of the country in Heilongjiang province. Chinese soybeans are GMO free and may be seen by the public to be preferable to GMO soybeans from the United States.

Financial Services

The most perilous part of the phase 1 trade deal is the section concerning the further opening up of China's financial markets to foreign capital. Over the last 10 years China has been very cautious in reducing capital controls and allowing foreign banks and hedge funds to invest in its capital markets.

The 1997 Asian financial crisis was caused by south-east Asian economies allowing foreign speculative capital into their tightly controlled financial markets. Forbes magazine has summed up the dangers posed by this process:

"Once a market deregulates, there'll be lots of speculative investments that go after higher interest rates. But as a result, with excessive amounts of foreign money stacking up, along with hot sectors and hot money, the economy ends up screeching to a sudden halt.

Thailand, Malaysia, Indonesia, the Philippines and other South-east Asian countries …. sought soaring stock markets, higher property prices and increased consumer lending, [just as China currently does-LT] they forfeited control over their financial systems.

Whenever the free-market gets mixed up in a closed controlled financial system, then something will go wrong.''

Economists Fengjuan Xiao and Donald Kimball in examining China's capital controls have concluded that there are many dangers to opening it's economy to international financial markets:

> "As it now stands, there is considerable risk that the outcome of quickly liberalizing capital account transactions will be costly for China. As demonstrated during the Asian financial crisis, there is no stronger, quicker, or more unforgiving punisher of poor financial practices than the power of free capital markets.''

Despite these warnings from history the phase 1 trade deal mandates China to granting banking licences to the "too big to fail" banks of Wall Street. The same banks that created the 2008 financial crisis. Since 2008 they have engaged in a massive crime wave fleecing American consumers and small-medium businesses helping to create the greatest increase in wealth inequality in over a century.

To add insult to injury, the trade deal allows American owned credit rating agencies to operate in China. These are the same credit rating agencies (Standard and Poor's, Fitch Group and Moody's) which gave triple A ratings to sub-prime mortgages that triggered the global financial crisis of 2008. Incredibly, China is now giving them the power to rate Chinese bonds sold to domestic investors and international investors.

The phase 1 trade deal also allows American banks to provide securities investment, fund custody services and to serve as underwriters for all types of non-financial debt instruments. You can imagine the hedge funds and "too big to fail" banks of Wall Street drooling at the prospect of the massive fees they can extract from investors in China.

The phase 1 trade deal also allows American payment processes such as MasterCard and Visa to operate in China. No doubt they see China as a lucrative market in which they can extract large amounts in fees from heavily-indebted consumers.

The phase 1 trade deal gets even worse when it comes to allowing American capital to conduct its parasitical activity within other key areas of the Chinese economy.

China will now allow American financial services providers to acquire non-performing loans directly from Chinese banks. Shareestates a New York investment firm notes the lucrative opportunities of this particular financial market, particularity in real estate where China has seen a massive boom with the growth of its 'ghost cities':

"Non-Performing real estate loans are a huge opportunity for investors who are serious about turning a discounted asset into a positive ROI [return on investment] and potentially a passive income that will keep your returns flowing in for years to come.

In 2019 China's banks had non-performing loans worth over $317 billion which is the highest since 2003. This comes at a time when Chinese authorities have been encouraging domestic banks to sharply increase the number of loans to small and medium businesses to help combat the slowdown in economic growth.

According to Price Waterhouse Cooper this poses systemic risks to China's economy:

> "Yet the real level of bad debt in China might be much higher than the official

> figures, according to some international rating agencies. NPL rates may have already been as high as 15%-21% for the financial system. If that was true, it would mean that if all these were written off, it would wipe out Chinese banks' capital base.''

China's government has overseen a massive credit binge over the last 10 years which has seen the country's total debt rise from [164% of GDP in 2008 to over 300% of GDP](over $40 trillion) accounting for over 15% of overall global debt. Offering non-performing loans to rapacious American banks is unlikely to help the country deal with its gigantic debt hangover.

The phase 1 trade deal also directs China to remove the legal barriers to American owned insurance companies supplying services to China's 19.1 trillion yuan insurance sector. In 2019 Chinese insurers premium income rose 15.9% from 2018 to 1.6 trillion yuan.

To cap it all off, the phase 1 trade deal also allows American owned companies to participate in China's derivatives markets that encompasses speculation in price movements for stock indexes, energy, foodstuffs, precious metals and bonds.

Needless to say, the sum total of all these concessions in the financial services sector amounts to a major retreat by the Beijing government. Now it will give American capital a considerable influence over vitally important sectors of its economy. By allowing foreign capital into its financial markets it remains to be seen whether China will suffer the same fate as the economies of south-east Asia during the 1997 financial crisis that swept the region.

Why has the CCP government made so many concessions to the American empire?

The number one priority of the Beijing government is to maintain economic growth at all costs to avoid the type of mass protests currently afflicting Hong Kong. President Xi and the oligarchs whom he represents have not forgotten the Tiananmen Square uprising of 1989. Social stability must be maintained at all costs.

They are acutely aware that the economic revolution, that has swept the country along since the 1980s, has created an enormous urban population. As long as the desire of the urban population for rising living standards can be met then the CCP government can sleep peacefully at night.

The phase 1 trade deal can be seen as a desperate attempt to help stave off a recession. American tariffs have undoubtedly hurt China's exporters and the limited partial relief on tariffs must have been accepted by Beijing as better than nothing at all.

It could be argued that China is playing for time while its major economic projects such as the Made In China 2025 initiative and One Belt and Road endeavour come to fruition. If allowed to develop unimpeded they will enable China to achieve its objective of becoming a high-tech manufacturing hub.

The phase 1 deal has helped postpone American demands that China abandon its state capitalist model that has played such a major role in the country's emergence as an economic powerhouse. American capital would love to see China privatize its strategic state developed industries as happened in Russia during the wild west days of the Yeltsin regime.

The China Worker publication makes the perceptive comment that Xi's regime felt squeezed by a number of intersecting forces that exerted an:

> "…enormous pressure to sign the deal and stave off further tariff increases, given a banking sector crisis which is beginning to flash red warning lights, an accelerating slump in investment and consumption, and fear of significant social unrest. The regime fears the effects on mass consciousness if it is seen as weak or as having capitulated to US pressure, especially as this comes after a number of serious political setbacks – not least the mass rejection of the Chinese regime in Hong Kong and Taiwan.''

Prospects for the next period

Many financial pundits argue that China's strategy in the trade war is to wait and see if the U.S. presidential election in November produces an incumbent who is less hostile to its interests.

This would be a huge mistake as recent votes in Congress reveal how the political establishment (both Democrat and Republican) share the same world view when it comes to China. Congress keeps voting unanimously for anti-China measures such as the Hong Kong Human Rights Act.

Regardless of who wins the presidential reality show in November China cannot expect any change in the hostile stance of the American empire.

China's relations with America over the next period will be shaped above all else by developments in the global economy.

The weak economic growth experienced by the world economy since the 2008 economic depression has been fuelled by a gigantic increase in debt the likes of which have not been seen before in human history. According to the Institute of International Finance global debt grew to "mind-boggling" levels from $173 trillion in 2008 to $253trillion by 2019. Global debt to GDP hit an all time high of over 322% in 2019. Global debt it set to continue growing rapidly in 2020 largely driven by China and the United States.

Yet this has not been matched by a corresponding growth of the real economy in goods and services.

Central banks across the globe, including China's, have taken a series of crisis measures in a desperate attempt to stave off the next economic depression. These measures range from the 67 interest rate cuts carried out by 46central banks to the huge stimulus measures i.e. money printing on a scale that was last seen during the depths of the 2008-9 financial crisis. The U.S. Federal Reserve, the ECB and the People's Bank of China have all been forced to print digital cash in huge quantities – yet it's not working.

Numerous metrics indicate that there is a 'synchronized global economic slowdown' due to the limits to debt-fuelled growth. The Institute of International Finance estimates that, "Over 60% of the world's countries expected to see below-potential growth in 2020,…'' Global manufacturing activity is hovering barely above the recession at 50.1. The Baltic Dry Index (which monitors bulk commodities shipping) is a closely watched indicator of future trading activity has fallen 50% during 2019. Meanwhile, the DHL Global Trade Barometer indicates that a global economy in serious trouble. According to the Brookings Institute:

"The indexes for China and the U.S., the two main drivers of global growth, are below 50 and have been falling. The indexes for other major advanced economies have also declined, reflecting the broad-based nature of the slowdown in trade as well as GDP growth. The low and declining index for Germany, the main driver of growth in Europe, points to an economy that is flirting with recession, as it has experienced virtually zero growth in recent quarters.''

The dizzying new heights reached by financial markets, particularly in the U.S., are reminiscent of the roaring twenties boom that ended in the disastrous Wall Street Crash of October 1929.

The economic upswing since 2009 is very long in the tooth. If the global economy recedes into recession during 2020-2021 then China will be placed in a very difficult position as markets for its export industries start to dry up.

The uprisings currently taking place across the globe before a recession may well spread to mainland China once an economic downturn starts and living standards start to fall and people feel the pain.

In such a situation the Beijing government will have very limited room for making any further trade concessions to its American enemy. Yet the American empire will be even more hostile in such an economic environment. It will use its vast military machine and the its control of trade, through the U.S. dollar, as cudgels to try and pressure China into making more fundamental concessions.

The Chinese nation will face a choice: draw upon its rich heritage of revolutionary anti-imperialist action to resist the U.S. empire or capitulate to its enemy.

Long term, the current strategy pursued by Beijing of peaceful coexistence with U.S. imperialism will not work. History is full of examples where declining empires fight to maintain their hegemony.

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