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The Impact of High-Tech Industries on China-US Business Negotiations

- Taking the Chip Industry as an Example

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Abstract: Since 2018, China and the US have held several rounds of high-level economic and trade consultations, which largely stopped in 2020. Subsequently, the US started a massive tax increase on China. However, faced with global inflation, the call was high to restart trade talks with China and eliminate tariffs on China. In June, US President Joe Biden said in a speech to the nation from Washington that the White House was reviewing the "penalties" imposed on China under former Donald Trump and "could opt to remove them altogether." However, the US has issued a series of containment policies in the chip industry, which further casts a shadow over the resumption of bilateral talks. The high-tech industry, with chips as the representative, has been playing an essential role in the China-US business negotiations. Compared to previous studies with more focus on the one-way research about how China-US gaming influences high-tech industries, this article attempts to analyze it from a new perspective: the China-US gaming in the chip industry. Through observational studies, the article intends to make an in-depth analysis of the significant role high-tech industries have played in the China-US business negotiations and explore where the crux lies. Through a series of observational studies, this article argues that America will not loosen controls on Chinese high-tech industries, especially on the chip industry. For the US and China - the world's first and second largest economies, the failure of business negotiations would mean no winners for either side.

Keywords: China-US business negotiations, chip industry, crux

1. Introduction

As China's status continues to rise in the global economy, the bilateral trade between China and the US has also soared. In 2020, the total trade volume between the two countries reached RMB 4.06 trillion, of which the exports to the US were RMB 3.13 trillion, growing by 8.4% and the imports from the US were RMB 931.87 billion, growing by 10.1%, making China the largest trading partner of the US then [1].

The overly close economic ties between the US and China, as well as the high US trade deficit with China, has raised great concerns from the then US President Donald Trump and has also set off a series of tariff-led trade wars between the two. In the war without smoke, business negotiations

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have become the battlefield. This follows a series of business negotiations between the US and China about the issue of tariffs and the signing of the China-US Phase-One Economic and Trade Agreement. However, for now, both sides do not think they have met their respective hopes. After Biden took office, there have been calls for renewed business talks.

Taking into account materials including official economic data, statements and opinions of government officials both in the past and present, this article attempts to analyze why it is necessary for China and the US - two countries with two different cultural backgrounds and thinking patterns, and with different negotiation objectives - to sit back down at the negotiation table, how the high-tech industry, represented by chips, becomes the largest bargaining chip, and what impacts different outcomes may bring about for both sides. In addition, this article tries to provide some suggestions for possible solutions to the China-US business negotiations.

2. Background Information: The Status Quo of China-US Relations

Both China and the US are in high demand for a resumption of business negotiations, with the focus on removing the high tariffs that America imposed on China in 2020. It comes against the backdrop of the current high inflation in the US, which failed to fall in June even under successive US dollar rate hikes, but rose by another 0.6% instead, with CPI as high as 9.1% [2]. Therefore, before the midterm congressional elections in the US in November, reducing the level of inflation will be a major objective for the Biden administration and also the biggest challenge facing the US economy. In this case, lifting the sanctions against China and allowing Chinese products to enter the US market in large volumes could stabilize the domestic economy in the US and curb inflation. Zhong Zhengsheng, the chief economist of Ping'an Securities in China, said in a speech that he had calculated that the US tariffs on China boosted the CPI by about 0.22% [3].

However, China and the US at present have not really started business negotiations about export tariffs. Moreover, the negotiations are bound to be difficult because the objectives of both sides do not coincide. The US hopes to get out of the inflation trap by resuming business negotiations with China.

According to the report by the US Bureau of Labor Statistics in August, although inflation eased slightly in July, the Consumer Price Index rose to 8.5%, compared to 9.1% in June. This was largely driven by higher costs of goods and services, such as cars, housing, food and health care [2].

High inflation has put severe financial pressure on many American families, who are forced to pay more for everyday necessities, including food and rent. More importantly, this heavy burden is largely shouldered by lower-income families, leaving their already stretched salaries greatly affected by price fluctuations.

The average American is spending an extra $717 a month because of the highest inflation in decades, according to an analysis. As said in the analysis, despite the slowdown of price increases from June to July, prices rose by 13.3% from January last year to July this year. Even if prices stop rising altogether, the inflation that occurred between August last year and July this year has added an additional $8,607 to household spending [4]. In addition, despite the drop in energy prices in July, Americans are paying a much higher share (32.9%) for gasoline than a year ago. Food prices have increased by 13.1% over the past year, the largest increase since 1979 [4].

The US has another objective for the China-US business negotiations, and that is, the US does not want the Chinese economy to overtake that of the US. On March 26, 2021, US President Joe Biden held his first press conference since entering the White House, which lasted about 62 minutes and included a total of 10 questions. On China-US relations, Biden said China would never be allowed to overtake the US as the world's top power during his tenure. He also claimed to invest more to ensure the US won in the competition with China.

However, China, the other side of this potential negotiation, hopes that the business talks could help lower the export tariffs so as to sell more goods to the US. As shown in an official statistic, in the first four months of 2022, the US foreign trade, both exports and imports included, totaled $1,746.6191 billion, a significant year-over-year increase of 21.4%. Moreover, Canada and Mexico became the first and second largest trading partners of the US. The bilateral trade volume totaled $258,5056 billion and $249,7835 billion, respectively. By comparison, the bilateral trade volume between the US and China in the first four months was only $241.1203 billion, with China falling to be the third largest trading partner [5].

It is evident that both China and the US have a huge demand for the resumption of business negotiations. In May 2022, Chinese Vice Premier Liu Hecen held a video call with US Treasury Secretary Janet Yellen. Both had a pragmatic and frank exchange of views on macroeconomics and the stability of supply chains in global industries. However, this widely-expected business negotiation has now taken a new twist with the visit of US House Speaker Nancy Pelosi to Taiwan, China.

3. The Status of High-tech Industries in Political Gaming

If lowering tariffs on China is one of the few options available to the Biden administration as it seeks to quell inflation, why hasn’t it been implemented since he took office? By contrast, his predecessor, Donald Trump, imposed tariffs on about $370 billion worth of imports from China. In fact, during the 2020 US presidential election, Biden attacked Trump’s trade policy towards China and made it a campaign priority. However, he did not scrap any Trump-era tariffs on China imports. The Biden administration’s hesitancy on this matter illustrates the sharp divisions within the US administration over the issue of lowering tariffs on China imports and the great significance of high-tech industries in the political gaming between the two countries.

In early July this year, The Wall Street Journal, citing people familiar with the situation, said that Biden had not made the final decision, but he might make the announcement that week to suspend tariffs on consumer goods such as clothing and school supplies, as well as simultaneously launching a broad framework to allow importers to apply for tariff waivers. However, the person also said that Biden was expected to raise tariffs on the high-tech items from China, thus maintaining the economic pressure on China.

The Wall Street Journal also reported previously that the US could open a new Section 301 investigation into China’s industrial subsidies for high-tech projects, for which the Office of the US Trade Representative (USTR) has been preparing for months. The move might also lead to tariffs on a series of high-tech products.

As Biden was weighing a tariff decision towards China, he was dogged by strong divisions from members within his administration and Congress, and also from different external forces such as businesses, Wall Street, and labor unions

The prospect of adjusting tariffs on China to curb inflation is a concern for some US officials. Treasury Secretary Janet Yellen has repeatedly said that tariffs were a clear drag on the American economy, and the government was looking at ways to re-configure tariffs to help curb inflation. In the interview with ABC News on June 19, Yellen said, “... re-configuring some of those tariffs, so they make more sense and reduce some unnecessary burdens is something that’s under consideration.” In early June, Commerce Secretary Gina M. Raimondo told CNN in an interview that the administration had decided to keep the tariffs on steel and aluminum to protect American workers and its steel industry, and it is a matter of national security, but there are other products, household goods, bicycles, and more, and it may make sense. Others, however, wish to maintain their strength against China by imposing tariffs. Tariffs are one of the means to restrict the development of the Chinese economy, especially that of the high-tech industries.

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Officials, represented by US Trade Representative Katherine Chi Tai and National Security Advisor Jake Sullivan, have stressed that existing tariff measures are a major bargaining chip in trade talks with Beijing. They argued that it would be self-defeating to remove tariffs first when China has failed to meet the commitments to purchase American goods as part of the 2020 Trade Deal with the Trump administration and has not made new gestures on specific issues [6]. About whether to remove tariffs on China, Katherine Tai said in a Senate Hearing on June 22 that tariffs on Chinese products are "a significant piece of leverage" in the US-China trade relationship and that removing tariffs might have a limited effect on controlling short-term domestic inflation.

Moreover, major labor unions, including the American Federation of Labor and Congress of Industrial Organizations (AFL–CIO), the United Steelworkers and the Service Employees International Union (SEIU), hold that ever since the Trump's administration's Section 301 investigation, nothing has changed in China's trade practices to warrant the removal of tariffs. If anything has changed, as they stress, it is the Chinese government that has "just doubled down on their strategy and methods." On August 10, 2022, Bloomberg quoted Commerce Secretary Raymond Raimondo as saying that the Biden administration hopes to "ensure nothing is done that might hurt American workers." It is clearly a challenge for the Biden administration to bring these different views together into one unified theme and to arrive at an answer that satisfies all parties.

4. The Impact of the Chip Industry on China-US Negotiations

In the game of high-tech industries between China and the US, chips have always been a part that cannot be ignored. As the world undergoes a comprehensive transformation towards information technology and digitalization, the rapid development of new industries such as 5G, artificial intelligence, the Internet of Things, and new energy vehicles has brought about a significant rise in demand for chips. Moreover, the "chip shortage" that stirred the world last year has also highlighted the vulnerability of the global chip supply chain under the impact of the epidemic and the imbalance between supply and demand.

The chip industry is of great importance to the China-US business negotiations firstly because of its pivotal position in bilateral trade. While China has to export many goods to the US, it is also the world's largest importer of chips. Moreover, in the first seven months of 2022, among goods imported into China, "only the volume of chips and petrol exceeded 1 trillion yuan". In these months, the cumulative number of imported chips was 324.67 billion, shrinking by 11.8% year on year; the amount paid was 1.58 trillion yuan, a 5% increase from 2021, accounting for around 15% of China's total import value of RMB10.23 trillion in the first seven months [7]. The US, on the other hand, is the largest exporter of chips around the globe. During the whole year of 2021, the sales of US chip companies totaled $258 billion, representing 46% of the global market, compared to 47% in the previous year [8].

Secondly, the importance of the chip industry also lies in its essential role in the China-US competition and its leverage for the US to curb China's rapid development. On August 9, Biden signed the "$280 billion" CHIPS and Science Act of 2022. The Act, the rarely-seen high subsidy bill for a single industry, aims to increase the manufacturing capacity and technology research and development capacity of the domestic chips through massive financial subsidies and tax breaks and finally attract semiconductor factories to stay in the US. According to the Semiconductor Industry Association (SIA), in 2020, the US accounted for 12% of the world's semiconductor production capacity, down 25% from 30 years ago [9]. However, the Act also seeks to further restrict the development and upgrade of China's chip industry, requiring "any company that receives US subsidies can manufacture chips and invest in America, but cannot in mainland China." Apart from the efforts to prevent China's chip industry from obtaining more external investment, the US has been expanding its export controls to China.

In addition to previous calls for allies to ban the sale of lithography machines to China, Bloomberg reported on July 30 that Lam Research and KLA Corp., two US chip equipment suppliers in the US, have confirmed that the restriction level on chip gear to China has been raised from 10 nanometers to 14 nanometers. On August 31, the chip-designing company Nvidia was requested by the US government to stop the export of A100 and H100 products to China, two latest flagship GPU computing chips. The US government may have done so because China and the US are the only two countries entering the first echelon around the world in artificial intelligence development [10].

Therefore, if the chip dispute is not resolved, it would be difficult to resume and effectively pursue the business negotiations between China and the US. The strict restrictions that the US and its allies have imposed on China's chip industry would make the negotiations even more difficult. China would certainly like to see all the various restrictions on its high-tech imports lifted, while the US is not expected to do so.

5. Suggestions on the Development of China-US Business Negotiations

Beneath the high demand for business negotiations between both sides, the bilateral trade between China and the US, important economic and trade partners of each other, has kept an extremely high volume despite constant frictions.From 2009 to 2021, the share of US imports from China remained between 18-22% of its total volume [11]. Customs data show that the total trade volume in the first seven months this year amounted to RMB 2.93 trillion, up 11.8% year-on-year [7]. Moreover, China is the largest potential market for US exports, and China has long been an important export market for the agricultural and machinery products of America.

However, the business negotiations on tariff reductions between the two countries are expected to be unsatisfactory, and it would be difficult to implement large-scale tariff reductions on Chinese goods.

Firstly, the US is concerned about the interdependent economic and trade relationship with China, arguing that over-dependence on China would threaten its own economic security. Therefore, the US tries every means to get rid of its dependence on China, to decouple itself from China, and to reconstruct the supply chain on a global scale, which represents the root cause of trade frictions between the two countries.

Secondly, it would be quite helpless if America were to lower tariffs on China on a large scale. With its inflation at a 40-year high, the US increased the tariffs on China, which further pushed up the CPI by 0.22%. Moreover, there was a clear positive correlation between the pressure to raise the prices of industrial products and the tariff increase in China. The tariff increase on China would directly affect companies with higher import costs, leading to a great increase in the PPI. By contrast, lower tariffs would help curb inflation and reduce the living cost of US consumers. The US government would never reduce its tariffs on China unless it is forced under public pressure. However, even then, the US will not lower its export restrictions on China in the high-tech sector, the chips included.

It can be assumed that the China-US business negotiations on tariffs succeeded and what benefits it would bring to both sides. For China, it would solve all the import/export problems it has been facing in recent years and also gives its long-stifled high-tech industry some room for development. For America, inflation, the top concern of its people, would be eased. According to a survey by the Pew Research Center, 70% of the American people say that inflation is the top problem facing America, a much higher percentage than the issues of health care affordability (55%) and violent crime (54%) [12].

However, what would be the downside of an unsuccessful China-US business negotiation on tariffs? It is actually a war with no winners. If the tariff negotiations are successful, imports from the US will be significantly increased, as promised by China. However, it has not been realized yet. And the restriction on China's imports of chips would worsen the relationship. On August 11, 2022, the US Department of Commerce's Bureau of Industry and Security (BIS) published in the Federal Register an interim final rule to impose extra export controls on China for four "emerging and foundational technologies", three of which are closely related to advanced chips. This move on the American side would further increase the distrust between the two sides in future business negotiations.

6. Conclusion

Firstly, as the world's first and second largest economies, the trade relationship between China and the US is of great importance not only for the economic development on both sides but for the development of the world economy as well. If the commercial negotiations on tariffs between the two countries go well, it would not only promote the economic growth of both but also add more prosperity and dynamism to the global economy. Otherwise, there would be no winners for either China or the US, with the negative impact on China much worse than that on the US.

Secondly, the US will make no concessions in the tariff negotiations, especially about export restrictions on high-tech products like chips. It would be an essential tool for the US to suppress China's rapid growth in economy and science, which will bring harm to the long-term development of the high-tech industries in China and also add negative impacts on the potential business negotiations between the two sides.

In addition, the US does not care whether the business negotiation with China succeeds or not, as it believes the US must be the final winner. At the signing of the CHIPS and Science Act 2022, President Biden declared that this Act would help the US "win the economic competition of the 21st century". It also signals that the confrontation between the two superpowers, the US and China, will be increasingly intense.

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