



China Watch | Politics

TENSIONS OVER TECHNOLOGY AT G20

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- **White House opens up a new front in the trade war, dashing hopes of de-escalation at weekend Xi-Trump meeting**
- **Administration takes three key moves to block development of China's high-technology industry**
- **Xi will fail to convince Trump China is opening up to foreigners**

Xi and Trump are meeting in Buenos Aires for the first time since the start of the trade war, and markets are optimistic that their dinner on Saturday could result in a de-escalation of the trade war. As we laid out in our 22 November [Global Political Drivers note](#), meetings between leaders at multi-lateral summits have eased geopolitical tensions in the past, but hopes for this meeting providing an off-ramp for the trade conflict should not be overstated. Points of fundamental dissonance between China and the US remain that cannot be solved over an Argentine steak.

The main question on investors' minds is whether Trump will put a halt on the hike from 10% to 25% on US\$200bn of Chinese exports, scheduled for January 2019. In the build-up to the summit, Trump has played his usual game of contradictory messaging in order to put pressure on Xi: on Monday he first said it was "highly unlikely" that he would acquiesce to Beijing's demand for a delay to the tariff increase but later he told the press a deal "could happen". Whilst his flip-flopping, combined with his insistence on the excellence of his relationship with Xi, makes it impossible to accurately predict the outcome in Argentina - it is feasible that there will be agreement to go on talking and that the US agrees to delay the hike as part of this, meanwhile bolstering a new front to block access to its technology.

Behind all the media bluster over the disastrous APEC summit and Trump's threats of ratcheting up the tariffs, significant developments in Washington confirm [our conviction](#) that the trade war has morphed into a broader economic confrontation which is set to be long and ugly. The administration is focusing attention on preventing China from accessing US' cutting edge technology sector through unilateral export restrictions. Last week, the Bureau of Industry and Security (BIS), an adjunct of the Department of Commerce, opened up a public comment process for a proposed rule that significantly expands the criteria for identifying dual-use technologies which may be deemed essential to US national security. The rule will go into effect once the comment process ends on 19 December and those portions of the Export Control Act (ECRA) that passed Congress in August are enacted.

ECRA does not strictly define the list of "emerging and foundational" technologies to be subject to government export controls and the BIS is now soliciting opinion from the public to define the parameters. Previous administrations have kept to the precept that only exports of sensitive military technology to China constitute a "national security risk". The current document

proposes widening this definition to include a wide array of emerging technologies, including AI, robotics and biotechnology.

The administration is capitalizing on grievances against IP theft to push through moves to block China from acquiring cutting-edge expertise. With anger over the economic cost of forced technology transfer running deep, the administration is presenting these steps as a corrective measure to historic theft. But this is, in fact, more of a forward-looking than retributive action, primarily aimed at blocking China's ambitions to become the leading global technology power.

Anxiety centres on the "Made in China 2025" initiative. Trump is seeking to cripple its aims through unilateral restrictions on key cutting-edge components the People's Republic needs to develop its advanced technology products. The measures echo taken in the summer to block exports of US components to ZTE. The restrictions have since been lifted, but the incident created an impetus in Beijing to reduce dependency on US tech. Xi, for whom modernizing the economy and military is a core concern, has taken a personal lead in driving up support for home-grown substitutes for imports from the US (particularly semi-conductors) while China also seeks alternative sources of supply. Meanwhile, the moves to "protect" American technology from China, the second biggest global importer of tech, have met opposition in Silicon Valley with criticism centring on how this will boost competitors in Taiwan, South Korea and Japan.

US Trade Representative Robert Lighthizer has been vocal in the past week in his accusations of IP theft, following a USTR update to its March Section 301 Investigation. His latest report accuses China of failing to respond constructively to US demands for better protection of IP following talks in May and June as well as singling out Chinese "unreasonable actions in recent months" in cyberattacks on the US and its allies.

Washington will take comfort from moves by the EU to apply greater scrutiny to foreign investment as evidence that the global community is getting behind its agenda of targeting unfair Chinese business practices. The EU is proposing to increase FDI-screening capacity and introduce a new rule for the Commission to review any investment to which one-third of member states object. The initiative still leaves to final decision up to each country, and some member nations will continue to embrace Chinese FDI through the Belt-and-Road initiative, while Greece and Hungary having demonstrated their ties to Beijing by blocking EU moves to condemn PRC actions in the South China Sea.

The EU legislation, on the surface at least, fits with the Trump administration's strategy of soliciting support from allies in targeting China's technological ambitions. In an unprecedented move, the US has initiated an outreach campaign to get foreign allies to stop using Huawei telecommunications equipment; US officials have been briefing government counterparts and telecoms executives in friendly nations about the dangers of employing the Chinese telecom firm's 5G network connectivity.

Xi will tell Trump at their meeting that China is addressing key areas of US grievances. As evidence of this he will point to recent examples of China opening up to foreign business investment and allowing them sole ownership of projects, along with legislative changes to give more power to the Supreme Court in IP cases. These arguments will not convince the sceptics who complain that China often promises reforms, only to renege on them later. The two sides are set to continue the conflict. As with the escalating tariffs, the tactic of denying China access to technology is unlikely to elicit concessions which the administration would regard as satisfactory.

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