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PROPOSITIONS ON
SINO-AMERICAN TRADE DISPUTE
SOME HELPFUL IDEAS FROM SOCIAL SCIENCE

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Abstract

This short essay introduces some concepts and propositions from social science research that I personally find helpful in understanding the ongoing Sino-American trade dispute. Naturally, they are not meant to suggest a comprehensive or exhaustive list of factors that inform this topic. Given the purpose and the limits of my essay, I also do not engage any specific theory or method, such as the efficient-market hypothesis or game theory pioneered by well-known Nobel laureates (e.g., Burton Malkiel and Eugene Fama[1]; Thomas Schelling[2]).

Keywords: international signalling, self-selection, two-level games, issue linkages, factor endowments

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[1] Burton Malkiel and Eugene F. Fama. "Efficient Capital Markets: A Review of Theory and Empirical Works." *Journal of Finance* 25 no.2 (1970): 383-417.

[2] Thomas C. Schelling. "The Strategy of Conflict: Prospectus for a Reorientation of Game Theory." *Journal of Conflict Resolution* 2 no.3 (1958): 203-264.

Introduction

China and the United States, the world's two largest economies, have been involved in a trade dispute. How can social sciences help us to understand this dispute better? This essay does not try to predict how the dispute will eventually be settled or how long it will take to reach a settlement. It also does not attempt to give a blow-by-blow account of the bilateral negotiation, or a score card of its likely outcome as if judging a boxing match. Rather, it presents some basic ideas and propositions to orient our thinking about the ongoing process.

Signalling Resolve

When a trade dispute has escalated to the point of reciprocal rounds of escalating tariffs, it has obviously reached a very serious point. The mutual imposition of retaliatory tariffs is a deliberate and public act of self-denial because the costs will reduce the choices available to one's own consumers and more importantly, reduce their purchasing power – tantamount to an additional tax on one's own citizens. This self-infliction of pain, however, is obviously undertaken with the intention to cause even greater pain on the other party – hence, a game of relative loss. In contrast to international cooperation which is said to produce a win-win situation for both parties, we are here presented with a reverse situation whereby the public posture of each disputant is to indicate that it is willing to accept losses in the belief that a disruption or deterioration of trade will cause the other side even greater losses. Moreover, by imposing tariffs on the other side's goods, each party is declaring by its action that it believes that it can tolerate and endure this pain (in terms of both the economic and political costs resulting from these tariffs) more than the other side.

There are two signals being sent in this situation. First, by taking tangible actions that are costly to itself (imposition of tariffs) a state is backing its words with deeds, thus lending credibility to its declared resolve to get its way as expounded by James Fearon's well-known rationalist explanation of war.[3] The intended message is that by taking on the self-inflicted pain, one is serious and not bluffing. The heavier the self-imposed costs, the more believable is one's threat to disrupt trade and one's willingness to endure this disruption ("one is walking the walk, and not just talking the talk"). Second, the tariffs being imposed represent a public wager professing that one has a higher threshold for accepting the pain resulting from the lost trade than the other side.

This remark in turn has a strong implication. It calls attention to a state's own willingness or ability to endure privation as opposed to its ability to inflict pain on the other side. Most studies of economic and military struggles tend to focus on the latter rather than the former consideration.

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[3] James D. Fearon. "Rationalist Explanations for War." *International Organization* 49 no.3 (1995): 379-414.

Accordingly, they tend to stress the balance of power between the pertinent parties rather than their balance of interest or resolve so that, for example, their analyses cannot explain the outcome of asymmetric conflicts such as the Vietnam War. Although the US inflicted far heavier casualties and destruction on North Vietnam, it had a much lower tolerance for the lighter costs imposed by North Vietnam on it.

Importantly, we do not know whether the tariffs being imposed are really intended to satisfy the demands that the respective disputants have stated publicly – or whether the tariffs are meant to advance some other hidden goals. For instance, from Beijing's perspective, are the US demands intended to correct the bilateral trade imbalance and provide protection for US intellectual properties? Or are they part of an undeclared agenda to block China's rise, such as to thwart the Made in China 2025 strategy or to frustrate China's push to lead the next technology frontier (e.g., 5G, Internet of Things, artificial intelligence)? It is possible that a state chooses to escalate a trade dispute because it believes that it has a stronger bargaining position in this issue area and that it is using it to advance some other goal unrelated to trade. Therefore, what is at stake in the trade dispute can be something "bigger" than the bilateral trade relationship itself. The goalposts for ostensible trade settlement are subject to change and may very well involve undeclared and non-trade objectives. Given the so-called commitment problem, either side may demand negotiations be re-opened again in the future (to press for further gains or to preserve gains already made). As Fearon has explained, an inability by both sides to commit to live with the terms of a settlement in the future makes a current agreement more difficult to reach. Moreover, whatever agreement that is reached this time, it is a good bet that the parties will re-litigate the same issues again in the future. That is, we are likely to see recurrences of similar trade tensions. This being the case, signalling resolve and standing one's ground is important for prevailing not just in the current round of struggle but for future rounds as well because one's reputation carries over time.

Finally, it is important to note what the current situation has *not* yet fully come to. It does not indicate that the bilateral relations have reached the breaking point – for if it *were* the case, a government would be restricting its country's own exports to the target country rather than limiting imports from that country because the former action would be an even more compelling signal of one's resolve. Restricting one's own exports would be a more credible signal of resolve because it communicates to an even greater extent one's self-denial of economic benefits for a political purpose (after all, limiting imports from another country can be motivated by a desire to promote one's own industries whereas restricting one's own experts cannot be construed in the same way). The US embargo of oil and other strategic materials to Japan before Pearl Harbor comes to mind as an example. That said, the Trump administration's latest actions (as of 9 October) to ban US trade with six Chinese companies for alleged mistreatment of Uighurs point to an escalation in limiting exports (in addition to its earlier decision to ban US companies from selling to Huawei, a leading Chinese technology company). Press reports that the White House is considering banning Chinese companies from being listed on US stock markets suggest another possible pending escalation – one that reinforces the

remarks above about moving goalposts and about Beijing's suspicions that Washington's real objectives extend beyond trade.

Self-Selection

This is just a fancy term for describing decisions by states to become involved in a dispute of some kind. When faced with a threat of tariff, economic sanction, or military intervention, most states will decide to settle peacefully especially when they face a much stronger opponent such as the US. That is, when faced with a very serious disadvantage in relative power, most states will make the necessary concessions to avoid the threat of tariff, economic sanction, or military intervention from being carried out by the stronger party. This being the case, just the threat of these actions will be enough to resolve the dispute on the stronger side's terms – and the actual implementation of tariff, sanction, or intervention will be unnecessary from the point of view of the party making these threats. There will be non-events because history will not record any hostile encounter between these parties. The reverse situation, however, is equally important. History has shown that when the US has applied sanctions against Iran and North Korea over their nuclear programmes, imposed tariffs on Chinese or European goods, or intervened militarily against Iraq and Cuba, Washington's threats have not worked. They are "hard cases" whereby Washington's threats to undertake inimical actions were *not* enough to coerce its counterparts to concede to its demands. Self-selection refers to the decision by these counterparts' officials to resist Washington's demands – that is, to consciously accept or "select" themselves into a confrontation with the US. When evidently weaker states accept a confrontation with a stronger US, the obvious inference is that these countries must care intensely about their cause and they must be highly resolved to resist US pressure (because those that are less committed or resolved would have already conceded to US demands, thereby making it unnecessary for Washington to carry out its threats and consequently history would not have recorded these actions being undertaken).

Because only highly committed and resolved states will confront the US, Washington will have more difficulty in having its way with these more "recalcitrant" countries (such as in the example of the Vietnam War cited earlier). When a trade dispute has escalated from just a threat to impose tariffs to actual and even repeated rounds of tariffs, the selection logic tells us that we are witnessing an especially intractable dispute, and we should not expect an easy or quick resolution. Those cases that can be settled easily and quickly would have already come to pass (as non-events) long before this point is reached. Significantly, the selection logic being presented here suggests that when a lopsided contest does take place – such as in the Korean and Vietnam War, in US invasions of Iraq and Afghanistan, and in US sanctions against Iran and North Korea – the weaker side must believe that it has some advantage such as a greater dedication to its cause and a greater willingness to suffer privation, so that the eventual outcome of such contests cannot be simply inferred from the balance of tangible power between the contestants. This phenomenon in turn means that those "normal" variables expected to predict successful economic sanction or political/military coercion (such as the balance of power between the two sides) would have their regression signs reversed in these "hard cases" in which

the weaker side has decided to engage a stronger side in a confrontation. The weaker side's leaders must have discounted publicly known variables that are supposed to influence the outcome of these encounters; they must have concluded that these commonly accepted factors are offset by information only known to them "privately".[4] The relevant leaders' private information may reflect the extent of their commitment or dedication to their cause, their ability and willingness to suffer privation, and their evaluation of the strength of their own domestic political position and that of their domestic opposition.

Win Sets and Two-Level Games

Naturally, if a dispute is to be settled its terms must fall within the range of what is acceptable to both parties – or what Robert Putnam has called the opposing chief negotiators' "win sets."[5] Putnam also quotes former US Labor Secretary John Dunlop saying that any foreign deal requires three agreements – one across the table and one on each side of the table. That is, any foreign deal will have to be acceptable to each party's domestic stakeholders. Whether they come from democratic or authoritarian states, these chief negotiators face domestic constraints in their negotiation space. The settlement negotiated by these executive officials will have to be "ratified" by their domestic constituents even if it does not require formal legislative approval and even if it only entails passive acquiescence by important stakeholders. Significantly, strong leaders are more likely to be "pushed around" to make concessions to their foreign counterparts because they have a larger "win set" or more discretion about the terms of an eventual settlement. They are less likely to be constrained by domestic opposition, and there is less danger of their negotiated deal being rejected by their domestic constituents. Their personal approval or authorisation is usually enough to ratify a foreign deal. Thus, think of Mao Zedong reaching an accord with Richard Nixon or Kim Jong-un prospectively with Donald Trump. Conversely, weak leaders are more vulnerable to domestic criticisms and rejection by veto groups, and the deals they reach with foreigners can be overturned by their successors (such as in the case of the Iran nuclear deal negotiated by Barack Obama and subsequently renounced by Donald Trump). They have less domestic political "wriggle room," and they are therefore more able to threaten credibly that unless they can obtain more favourable terms from their foreign counterparts, they will be unable to gain domestic approval for a deal. Thus, for example, Barack Obama faced a very skeptical Congress in trying to reach the nuclear deal with Iran and he had to instead resort to executive action to reach a multilateral deal to freeze Iran's nuclear programme in exchange for lifting economic embargo aimed at that country. Nevertheless, this deal was still undone by his successor, Donald Trump, who decided to withdraw the US from this agreement.

According to the reasoning being presented here, a Trump presidency beset by personal, legal, and political problems will tend to work to the advantage of US negotiators – assuming that the Chinese

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[4] James D. Fearon. "Selection Effects and Deterrence." *International Interactions* 28 no. 1 (2002): 5-29.

[5] Robert D. Putnam. "Diplomacy and Domestic Politics: The Logic of Two-Level Games." *International Organization* 42 no.3 (1988): 427-460.

negotiators have a large enough "win set" to allow them to make the necessary concessions in view of their own domestic agenda and situation (a big assumption). Weakened by the investigation conducted by Special Counsel Robert Mueller and engulfed in a constant partisan struggle with Democrats who control the House of Representatives, the president would more desperately want a "win" in his trade dispute with China, and he can use his domestic political vulnerability as a bargaining lever to demand more Chinese concessions or to otherwise threaten Beijing with a breakdown of negotiations. From this perspective, US negotiators would also want to see a strong Xi Jinping who has successfully consolidated his position as China's paramount leader and has the authority and power to overrule potential objection from powerful interest groups inside China to accept a deal that he has negotiated with Trump. Naturally, recent events in Hong Kong are more likely to challenge rather than bolster Xi's domestic position and reputation, thus shrinking his "win set."

Parenthetically, this line of reasoning would also imply that it would have been better if Beijing had concluded a deal with Washington before the US midterm elections held in November 2018. These elections brought about the Democrats' control of the House of Representatives, thus creating more political constraints on the Trump administration (especially considering that the Democratic Party has traditionally been more in favour of trade protectionism). By the same reasoning, Trump's "win set" could have further shrunk in the aftermath of the partial US government shutdown, and the widely-held perception that he had "caved" in re-opening government operations without obtaining any reciprocal concession for funding the building of a border wall and that he had failed to reach a deal with Kim Jong-un in Hanoi to end North Korea's nuclear programme. From Beijing's perspective, strategic timing also becomes an issue. Should it wait to conclude a deal with a possible one-term US president or his possible Democratic successor who can be even more demanding on Chinese trade concessions?

The preceding remarks gain increased relevance in view of the impeachment inquiry launched recently by the US House of Representatives against President Trump. As these words are being written, Washington is being consumed by intense, acrimonious partisanship over this proceeding. Moreover, the campaign season for the 2020 US presidential election has also started in earnest. One implication of these political developments is that any trade deal reached by Trump with the Chinese is likely to be criticised by the Democrats for being unsatisfactory for any number of reasons. Trump's anticipation of these criticisms can in turn cause him to demand increasing Chinese concessions, thus possibly making a deal even more difficult to reach considering Xi's own "win set."

Issue Linkages

As already indicated, trade negotiations are not a tug of war that will necessarily bring victory to the supposed stronger side – in this case, presumably the US which buys more imports from China than vice versa. For a deal to be reached and more importantly, for it to endure, it must make both sides better off than they would otherwise have been.[6] Issue linkage helps such a win-win solution to be found. The larger the number of issues that impinge on the relations of two states, the greater the possibility for them to come up with ideas for side-payments and log-rolling arrangements. For this reason, Taipei should be concerned because its interests could become collateral damage in settling Sino-American trade disagreements. The same reasoning also suggests that states have the option of "jumping" issue arenas so that, for example, Beijing can retaliate against US trade sanctions by easing its embargo on North Korea and Washington can similarly respond by selling weapons to Taiwan. Even within the broad area of trade, there can be various reciprocal compensations or denials such as those relating to restrictions on foreign corporate ownership, access to sensitive technologies or sectors (such as banking), and differential treatment of third parties (such as Chinese policies toward automobiles and auto parts manufactured by Germany, Japan, and South Korea). There are moreover other related concerns such as currency exchange rates (as evidenced by the recent decline of value in China's renminbi relative to the greenback) and China's purchase of US debt instruments that can be part of any explicit or implicit "horse trading." Therefore, it is necessarily difficult to tally up a net summary of "wins" and "losses" whatever the deal that is eventually concluded and whatever trade negotiators are willing to say publicly. Significantly and as implied earlier, what are quantifiable and specified in an eventual trade deal may not reflect the most important concerns motivating the disputing sides. Moreover, we are dealing with a moving target. That is, the settlement of the current round of disputes will influence the parties' relative bargaining power and resolve in future rounds. Thus, there is path dependency and serial interaction with multiple rounds of encounters. This being the case, the negotiating parties' respective time horizon matters. Delayed gratification and long-term strategic planning are easier to contemplate when electoral cycles and term limits are less likely to intervene.

As suggested above, there can be collateral "winners" and "losers." Any disruption or displacement of US trade with China can hurt countries that are currently part of the production chains connecting their trade, or alternatively, help others that stand to gain as a substitute export platform in lieu of China. Moreover, given the possibility of issue linkages, the relevant costs and benefits need not be limited to trade, currency, or investment, but can extend to the political and military realms and cause regional realignments in these areas.

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[6] R. Harrison Wagner. "Political Influence, Bargaining Power, and Economic Interdependence," *International Organization* 42 no.3 (1988): 461-483.

Factor Endowments

Tip O'Neill, the veteran Massachusetts politician, is quoted to have said "all politics are local." Naturally, trade negotiations can have the effect of redistributing economic and political costs and benefits. Although it is difficult to tally up wins and losses from the published details of a trade deal, this remark should not be construed to mean that we cannot say anything meaningful about prospective winners and losers in terms of sectors, regions, or groups if trade disagreements are settled – or if there is a deadlock that perpetuates trade tension (after all, some domestic interests will benefit from trade tension and protectionism). The basic truth presented by the Heckscher and Ohlin trade theorem (for which Ohlin received the Nobel prize, which was not given posthumously to Heckscher who had died earlier) remains valid today as much as when this formulation was first presented (this theorem was subsequently expanded and elaborated by two other Nobel laureates, Wassily Leontief and Paul Samuelson): a country exports goods for which it has a comparative advantage. Accordingly, the US exports in areas that are capital and technology intensive, and China exports in areas that are labor intensive. This observation in turn means that a trade war is likely to hurt the interests of those US sectors, regions, and groups that have strong endowments in capital and technology, and those parts of China with a relatively cheap and skilled workforce. Geography also matters such that California will be hurt by reduced trade more than, say, Missouri because most imports from China and exports from the US are processed at California's ports. Two ironies immediately suggest themselves. First, the main support for Trump's "America First" policies, including his policies on immigration and trade protectionism, comes from white workers who hold blue-collar jobs and who do not have a college degree. This base for Trump's political support is in the so-called fly-over country – that is, in "Middle America" in contrast to the two coasts where large urban centers and liberal voters are concentrated.

Conversely, those Americans who favor de-escalation and a quick resolution of the trade dispute with China tend to be more educated professionals working for large corporations and especially the financial world of Wall Street – the citadel of large monopoly capital that is the proletariat's nemesis according to communist dogma. It does not take a professional expert on financial markets to notice that recently the US stock market has been volatile, and this volatility has been closely tied to optimism and pessimism reflecting rumors on the state of the US-China trade negotiation. The other irony is that China's coastal provinces are most dependent on exporting to the US, and this region also represents most prominently those groups favouring economic openness and conciliatory foreign policy. In other words, a trade war tends to hurt particularly this region and its interests and can thus have the self-defeating consequence of undermining those moderate groups who have the greatest vested interest in continuing a peaceful, stable relationship with the US. These are also groups who have invested heavily in US real estate and whose children are most likely to be getting an education at US colleges.

The general point being made here is that economic considerations of factor endowments obviously interact with political alignments of interest and identity. There is moreover a complicated relationship between people's economic interests and their social identities and political values, and

oftentimes, these identities and values tend to trump (no pun intended) economic interests – such as when those whose farming and ranching businesses are being hurt by reduced demand from China continue to support Trump for non-economic reasons.

Concentrated versus Diffused Interests

Import tariffs raise costs for a country's own consumers. When another country retaliates by imposing tariffs on one's exports, it hurts one's most competitive producers. In the case of the US, these exporters can be farmers who produce pork or soybeans, and companies like Boeing and Caterpillar. From Mancur Olson's well-known work (for which he also received a Nobel prize), we know that concentrated interests are much more likely to organise effectively for collective action than diffused interests.[7] This observation in turn suggests straightforwardly that the influence of producers tends to override the influence of consumers in policy processes regarding trade. We can perhaps hypothesise further that those who suffer relative deprivation are more likely to mobilise to protest politically than others who have benefited from a new policy.[8] Thus, those whose existing businesses are hurt by the newly-imposed tariffs are likely to complain more loudly than others who have profited from the shortages and dislocations caused by the same tariffs. The combined implications of these remarks point to more political activism and greater influences for those who have been hurt by the trade dispute than others who have benefited from its redistribution effects. Parenthetically, it seems that Beijing's retaliatory tariffs have been selected strategically to target those industries or regions that are most likely to affect Trump's political base, such as producers of soybean, pork, and automobiles (General Motors) in Midwestern states like Iowa, Wisconsin, and Michigan that were critical for his electoral victory in 2016.

How are the redistribution effects – positive or negative – likely to be felt across sectors, regions, or groups? Are Hollywood studios and Silicon Valley high-tech companies, or Texas ranchers, Florida citrus growers, and Iowa hog farmers likely to be the main casualties or beneficiaries of a trade war with China? Obviously, the current US administration under Trump draws its political support from some of those sectors, regions, and groups mentioned earlier much more than others. Losers and gainers from a trade war with China are likely to be especially concentrated in a few regions and sectors, whose general partisanship is not a mystery to those in charge of trade negotiation. Although California, New York, and Texas, for example, are populous states with many electoral votes, they may not figure as prominently as less populous states that represent "battleground" states such as Iowa, Wisconsin, Michigan, and Florida. Both Democratic and Republican presidential candidates tend to bypass the former states because their opponents are expected to win these states by a large margin. Thus, Democrats are unlikely to "waste" their time and funds in campaigning in Texas and similarly Republicans are likely to concede California and New York. Instead, both parties are likely to

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[7] Mancur Olson Jr. *The Logic of Collective Action: Public Goods and the Theory of Groups.* Cambridge, MA: Harvard University Press, 1971.

[8] R. Ted Gurr. *Why Men Rebel.* Princeton, NJ: Princeton University Press, 1970.

concentrate their competition in those states where they have a reasonable chance of winning and where winning will make an important difference in their ability to gain most votes in the electoral college. This logic means that the effects of Chinese trade retaliation are politically most impactful in these states. An important point to be emphasised in thinking about this political impact is its marginal rather than average effect. Given Trump's narrow margins of victory in the so-called swing states, the key point is not the average effect of lost trade on a typical voter but rather the critical difference this lost trade can make in the decisions of those voters who are naturally cross-pressured and who as "fence sitters" can be persuaded to switch their support from one candidate to another – or just to sit out an election. A lower voter turnout, such as when young voters and black voters failed to turn out to vote for Hillary Clinton as they did for Barack Obama, could be decisive in determining the outcome of an election.

The above discussion may be based on a naïve assumption. Although the logic just presented may suggest a strategy to hurt Trump's reelection chances by denying him some political support in critical swing states, this possibility does not necessarily mean that the advantage thus created for the opposing Democratic candidate will be to China's benefit – after all, this Democratic candidate can be equally or even more critical of China when it comes to trading with that country. Indeed, two of the Democratic Party's frontrunners for its presidential nomination, Bernie Sanders and Elizabeth Warren, appear to be closer to Trump in their protectionist and isolationist sentiments than their other counterparts in the Democratic Party, such as Joe Biden. By the way, as the above reference to General Motors suggests, strategic targeting can also point to deliberate promotion of "heavy hitters" who can be leveraged as one's "lobbyist" – if for nothing else but that their large economic stake in China can be jeopardised should there be a further deterioration in trade relations (as shown by concerns expressed with respect to the sale of Apple's iPhone in China). Naturally, as a company like General Motors faces more domestic challenges (it has just experienced a protracted labor strike), the Chinese market becomes more important.

Global Positioning

Unlike Russia, China is not economically isolated in the world. On the contrary, Beijing has pursued a deliberate strategy of deepening and widening its involvement in cross-border production chains and interlocking investment networks. Much of its exports to the rest of the world are products assembled in China from components and technologies imported from other countries, and they can even be products manufactured by companies owned by foreigners but located inside China. These features tend to differentiate Chinese manufactured exports from US manufactured exports which have a higher domestic content. This feature makes it more difficult for Washington to specifically target China for economic coercion compared to, say, Russia. This is because sanctions directed against Beijing will have more adverse ripple effects on other countries such as Taiwan, South Korea, Japan, and Australia – many of which are US strategic allies. Thus, even though the US holds a stronger hand because China needs access to the US market more than vice versa, Washington can be persuaded by

important third parties not to play as forcefully its strong hand as it might otherwise be inclined to because of the collateral damage such action can cause to significant others (although from all appearances, Trump is much less likely to be swayed by this consideration than his predecessors; he has directed his ire against long-time allies, including South Korea, Japan, and the European countries that have accumulated large surpluses in trading with the US). Note also that production chains involving many different partners in different countries cannot be easily built and quickly replaced, a consideration that in turn cautions against abrupt changes in trade relationships. Moreover, to the extent that Trump lashes out against practically all the close commercial partners and military allies of the US, including Canada and Mexico, for alleged unfair trade practices, his actions have the effect of reducing the collective pressure that could have otherwise been mobilised against China and indeed, these actions could have had the reverse effect of arousing all these countries' misgivings about future US intentions.

How easily and quickly can established trade relationships be replaced? The availability of alternative suppliers and markets is naturally a critical question. Given the huge size of the US market, it will be very difficult for Chinese producers to find anything close to a substitute for their exports. For specific commodities or products on the import side, China may be able to purchase soybean and grain from Argentina and Brazil or enter into collaboration with Volkswagen and Airbus. Similarly, although Vietnam and Taiwan can be recruited as alternative suppliers for some merchandise sold by Walmart and Target, this will not be a process that can be accomplished quickly. To the extent, however, that the construction of cross-border production chains involves long-term contracts and large initial sunk investments, they will require time to negotiate, implement, and develop. Thus, there is a certain "stickiness" in existing trade relationships that tends to discourage "forum shopping" even in the face of a serious trade dispute. If we extend our attention beyond trade to international finance, we encounter similar questions such as which country will step forward to replace any shortfall caused, for example, by reduced Chinese purchase of US treasury bills. Would Japan and Saudi Arabia (the latter country's relations with the US have deteriorated recently) suffice to meet Washington's voracious appetite for debt financing? This discussion introduces still another question: in today's multilateral world, would a Sino-American trade dispute work to the advantage of third countries, conferring upon them (e.g., Canada, Australia, Brazil, Japan, South Korea, and Germany) benefits and a competitive edge in the future that may be difficult to reverse. For example, if Boeing and General Motors were to lose their market share in China, would their losses be gains for Volkswagen and Airbus? Once new trade networks are established, it may be difficult to revive old ties because of the reasoning just presented (it is difficult and costly to switch existing relations). When assessed in a multilateral context, bilateral trade confrontations can hurt both sides to the benefit of other significant competitors.

At the same time and if what is being traded is highly substitutable, a Sino-American trade deal can also hurt third parties. Donald Trump seems to be especially interested in reversing the chronic deficit that the US has experienced in trading with China. If Beijing agrees to increase its imports of pork, grain, soybeans, and minerals from the US, this change will most likely come at the expense of

US allies like Australia, Brazil, Argentina, and Canada. Similarly, if Beijing promises to purchase more Boeing aircraft (setting aside the recent problems involving its 737 Max 8 model), this development will naturally hurt sales by Airbus. Given Washington's self-imposed restrictions on exporting certain sensitive technologies to China, there is also the question of how much more pork, grain, soybeans, and minerals China can import to redress the bilateral trade imbalance.

Political Sensitivity and Vulnerability

In their well-known work, Robert Keohane and Joseph Nye introduce the concepts of sensitivity and vulnerability with respect to how a country's interests can be affected by another country's action or inaction.[9] Everything else being equal, one would surmise that democratic governments are more sensitive to voters' sentiments than authoritarian governments whose officials are almost by definition more insulated from and invulnerable to public opinion. This remark suggests that democratic officials are more sensitive to a political backlash from voters and opposition parties if a trade dispute causes a severe economic downturn. This observation does not, however, mean that Beijing will necessarily have an upper hand in trade negotiations with Washington. As implied earlier, "getting tough on China" appears to be an issue that Democrats and Republicans, despite their many differences, can increasingly agree on. There is interestingly and ironically a convergence on trade protectionism and opposition to multilateral economic deals (e.g., the Transpacific Partnership, the North American Free Trade Agreement) from people on the left and right ends of the US political spectrum, such as among supporters of Donald Trump and Bernie Sanders. Moreover, objections to China's alleged trade malpractices have become more popular among US voters. This being the case, there can very well be an attempt by both Democratic and Republican candidates to outbid each other in showing how tough they can be on China over the trade dispute. According to this logic, it can even be politically costly for a US candidate to be perceived as weak in dealing with China. This possible domestic dynamic can cause a hardening of US negotiation position as suggested by Putnam's metaphor of two-level games, and this development can in turn strengthen hardliners in China's domestic political discourse.

Concluding Remarks

The intense co-dependency of the US and Chinese economics has been described by one analyst as super-fusion,[10] and the state of their trade negotiation has been widely and consistently mentioned in the media as one of the two most important influences affecting stock prices. The other influence is the

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[9] Robert O. Keohane and Joseph S. Nye. *Power and Interdependence: World Politics in Transition*. Boston: Little, Brown, 1977.

[10] Zachary Karabell. *How China and America Became One Economy and Why the World's Prosperity Depends on It*. New York: Simon & Schuster, 2010.

Federal Reserve's deliberations on future interest rates. As China has been the leading creditor to the US,[11] the evolution of their trade dispute will also have an impact on the US and world credit market.[12]

Because of their deep mutual suspicions, any prospective trade deal reached between the two will likely involve phased-in provisions. That is, the terms of a deal are likely to provide incremental adjustments over several years rather than a once-and-for-all settlement of bilateral disagreements. Clearly the latter sort of resolution will entail basic and sharp changes in both sides' practices and can thus cause sudden and massive adjustment costs. The point being made here, however, refers to the need for instituting incremental revisions because such an approach also reduces the problem of commitment – as such revisions can be more easily reversed, and the costs of the other side's defection can be more easily offset if one's concessions are made according to a multiyear installment plan. This appears to be the only feasible approach when there is a great deal of mistrust on both sides – and when the issues involved are too many and too complicated to be resolved all at once.

Another expectation – based on prospect theory (Kahneman and Tversky 1979, for this work Kahneman received the Nobel prize six years after Tversky had died) – suggests that it will be easier to reach a deal based on limiting China's future gains as opposed to reversing its past gains.[13] This theory argues that people are more risk-averse when in the domain of gains (seeking to protect the gains they have already made), and they are not nearly as disposed to take risks to further extend their gains. Conversely, people are more risk-acceptant in the domain of actual or prospective loss when they try to prevent or reverse their setback. As leaders of the country that has suffered relative decline (in trade as well as other areas), US officials would be more inclined to "gamble for recovery" according to this theory.

US public statements had indicated multiple areas of concern to Washington in its trade relations with Beijing. These concerns range from a persistent and widening deficit in these countries' bilateral trade, China's alleged theft of intellectual properties from US companies, its alleged practice of forcing foreign companies to transfer technology, to its strategic vision for Made in China 2025. Whether intended or not, the timing of US request to Canada to arrest and extradite the financial officer of Huawei, the biggest Chinese internet company, coincided with the arrival of a Chinese delegation for a scheduled meeting to negotiate trade with their US counterparts. Many in China perceived the arrest of Meng Wanzhou, the daughter of Huawei's founder, to be a thinly disguised effort by Washington to put political pressure on Beijing, and also as another sign that the current trade dispute had originated from Washington's desire to block China's rise as evidenced by its efforts to lobby other countries, especially Western developed countries, to ban the purchase of Huawei's equipment and technology

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[11] Steve Chan. "Money Talks: International Credit/Debt as Credible Commitment," *Journal of East Asian Affairs* 26 no.1 (2012): 77-103.

[12] Daniel Drezner. "Bad Debts: Assessing China's Financial Influence in Great Power Politics." *International Security* 34 no.2 (2009): 7-45.

[13] Daniel Kahneman, and Amos Tversky. "Prospect Theory: An Analysis of Decision under Risk." *Econometrica* 47 no.2 (1979): 263-292.

in the Sino-American global competition to establish leadership in the next round of information revolution based on 5G networks. Thus, as suggested earlier in this essay, many believe that the current Sino-American trade dispute will be difficult to resolve because it involves more than trade or investment, as it implicates important strategic and political matters that are inherently more intractable. Whereas China may readily agree to purchase more US soybeans or grain, and automobiles or aircraft, it is widely expected to resist US demands to alter fundamentally its strategic vision, plans, and organisation for its economic modernisation – a matter that is more sensitive to the Chinese government because it is perceived to impinge on China's sovereignty. Given the larger geostrategic and political context of the current Sino-American trade dispute, its evolution and resolution may therefore differ from the usual kind of commercial disagreements among countries for which there are much less such geostrategic and political "externalities."

U.S. news media report that some people in Washington want to see a "decoupling" of the Chinese and American economies. Redressing these countries' chronic trade imbalance is therefore not the only or even the top priority for them, and the current trade tension can serve to advance their "decoupling" goal. The demands of these US hardliners that Beijing must fundamentally reorient China's economy and revise its development plan present the most formidable obstacle to reaching a trade deal. In their view, a deal that does not require basic changes in China's economy and its economic policies is worse than the alternative of continuing current tensions without a deal. As suggested by these remarks, the present impasse reflects an asymmetry in bilateral demands – Beijing is not insisting basic changes in the US economy or Washington's policies as a condition for resolving their trade dispute.

Some people see Washington's attempts to limit or even ban Chinese internet or electronics companies like ZTE and Huawei as the opening salvos of a new cold war to contain China, and its unilateral imposition of tariffs on its trade partners (including China) to be a blatant violation of the World Trade Organization's rules. In their eyes, this behavior – in addition to Washington's demands made to countries such as Canada, Mexico, and South Korea to renegotiate their trade deals with the US and its decisions to withdraw from multilateral accords such as the Transpacific Partnership, the Paris climate agreement, the Iran nuclear deal, the Intermediate-Range Nuclear Forces Treaty, and the U.N. Human Rights Council – constitutes cumulating evidence that the US under the Trump administration is pulling back from the liberal economic order and international institutions of multilateralism that Washington had fostered since World War II.

Washington has lobbied other countries strongly to ban Chinese manufacturers of internet equipment such as ZTE and Huawei, arguing that these companies are subject to the control of Chinese government. Its lobbying efforts, however, have been met with mixed results. While some like Australia and Taiwan have agreed to ban Huawei's equipment on grounds of protecting their national security, others like Britain and Germany have responded with much more equivocation and skepticism even after the US has threatened to withhold sharing intelligence with those countries that defy its pressure.

Another recent sign points similarly to diminishing US influence in affecting other countries decisions and perhaps even deepening suspicions about Washington's hidden motivations when it comes to commercial or technological competition. This sign came from various countries' decisions to ground Boeing's 737 Max 8 aircraft after a second tragic crash involving this model in Ethiopia (following the first one in Indonesia). Many US allies – including the Europeans, Australians, and Canadians – banned this aircraft from their airspace even though the relevant US authorities had continued to insist on its airworthiness. The US Federal Aviation Administration has been widely criticised for its seeming disregard for passenger safety and its cozy relationship with the aircraft's manufacturer to advance its commercial interests.

This essay has introduced several propositions, derived from past social science research, to illuminate the ongoing Sino-American trade dispute. Some of the empirical tendencies mentioned are mutually reinforcing whereas others are cross-cutting and even contradictory. As these words are being written in early October 2019, we still cannot see how this trade dispute will be resolved eventually. In a sense, this is a good thing because it allows social scientists to see how helpful their ideas and suggestions can be in informing the future evolution of this dispute – and thus, also to potentially disclose how inadequate their understanding can be. As shown by this discussion, the best that can be offered is a sense of general orientation about trends and processes that are likely to unfold in the coming days. Readers can judge for themselves prospectively or retrospectively how helpful or unhelpful are or have been the ideas and suggestions offered in this essay.

About the Author

Steve Chan is College Professor of Distinction at the University of Colorado, Boulder, where he teaches political science. He was the recipient of the Karl W. Deutsch award given by the International Studies Association, the Distinguished Scholar award given by this Association's Foreign Policy Section, and the Marinus Smith award in recognition of his teaching at the University of Colorado. His research interests encompass theories of international relations (such as democratic peace, power transition) and political economy (such as defence economics, developmental states, economic sanctions) with a focus on East Asia. His publications include nineteen books and about one hundred and eighty articles and chapters. His most recent books are *Thucydides's Trap? Historical Interpretation, Logic of Inquiry, and the Future of Sino-American Relations* (University of Michigan Press, 2020); *Trust and Distrust in Sino-American Relations* (Cambria, 2017); *China's Troubled Waters? Maritime Disputes in Theoretical Perspective* (Cambridge University Press, 2016); *Enduring Rivalries in the Asia-Pacific* (Cambridge University Press, 2013); and *Looking for Balance: China, the United States, and Power Balancing in East Asia* (Stanford University Press, 2012).

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