Bush administration stokes trade tensions with China

John Chan
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The Bush administration took a drastic step last Friday toward provoking an open trade conflict with China by referring its disputes with Beijing to the World Trade Organisation (WTO).

The US trade representative Susan Schwab filed a formal complaint with the WTO, accusing Beijing of using "its basic tax laws and other tools to encourage exports and to discriminate against imports of a variety of American manufactured goods". She claimed that Chinese subsidies had "denied an opportunity [for US firms] to compete fairly in the United States and in third country markets".

This is the third time that the US has taken a case to the WTO since China joined the body in December 2001. However, unlike previous cases that targetted specific categories of Chinese goods, the latest US action alleges "illegal" subsidies across a wide spectrum of Chinese products, from steel and paper to information technology. Some 55 percent of Chinese exports to the US could be affected.

Beijing has 60 days to reach a negotiated settlement with Washington or the WTO will set up a panel to arbitrate the dispute. If it loses, China would have to remove the subsidies or face US trade penalties. The process of WTO consultation can, however, be lengthy. The US, EU and Canada filed a joint compliant last March against China's policy of restricting the import of foreign-made car parts, but a ruling has not been made.

In the wake of the 1997-98 Asian financial crisis, Beijing introduced a series of tax rebates to protect Chinese exporters from the impact of rapidly depreciating Asian currencies. These measures, along with China's fixed exchange rate with the US dollar, established in 1994, played a significant role in making China the world's major export processing centre.

The US trade deficit with China ballooned to a new record of $230 billion last year. In the face of growing pressure from Washington over this expanding deficit, Beijing has already been forced to cut some of its tax rebates.

Schwab's announcement came in response to intensifying demands from the new US Democratic Congressional leadership—backed by the trade union bureaucracy and sections of business—for a more confrontational approach to China on trade issues.

In a hearing before the Senate Banking Committee two days earlier, US Treasury Secretary Henry Paulson came under fire over his policy of conducting a "strategic economic dialogue" with Beijing as the means of encouraging it to adopt a more flexible exchange rate regime. The new committee chairman, Democratic Senator Christopher Dodd, told Paulson that protectionist sentiment at home was "livid" over China's failure to allow its currency to appreciate against the US dollar. The US Treasury is under so much criticism over the issue that Tim Adams, the official in charge of the department's Chinese affairs, resigned on February 2.

Both Democratic and Republican lawmakers have accused Beijing of deliberately keeping the yuan undervalued by as much as 40 percent in order to give Chinese goods a competitive advantage. Congress has threatened punitive protectionist legislation over Beijing's alleged "currency manipulation".

Leading Democrats responded to the US administration's latest action against China by pushing for further measures. Democratic chairman of the Senate Finance Committee, Max Baucus, declared: "The US government needs to stand up for American workers and companies when our trading partners are bending, or breaking, the rules." Sander Levin, the Democratic head of the Ways and Means trade panel in the House of Representatives, commented: "This case represents a step in the right direction, but it must be part of a much more aggressive program to take action against violation of

WTO obligations."

Sections of American business that face strong competition from China and internationally have also demanded tougher steps. Nancy Gravatt, spokeswoman for the Washington-based American Iron and Steel Institute, declared: "This filing [at the WTO], while significant, only touches the tip of the iceberg of the full range of subsidies being provided to steel and other manufacturing industries in China."

The Bush administration is walking a fine line. While the White House wants to defuse the discontent over rising trade deficits, it cannot afford to disrupt the operations of major American corporations that have large investments in China. Moreover, if the Chinese People's Bank is forced to sell off US bonds and other dollar-based assets to depress the value of the yuan, other Asian central banks may follow suit, leading to a collapse of the US dollar and a financial crisis in the US.

In a speech to Illinois-based bulldozer maker Caterpillar on January 30, Bush declared: "I understand trade with China is considered controversial... But I want to tell you something, if you're a Caterpillar worker, or a Caterpillar shareholder, what that has meant." Warning against protectionist measures, he noted that Caterpillar had strong sales in China, which had in turn created 5,000 jobs in the US.

It is not so much US corporations like Caterpillar that are under pressure from Chinese competition. The company is a transnational giant that operates in 23 of the world's 24 time zones and has seven large production facilities in China itself. Small and medium American manufacturing firms, which employ millions of workers, are the hardest hit by the impact of cheap Chinese goods.

Morgan Stanley chief economist Stephen Roach commented on the *Globalist* website on January 30 that trade sanctions on China would not resolve US economic problems. He noted firstly that the US current account deficit stood at 6.8 percent of GDP in the third quarter of the 2006, nearly double the 3.5 percent level of 1986. He also pointed out that the bilateral imbalance of -1.9 percent of GDP with China was more than 50 percent above the peak reached with Japan in the late 1980s.

Unlike the aggressive expansion of Japanese banks and corporations in 1980s, Roach explained, China's "competition" today involves American-based transnational corporations using low-cost Chinese labour to increase profitability at the expense of jobs and wages in the US. Protectionism would do little to stop this process. Higher tariffs on Chinese exports would simply force US companies to turn to other cheap labour countries.

Roach pointed out that only 20 percent of Chinese exports to the US were value-added in China, which is "more of an assembler than a manufacturer". In other words, "Chinese" goods are produced from components sourced from a network of other countries, to which trade measures against China would not apply. Services such as IT were also being outsourced from the US to China and India to take advantage of their cheap skilled labour.

Roach noted that these processes have produced an "extraordinary disparity between the capital and labour shares of US national incomes". The share of profit is now at a 50-year high of 12.4 percent, whereas labour's share is just 56.3 percent—back to the levels of the late 1960s. "Today, US companies, as seen through the lens of corporate profitability, are thriving as never before while the US workforce is increasingly isolated in its competitive squeeze," he wrote.

The American ruling elite has no progressive solution to the economic problems produced by its rising trade deficit with China. The political dilemmas in Washington are being produced by the steady long-term decline of American capitalism. On the one hand, the US heavily relies on China to offset its deteriorating economic position, while, on the other hand, it fears that China's continuing expansion is creating a major new rival.

Beijing has repeatedly urged Washington to lift restrictions on high-tech exports to China as a means of reducing the huge US trade deficit. But the Bush administration has turned down all such appeals, fearing that China will become a competitor in such items and that imported US technologies will bolster the military capacity of its "strategic competitor".

The Chinese government has made a low-key response to the US complaint to the WTO, declaring only that it was "a pity" that Washington had taken such action. Beijing is desperately seeking to avoid any trade conflict that would cut into economic growth, resulting in huge layoffs and broad social unrest. For the same reason, however, the Chinese leadership is very reluctant to abandon the industrial subsidies that have assisted its rapid economic expansion.