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The Investment War With China: US Investment in China

Part three of this series looks at American pressure on U.S. foreign direct investment in China

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[Part one](#) in this series pondered the merits of delisting Chinese stocks on American exchanges and limiting American capital flows into Chinese stocks. [Part two](#) of this series examined the three-pronged United States war against Chinese outward foreign direct investment.

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The massive footprint of American firms in China has long caused angst. Under U.S. President Donald Trump, the trade deficit has become another factor fueling displeasure with the aforementioned state of affairs. Worries about the security threats posed by high-technology goods imported

from China have added impetus to the push for the reshoring of American firms. The COVID-19 epidemic has put into stark relief the risk of relying on goods produced elsewhere. Washington's action to address the aforementioned anxieties has entailed three features. One is rhetoric against foreign direct investment (FDI) in China. Another is Trump's tariff war against China. And another ties to products, encompassing adverse steps such as restrictions on the import of "Chinese" goods and positive measures like efforts to support U.S.-based production.

U.S. rhetoric has ranged from the very direct to the indirect. Illustrating the former, Trump, via a tweet in late August 2019, commanded American companies to "[immediately start looking for an alternative](#)" and to produce more of their output in the United States. Later Trump specifically slammed General Motors for its extensive manufacturing activities in China. During a speech in mid-January, U.S. Secretary of State Mike Pompeo remarked, "I'm not here to demand that you get out of China," only to undercut this soon thereafter when [he stated](#):

“At the same time, we need to make sure that our companies don't do deals that strengthen a competitor's military or tighten the regime's grip of repression in parts of that country. We need to make sure American technology doesn't power a truly Orwellian surveillance state. We need to make sure American principles aren't sacrificed for prosperity.”

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The tariff facet came into play in June 2018 with Trump imposing 25 percent tariffs on \$50 billion of Chinese imports and entailed a subsequent broadening of the goods subject to tariff and increases in tariff rates from 10 to 25 percent, contingent on the specific goods involved. No one motive sparked the imposition of tariffs or has sustained them until now. Regardless, an intent to spur American companies to leave China and return to the United States plainly is part of the equation for Washington as evidenced by Trump's statement at a rally in May 2019 in Pennsylvania that "Anyone who doesn't want to pay the tariffs has a simple solution: build your product in America, bring your factories back."

American FDI in China further faces an uncertain environment because of the administration's efforts to restrict inflows of certain "Chinese" goods, control Chinese access to other U.S. products, and reshore the production of other items. As with tariffs, multiple dynamics are driving

U.S. policy, including a desire to hinder China's access to dual use goods, obstruct China's technological progress, and punish China for intellectual property (IP) theft.

A recent illustration of U.S. efforts to limit inflows of "Chinese" goods into the United States is a rule proposed by the U.S. Department of Commerce in December 2019 that would give it the right to "keep makers of technology products out of America's information and communication technology (ICT) supply chain if they are under the jurisdiction of 'foreign adversaries'... and pose an 'undue risk to critical infrastructure or the digital economy.'" More recently, Washington has turned its attention to medical goods and is contemplating using "Buy American" laws, more stringent product origin labeling regulations, and other tactics to encourage production in the United States. Aside from this, U.S. export controls on Chinese firms like Hikvision, IFLYTEK, and Huawei affect American firms in China by hampering sales, partnerships, and research and development (R&D). Regarding the first category, worries about reliable access to American tech reportedly have led Chinese companies to reduce the amount of American content in their products. Concerning the latter two, IBM, Google, and Microsoft conduct artificial intelligence work in China and U.S. controls on AI software exports appear likely to constrain such activities in China. More positively, the United States is considering *inter alia* loosening red tape, providing loans and tax breaks, and leveraging government procurement to spur more medical goods production in the United States.

Assessing the political benefits of the war on American FDI in China is no easy matter. For one, the public lacks access to possible classified information supporting claims about the security threat posed by Chinese goods. As for obstructing China's access to American goods and IP, there is some logic *if* one expects a high probability of conflict, restrictions would meaningfully degrade China's efforts to develop alternatives (which is not clear), and controls actually do not prove counterproductive and facilitate China's pursuit of alternatives (which it seems they are doing). It is clear the United States would gain some independence from China, albeit not necessarily supply security, by decreasing the presence of American companies or undercutting American supply chains there.

Nevertheless, boosting U.S. independence is a double-edged sword since it also means, in concept, reducing China's dependence on the United States. With respect to political costs, U.S. actions incontrovertibly irk Beijing. To date, though, it has not initiated any serious retaliation. Relatedly, Washington's policies have the potential to decouple its

allies and other countries from the United States since many countries do not share Washington's anxieties, dislike American tactics, and want to their firms to continue operating in China.

The economic benefits of the war on American FDI in China are not readily apparent. There is no evidence American firms will move to the U.S. en masse versus other destinations or that they will create lots of jobs if they return to the United States. Furthermore, while pressure can play a productive role, undercutting American businesses in China through the policies described above seems unlikely to enhance IP rights, level the playing field, or ensure American companies do not "slit their own throats" in pursuit of short-term gain. As above, it again must be asked if the administration's three-pronged attack will succeed in substantively disrupting China's advances. This is not *prima facie* obvious.

Turning to economic costs, those rejecting the administration strategy contend U.S. firms will lose money and the innovation that flows from it, access to the best talent, and drive firms away from the United States. The first point may be true, but one counterpoint is that such reasoning ignores future losses that will occur from U.S. firms building up a potent competitor. As for the second point, one interviewee told the *New York Times*, "You can't do science with walls around it." The case of China, however, seems to belie this, at least to a point.

In sum, there does seem to be some value in the assault against American FDI in China. Nevertheless, the precise political value is murky or, in the absence of certain conditions, low. The political costs, while real, do not appear great, but could be in certain circumstances. The economic gains from the attack remain to be shown. For their part, critics have not proven that U.S. economic and security interests would suffer dire harm as a result of Washington's moves against U.S. FDI in China. In the final analysis, this piece, like the other two in the series, demonstrates systematic and comprehensive analysis is essential and that slogans are no substitute for careful policymaking.

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