US-China Ties: Damage Controlled But Obstacles Ahead

By Pushan Dutt, INSEAD

Even before the top US diplomat headed to China this week, talk of a new Cold War was unhelpful. Still, Washington and Beijing have their work cut out steering their relationship back on course.

Antony Blinken, the United States Secretary of State, has finally visited China, four months after his trip was abruptly postponed over the discovery of a Chinese spy balloon in US airspace. Initial reactions have been positive, with Chinese President Xi Jinping himself declaring that the US and China had made progress in improving their acrimonious relationship.

But while any attempt at dialogue and cooperation is welcome, we should be realistic: Blinken’s trip was more about damage control and drawing up a roadmap for stabilising an increasingly shaky relationship. Setting up communication channels to reduce the risks of miscalculation and crises is a minimal but essential achievement. Both sides agreed to establish working groups, initiate more commercial flights, and foster more exchanges among students, academics and journalists. The Chinese, however, rejected military-to-military communication.
That was one sign that the fundamentals of the relationship have not changed. Deep differences persist on Taiwan’s future, tensions remain heightened in the South China Sea, tariffs remain in place, and severe restrictions imposed by the US on technology transfers and access to semiconductor chips and related technology continue.

**Cold War 2.0?**

So is this a new Cold War? The media, as well as many politicians, think tanks and pundits seem to think so. In the US, Republicans and Democrats remain polarised on all issues save the perceived threat China poses to US dominance. Worryingly, many Western business leaders - the strongest proponent of trade and investment ties - are contemplating or have even gone ahead with disinvestment (e.g. Apple, Samsung, Hasbro, Sequoia Capital and AstraZeneca) from China.

Undoubtedly, the current US-China relationship bears certain similarities to the one between the US and the Soviet Union. Two superpowers with starkly different ideologies and world views - on the importance of political and civil rights, and the degree of intervention in the economy, to name just two - are jockeying for dominance, and the rivalry is likely to play out over a long time. Even the balloon incident had a whiff of the Sputnik launch in 1957 that set off a race to space in the early days of the Cold War.

But a deeper examination reveals major differences between then and now. The Soviet Union was on a par militarily with the US but lagged in infrastructure, innovation and economic growth. China is the opposite. It trails the US in terms of global projection of force (11 aircraft carriers for the US vs. three for China), **defence spending** (US$877 billion vs. US$292 billion in 2022), and **nuclear warheads** (3,600 vs. 350) but boasts a bigger economy in terms of GDP at purchasing power parity. Until recently, before President Xi’s crackdown under the slogan of **common prosperity**, China also had a thriving tech sector with highly innovative firms.

While the country still has far to go in terms of matching the US in GDP per capita (see below), it has pulled ahead of the US in many next-generation industries such as solar panels, solar and wind power generation, electric vehicles and batteries. China leads in AI adoption and has caught up in the number of AI researchers and top-cited AI papers. In infrastructure, it has built a high-speed rail network nearly twice as long as all other high-speed rail networks in the world combined.
At the heart of the Cold War was an ideological contest between communism and capitalism, and a push by the US and the Soviet Union to export their ideology worldwide. In contrast, ideological competition on the economic front between US and China is weak, especially as both deploy different versions of capitalism. Even the modest ideological gap seems to be closing. The US recently embraced state-directed capitalism via the **CHIPS and Science Act**, which encourages semiconductor companies to manufacture in the US and not in China, and the **Inflation Reduction Act**, which provides billions in federal investment in clean energy.

Further, there are no proxy wars yet between the two sides. In stark contrast, during the Cold War, both the US and the Soviet Union participated in conflicts around the globe, ranging from Korea to Angola and from Afghanistan to Nicaragua. The very concept of decoupling reflects how coupled the US and China are in terms of the flow of goods, people, ideas and capital. Compare this with the few trade or investment ties as well as serious travel impediments between the US and the Soviet Union.

Finally, while China is taking a bigger role in the world economy, the US seems to be retreating. We could be one election away from an inward-looking, America-first agenda.
Developments to watch

Therefore, the Cold War analogy may not be helpful. In fact, calling the relationship a war could predispose parties towards confrontation instead of cooperation. We should not overlook the collaboration between the US and the Soviet Union even at the height of the first Cold War that achieved, among other things, the eradication of smallpox, the Helsinki Accords, the Nuclear Non-Proliferation Treaty and START treaties. Likewise, China and the US will have to cooperate on today’s burning issues (literally), including climate change, global pandemics and AI regulation.

Framing discord between the two superpowers in zero-sum terms could also manifest in demonising of the “other” and persecution of business executives, scientists and students. It could blur the boundaries between economic and political decisions, engendering geopolitical repercussions far beyond the two countries. Recall McCarthyism and the communist witch hunt in the US, and American support for the apartheid regime in South Africa as well as autocrats in Iran, Pakistan and Chile.

Both sides should seek to avoid a repeat of such mistakes. We have already seen attacks on Asians during the Covid-19 pandemic encouraged by former US President Donald Trump, tit-for-tat arrests of executives (e.g. Huawei CFO Meng Wanzhou and the two Michaels) and China’s support for the junta in Myanmar, mirrored to some extent by US tolerance of authoritarian populists.

Blinken’s two-day visit ended on a cautiously positive note and can help break the mutually destructive cycle of hostility and mistrust. Nevertheless, there are three things to watch closely: the territorial disputes over Taiwan and the South China Sea, China’s economic recovery, and the 2024 US election.

In the South China Sea, there are increasing incidents of hostile contact between the two sides and their allies. Examples include Chinese and US aircraft flying very close to each other, a near collision between a Chinese naval vessel and a Philippine coast guard, and Chinese warships circling the Japanese home islands in May. This raises the risks of conflict, making it even more critical that mechanisms are put in place to reduce the risks of miscalculation and contain crises.
On the economic front, China is contemplating expansionary monetary and fiscal policies amid flagging growth. Beijing’s worries about the property sector, the rise in youth unemployment and restrictions on technology transfers could lead them down either of two very different paths: focus on growth and prosperity while eschewing conflict, or war as a distraction from worsening economic prospects.

Finally, the start of the 2024 election season in the US will distract President Joe Biden as he pivots towards campaigning for a second term. I foresee both Republican and Democratic candidates becoming increasingly belligerent and competing with each other in talking tough against China. US domestic political pressures can ratchet up hostilities, triggered by cheap talk on the campaign trail.

Find article at
https://knowledge.insead.edu/economics-finance/us-china-ties-damage-controlled-obstacles-ahead

About the author(s)

Pushan Dutt is a Professor of Economics and the Shell Fellow of Economic Transformation at INSEAD. He teaches in the MBA programme and the INSEAD Leadership Programme for Senior Executives.