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'THE US-CHINA TRADE WAR: FALL OUT IN CHINA'

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The mood in the Chinese Communist Party (CCP) hierarchy is sombre.

The US-China trade war as it is called marks a substantive change in the US-China relationship. Mutual suspicion now taints what Beijing has for decades described as its most important relationship. The bipartisan support that Trump's new policy towards China enjoys points to strains in the relationship lasting for quite some time and, in any case, fundamentally altering it.

Throughout his election campaign Trump has consistently highlighted terrorism and China as two issues that he would attack. Even prior to Trump there was recognition in the US strategic establishment that China's rise does not portend well for the US, but US President George Bush got distracted by the war in Afghanistan and Obama was unable to fashion a strategy. Trump is the first US President after Nixon – i.e. after 30 years – to begin to reshape US strategy and policy towards China.

Chinese Party cadres assess that the trigger for the US initiating the Trade war was Chinese President Xi Jinping's decision to abolish fixed tenures for top Party positions and the ambitious goal posts enunciated by him at the 19th Party Congress in October 2017. These are the 'China Dream', target date for achieving which was set to coincide with the centenary of the founding of the CCP in 2021; 'Made in China-2025' designed to propel China into the ranks of the world's most advanced hi-tech nations; and the declared ambition to make China a "major world power with pioneering global influence" by 2049, the 100th year of the founding of the People's Republic of China (PRC). If at all warning was required that China intends to surpass US power, this was it!

The US was precise in its targeting to prevent China's rise and singled out 'Made in China-2025' as well as its adjunct agenda of 'Civil-Military Integration', seen as the militarising of technology. The US picked on China's rapidly rising Shenzhen-based telecommunications company ZTE in April 2018. US sanctions on ZTE, including the conditions imposed following a reprieve granted on the personal intervention of Chinese President Xi Jinping, have virtually destroyed it. Next was China's fastest expanding hi-tech telecommunications company Huawei. Like ZTE, this too has clear ongoing links to China's People's Liberation

Army (PLA). The US charged Meng Wanzhou, Chief Financial Officer of Huawei and daughter of Huawei's founder Ren Zhengfei, with illegally selling prohibited components to Iran in violation of US sanctions. The US has approached Canadian courts to extradite Meng Wanzhou, under detention in Canada since December 2018, to the US. Meanwhile, the US imposed sanctions against 6 Chinese technical entities of which four are headquartered in Hongkong. The latter move implies that Hongkong might no longer benefit from the more relaxed application of trade restrictions by the US Government. There are currently 68 Chinese companies on the banned list in the US. In addition, 144 Chinese companies linked to the Chinese military are also on the banned list.

The sanctions have hit China hard. The Chinese leadership was severely jolted by their impact on China's hi-tech sector, which had been claiming that they are world leaders and self-reliant. According to indications the leaderships of ZTE and Huawei were also surprised at the dependence of their companies on a few foreign companies -- primarily four US companies -- for vital hi-tech components crucial for their products. Huawei's Ren Zhengfei, a former PLA engineer, after initially asserting that Huawei will not be impacted recently admitted that Huawei will take a long time to develop key components, like laser imaging chips etc., required to stay in business.

With trade talks making no progress and purchase of US made hi-tech components and parts banned, Chinese companies are in dire financial trouble as their production capacities have been severely hit. Shares have fallen sharply. Huawei's mobile phone handsets which are their major consumer product, for example, have lost 48% market share severely impacting the company's revenues. After brave initial comments that Huawei can weather this temporary storm, Huawei founder and CEO Ren Zhengfei recently conceded that Huawei is in serious trouble. In addition, Trump is applying further pressure and urging countries and US allies not to purchase Huawei's 5G on grounds of national security. There is no indication yet that the US will ease pressure on China and the latest round of trade talks that began in Shanghai on July 30, ended with US President Trump tweeting another 10 per cent hike on tariffs.

These new tariffs are in addition to those already imposed by the US on \$250 billion in imports from China. Beijing, which retaliated with tariffs on \$110 billion in US products, has only about \$10 billion in US goods left to hit in response against the threatened US tariffs on \$300 billion in Chinese products. The latest new tariffs of 10% starting September 1 on an additional \$300 billion a year of Chinese imports sent a shock wave through Chinese tech stocks on August 2. In Hong Kong, Tencent slumped by 2.6% that day, while Meituan Dianping was down 3.6%. Struggling smartphone maker Xiaomi went down 1.7%. Similarly on Wall Street, shares of Alibaba and JD.com both fell more than 4%, while search giant Baidu finished down 2.2%.

China's initial reaction to US actions was to try and "buy off" Trump. After the US hit China with 25 percent tariffs on \$50 billion of exports in July and August 2018 and added 10 percent tariffs on another \$200 billion in September 2018 and, with Trump threatening later that year to boost that tariff to 25 percent, China began serious negotiations with US Trade Representative Lighthizer and other US officials. China simultaneously activated pro-China lobbies and individuals to propagate that China will not be affected but that the US has hurt

itself by this action. The CCP began drumming up nationalism and xenophobia. China's official media gradually shifted to portraying the US as unfair and a bully and asserting that China can withstand US pressure. The official Party mouthpiece People's Daily, for instance, published 13 commentaries in May and June accusing the US of hegemonistic behavior. An example of the effectiveness of China's campaign are the numerous articles in the US and international media detailing how American consumers and businesses will suffer because of the trade war, how it will impact adversely on international trade, and how China is dominant in global supply chains which will get disrupted. An example is the 'open letter' to the US President addressed by the US foreign affairs and China scholar community. Beijing played on these apprehensions adding that it is reviewing its policy on the export of rare earths. But the US has stayed firmly on course. The draft amendments it gave Chinese Vice Premier Liu He to carry back to Beijing in mid-May were not accepted by the CCP CC Politburo which felt it impacted on China's sovereignty. The meeting failed. Chinese Foreign Ministry spokeswoman Hua Chunying declared: "The Chinese side will not give in to any extreme pressure, intimidation or blackmail and we will never concede an inch on major issues of principle."

But the suspicion that is beginning to run deep in China and the US is exhibiting itself in other areas. US business travelers in China are being harassed and questioned. By late July companies issued advisories to US citizens to postpone avoidable trips to China. Canadians are specially being singled out for harassment and two, of whom one is a serving diplomat, have been arrested and sentenced to death. While this is connected to the detention of Huawei CFO Meng Wanzhou, the threat to them is serious. In the US there are increasing reports of Chinese students being questioned on arrival and often deported. The services of Chinese scientists and researchers including in the National Institutes of Health (NIH) have been terminated. The FBI has begun investigating espionage cases in all its field offices in 51 states of the US with each linking back to Beijing.

The US-China Trade War has come at an inopportune time for Xi Jinping. It coincides with the slowing down of China's economy and spreading discontent among students, workers and ex-PLA personnel. The instances of criticism of Xi Jinping's policies by prominent academics, members of the Party's top advisory body the Chinese People's Political Consultative Conference (CPPCC), 'princelings' and former senior officials, including at least two Commerce Ministers, have been increasing. Reports suggest some prominent academics approached veteran retired leaders to pressure Xi Jinping to amend his policies or quit. Academics who, at a meeting in Beijing, expressed the view that China should modify its policies and not antagonize the US were 'disciplined'. Party cadres have been critical of Xi Jinping's policies saying that he has "over-reached" himself. Others have questioned the hyper-nationalism that surrounded the first Belt and Road Initiative (BRI) Forum and advised lowering of rhetoric. That was visibly toned down at the second BRI Forum in Beijing this April. In private conversation many senior Chinese cadres confide the sentiment that "China is alone" and "everyone is against us". Other countries are also beginning to reassess China's economic might and realise that China is not invincible.

In the face of growing pressure the CCP CC has decided on a tough stance. Chinese President Xi Jinping has begun preparing the Party and people for difficult times ahead. Visiting Jiangxi in late June, he asked the assembled cadres to prepare for the "second Long

March". 500 journalists were tasked to write eulogies of the Long March. China's official media reflected this decision. A People's Daily commentary said it was "laughable" to say the Chinese economy was being adversely impacted by the US tariffs, adding that "These irrefutable facts are not negated by anyone raising a hubbub." The CCP's leading theoretical fortnightly journal Qiu Shi asserted "China will not be afraid of any threats or pressure the United States is making that may escalate economic and trade frictions. China has no choice, nor escape route, and will just have to fight it out till the end. No one, no force should underestimate and belittle the steel will of the Chinese people and its strength and tenacity to fight a war."

The trouble that erupted in Hongkong on June 9 and shows no signs of abating, is an additional serious complication for Xi Jinping. The protestors are becoming progressively more articulate and have escalated their demands to scrapping of the Extradition Bill and resignation of the Beijing-appointed Hongkong Chief Executive Carrie Lam. Beijing has chosen not to interfere yet, but that it will at a time of its choice is certain. Meanwhile, an interesting divergence in tenor of the officially owned Chinese news outlets is visible. It suggests differences within the top leadership and the factions in the CCP. This could be an indicator of the vulnerability of Xi Jinping's position.

Xi Jinping's personal background shows his unwavering commitment to the CCP and realising the ambition of his forbears to see China as a major global power. His instinct will be to resist pressure and push ahead with achieving the goals set at the 19th Party Congress. Whether this will mean China becoming more aggressive in its foreign policy with possible military encounters with neighbours like Taiwan, Vietnam, Japan and India is uncertain. China's recent posture indicates that its People's Liberation Army (PLA) is confident of deterring the US from intervening on behalf of its allies in the region. The annual informal meetings at Beidaihe over the next few days could yield clues whether Xi Jinping will come under fire from senior veterans who will also be attending the informal conclave.

(The author is a former Additional Secretary in the Cabinet Secretariat, Government of India and is President of the Centre for China Analysis and Strategy.)

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