OPPORTUNITIES TO ADDRESS GROWING U.S.-CHINA TRADE TENSIONS

by Spencer S. Griffith and Stephen Kho
Akin Gump Strauss Hauer & Feld LLP

The U.S. and China are now each other's second largest trading partners, and China is now the single largest holder of U.S. Treasury debt. And both countries have massive stimulus programs in place to fight the recession, and agree that U.S. consumers need to save more and China's consumers need to spend more.

But despite this growing interdependence, trade tensions continue to grow. In the U.S., workers and their political representatives fear job losses to imports from China. China in turn perceives a growing backlash against its trade with, and investment, in the United States. U.S. producers and investors in China likewise fear continued difficulties in their competitive relationship with China.

At the same time, there are opportunities ahead to try to address these mounting tensions. This article will examine the source of some of these tensions. It then will examine key opportunities to address some of these concerns.

Growing Trade Tensions

A number of factors explain the growing trade tensions between the U.S. and China.

First, the massive volume of trade between the two countries itself explains much of the trade tensions. Increased trade brings increased opportunities for tension and disagreement. This problem is exacerbated because the huge U.S. trade deficit with China – down slightly year-to-date this year from 2008, but still massive – creates further political tensions. China is seen as a significant threat to job growth in America, and the bilateral trade deficit serves as a symbol of that threat.

Second, investment tensions between the two countries continue in light of recent high-profile events in both countries. While the direct investment by both countries in each other is not large, several high-profile events have heightened tensions over perceived unfair treatment. For example, CNOOC's aborted attempt to purchase the U.S. energy company UNOCAL as a result of political backlash in the United States arising out of concerns over a purchase of U.S. energy assets by a Chinese company have raised fears in China that the U.S. market is not welcoming to Chinese investment, at least not in sensitive sectors such as energy. Similarly, a more recent incident, in which Coca-Cola's bid to acquire a Chinese juice producer was rejected by the Chinese competition authorities, has likewise raised concerns in the United States that U.S. investments in China might be subject to political considerations.

Third, the worldwide recession will further stress U.S.-China trade relations. The recession has significantly slowed the United States' economy. Trade tension and trade case filings historically have been counter-cyclical, and usually increase in tough economic times. In the current downturn, U.S. companies thus should be more likely to file new trade cases against Chinese exporters.

Tensions are further exacerbated by the massive economic stimulus packages that both the U.S. and China have deployed to combat the recession. The two stimulus packages include hundreds of billions of dollars to stimulate demand in these two economies. Any efforts to restrict foreign suppliers' access to stimulus funds – and resulting perceptions of discrimination against foreign suppliers – will further exacerbate trade tensions.

Finally, high-profile trade disputes often serve as a "flash point" that further heightens trade tensions. The current U.S. Section 421 case involving tires from China is such a case. The Obama Administration is deciding whether to impose trade restrictions on imports of tires from China, pursuant to a special China-specific safeguard provision that China agreed to when it joined the WTO. The case is controversial in both countries for a number of reasons. In the U.S., the case is the first real test of the Obama Administration's position on trade restrictions. The President's decision will also be viewed as a signal to other potential U.S. industries whether the Obama Administration will be more receptive to Section 421 filings in the future than was the Bush Administration. And in China, the case is sensitive because China is concerned that if the Obama Administration imposes a remedy here, then other U.S. petitioners will file new Section 421 cases against China. Also, the volume of trade is large, and the

Chinese tire industry is powerful within China. All of these factors increase the sensitivity and political symbolism of the upcoming decision. President Obama must issue his decision by September 17, and observers in both countries will be watching carefully. One compromise approach might be not to restrict imports but to provide job training and other adjustment assistance to the U.S. industry.

Approaches to Reduce Trade Tensions

Despite the growing trade tensions, there are a number of important opportunities to reduce trade tensions in the long run.

S&ED

While the recently concluded Strategic & Economic Dialogue (S&ED) between the US and China produced few concrete agreements, the talks did set out general principles for eventual further liberalization of trade. The talks produced agreement that both countries will continue to press for completion of the important WTO negotiations in 2010 that will further liberalize trading rules. Also, the U.S. stated it will continue to review China's request to be granted market economy status in U.S. dumping cases. Although it is not likely the U.S. will change its position in the near future, once eventually granted, market economy status will make it easier for Chinese exporters to win antidumping cases. The U.S. also stated that its foreign investment review process, under which acquisitions of U.S. companies by Chinese (and other foreign) investors are reviewed for national security implications, is fair and transparent and will continue to be applied in this manner. Although this does not indicate any shift in practice by the U.S., this statement may make the U.S. market somewhat more attractive to Chinese investors, who to date have been nervous of the political backlash against Chinese investment in the U.S.

For Chinese companies competing in China, the S&ED also has long-term implications. For example, the two countries agreed to continue to negotiate a bilateral investment treaty ("BIT"), under which U.S. investors in China would gain new protections against arbitrary treatment by Chinese authorities against U.S. investments (and vice versa). And China agreed to continue to review possible ways to streamline rules for foreign investment in China, which will further open up investment for U.S. companies and make Chinese companies more competitive in the world marketplace. Also, China called on the U.S. to liberalize its current restrictions on exports of high technology items to China. While it is doubtful the U.S. will liberalize these export controls in the near term, over the long run any eventual easing of those restrictions would increase exports to China.

JCCT Talks

Another opportunity for further liberalizing trade are the bilateral talks under the Joint Commission on Commerce and Trade ("JCCT"). The recent S&ED talks focused on more long-term issues, with a particular focus on issues that the two countries could collaboratively work on. The JCCT talks, however, are conceived to deal with more technical, often industry-specific trade issues, and to deal with those issues on a more immediate basis. As the primary forum for trade issues prior to 2006, the JCCT was relatively successful in addressing bilateral trade disputes. If successful, there is no doubt that the JCCT will go far in reducing trade tensions between the two countries. Many of the more technical industry-specific issues that were not addressed in the S&ED talks will be addressed in the upcoming JCCT discussions in late October.

There is a heightened expectation in the U.S. that the October JCCT talks will result in more concrete trade deliverables. Between 2003 and 2005, the JCCT resolved a myriad of disputes, and limited the number of trade brought to the WTO by both countries. It is difficult to predict specific matters that may be addressed or resolved in the upcoming JCCT, but these include possible resolution of WTO disputes between the two countries involving the export restraints case and the "famous brands" subsidies case. Moreover, further movement in the area of special property rights, especially the area of ITR enforcement, will be carefully watched. Resolution of long-standing concerns on express delivery, insurance market access, medical devices standards, and electronic payment services would be useful as well. It is important that the JCCT be seen as a success and continues to serve as a forum for resolving trade disputes between the two countries.

Government Procurement

Finally, another opportunity to potentially reduce trade tensions over the long run will be China's entry into the WTO Agreements on Government Procurement ("GPA"). One of the important trade irritants between the two countries is the denial of access to government procurement projects. Both countries have many such projects, as well as numerous providers able to participate in such projects. Further opening of these procurement markets through China's accession to the GPA will encourage more healthy competition and increase mutually beneficial trade between the two countries.

GPA membership will shield China from the numerous "buy national" laws adopted by countries to favor domestic goods and services and government procurement. China has now developed many of its companies to a level where they can compete on the merits of their world-class products and services. For these reasons, China should accelerate its efforts to join the GPA, which will further reduce trade tensions and provide mutual benefits to both countries.

In conclusion, while there are certainly reasons to think trade tensions will rise, there are also important opportunities to try to resolve them as well.

Spencer Griffith is the partner in charge of the Beijing office of Akin Gump Strauss Hauer & Feld LLP. Stephen Kho is senior counsel at the firm in Washington, D.C., and Beijing.

This article originally appeared on Caijing.com *and is reprinted with permission:*
http://www.caijing.com.cn/2009-09-08/110242721.html.

AKIN GUMP
STRAUSS HAUER & FELD LLP