BOFIT blog

China fails to meet its Phase One agreement commitments

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AUTHOR



Juuso Kaaresvirta
Senior Economist

China has had huge difficulties to come even close to fulfilling its import commitments, which were consider to be hard to meet even before the coronavirus crisis.

Tensions between China and the United States have once more been on the rise. The US has heavily criticised China about its handling of the coronavirus pandemic, cyber security violations, and has tightened the screws on Huawei. Trade has also come back into the discussion after the truce made during the winter, when the countries signed the Phase One trade agreement on 15 January and agreed to reduce some of the additional tariffs.

In the Phase One agreement, China committed to reforms such as improving protection of intellectual property rights and opening up markets for American companies. These reforms were nothing new, however, as China had largely decided or even started to implement those reforms long before the agreement. The most significant commitment China made was to increase imports from the US by a total USD 200 bn in 2020 and 2021 from the benchmark year of 2017. The agreement covers a wide range of goods, from agriculture and manufacturing to energy as well as services.

The reason trade has now returned to the spotlight is that China has had huge difficulties to come even close to fulfilling its import commitments, which were consider to be hard to meet even before the coronavirus crisis. The detailed goods trade data provided by the US Census Bureau show that in the first quarter of the year the US has actually exported much less to China than in benchmark year 2017. Therefore none of the extra USD 200 bn in the agreement was exported. This applies to all of the broad categories: agriculture, manufactured and energy.

To be more specific, in 2020 China should import from the US at least USD 144 bn of goods

specified in the agreement. US exports of these goods to China were around USD 15 bn in first 3 months of the year, which leaves USD 129 bn for rest of the year. To fulfil its commitments, China should roughly triple the monthly imports from start of the year and import a record USD 15 bn every month in April-December.

It seems April did not bring any change in the picture, as data from China Customs show that China's total goods imports from the US were 20% lower than in April 2017. To encourage imports from the US, China removed trade war import tariffs from 79 US goods on 19 May, but this is not likely to make much of a difference.

China's commitment to increase services imports from the US does not look good either. While no data are yet available, it seems very unlikely that China can manage to meet its commitments, as the coronavirus crisis has stopped all travel and tourism, which is a major part of US services exports to China.

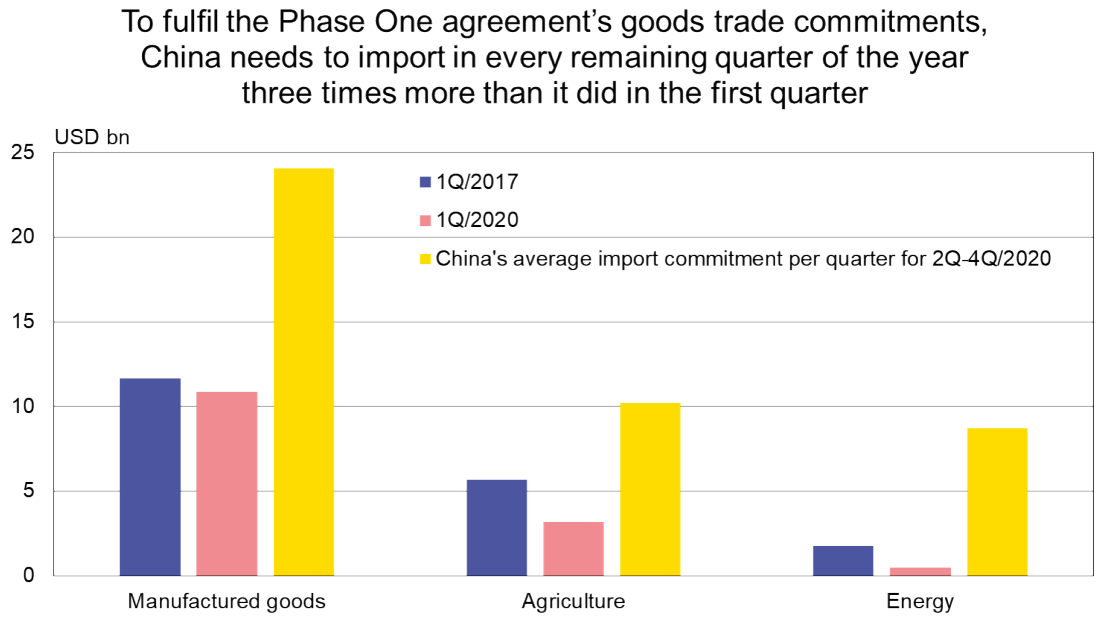
With such a sluggish start, the slow recovery of the domestic economy from the coronavirus crisis, and the collapse in international energy prices and travel, it seems impossible for China to meet its import commitments for this year. Due to the coronavirus crisis, however, it could be possible for China to ask for consultations, as the agreement allows them in the event of natural disasters or other unforeseeable events. So far, such consultations are not known to have taken place.

Instead, both parties have insisted that China will meet its commitments. In February, President Xi Jinping assured that China will meet all obligations under the agreement, despite the coronavirus crisis. A press release from the meeting of main trade negotiators on 7 May claims that "both countries fully expect to meet their obligations under the agreement in a timely manner".

The imbalance in bilateral trade has been an important issue for President Trump and he has regarded the Phase One agreement as a major win. To put more pressure on China, President Trump claimed in early May that he is not interested in renegotiating the agreement and could even terminate the agreement if China fails to meet its commitments. In mid-May, he also warned that he could cut off the whole relationship with China. As there are few obligations for the US in the agreement, it could make sense for China to just play for time.

Obviously, the Phase One agreement did not do much to solve any deep underlying issues between the countries, as government subsidies and involvement in the enterprise sector, cyber security, technology war aspects etc. were all left out of the agreement. Most of the additional import tariffs were left in place. Even if China would somehow manage to meet its Phase One commitments, these difficult issues will persist. Most likely, competition between the two super powers will only intensify.

Chart 1.



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