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## US-China Trade Update: Both Sides to Battle Stations

June 15, 2018

### Key Points:

1. The Trump administration today announced **partial implementation of its threat to impose new tariffs on Chinese goods**.
  - A first tranche of 25% tariffs on \$34 billion of goods will be applied beginning July 6. The remaining \$16 billion of goods – and perhaps an additional \$100 billion – will go through public notice, comment, and hearings to consider additional tariff application.
2. **China responded immediately with two lists of [retaliatory actions](#)** mirroring the US lists in size and scope. The first list will be applied the same day as the US tariffs, July 6.
3. **Further friction is coming** as the administration will decide by June 30 the scope of efforts to **curb Chinese access to US technology**.
  - Meanwhile, **Congress is working to reverse the administration's rescue of Chinese telecommunications firm ZTE**. Also, momentum on the Hill continues to build toward new legal restrictions on Chinese investment in the United States and controls on high technology exports from the US to China.
4. **It remains possible that this initial exchange of tariff hikes will lead to further dialogue** prior to implementation of the second tranche of punitive tariffs.
  - This trade skirmish has **already produced uncertainty that is leading to shifting trade patterns** and a re-invigorated Chinese push to wean itself from dependence on US companies.
  - The absolute value of the tariff hikes is minuscule compared to the size of the US and Chinese economies and will not alter Chinese behavior around industrial policy and intellectual property (IP). But the relationship and mood have shifted. The consequences are unpredictable, and the **consolidation of our adversarial roles in security and commercial arenas is likely to be costly** to both sides.

### **Section 301 IP Investigation**

President Trump released USTR's findings regarding China's IP practices on March 22. On June 15, the administration [announced](#) it would implement new tariffs to prevent further unfair transfers of US technology and IP to China. The impacted product list derives from the original retaliation list of approximately 1,300 tariff lines announced by USTR on April 3 and is divided into two parts containing 1,102 tariff lines. A **\$34 billion** retaliation [list](#) comes into effect **July 6, at which time the United States will apply an additional 25% tariff on the 818 tariff lines** included. **The second [list](#) targeting products that benefit from**

**China's industrial policies contains 284 tariff lines** and covers approximately **\$16 billion worth** of imports from China. USTR will conduct further review of the second list (and perhaps a yet undefined list covering an additional \$100 billion of goods) in a public notice and comment process, including a public hearing, to determine whether to impose additional duties on those products.

Shortly after Trump's announcement, **China's Ministry of Commerce responded in a [statement](#) saying it would impose measures of the "same scale and the same strength,"** and that the US tariffs were "undermining the world trade order." It added that **settlements reached in earlier discussions between US and Chinese officials were now "invalid."** The Chinese State Council immediately announced the imposition of 25% tariffs on \$50 billion worth of US goods. **China's reciprocal tariffs cover 659 items, and like the US tariffs, will be implemented in two steps. Duties on a list of \$34 billion worth of US agricultural, auto, and aquatic goods will take effect July 6.** The range of agricultural products affected by these tariffs include **soybeans, corn, rice, and other grains.** The **effective date for a separate tariff list targeting \$16 billion** of US chemical, healthcare, and energy products is **to be determined.**

### **Section Auto 232**

The new **tariffs clearly affect the overall atmosphere but are not likely to alter the course of the Commerce Department's ongoing 232 investigation on imported vehicles** and parts. The Trump Administration appears to be committed to moving quickly on that investigation, which should proceed on a parallel track, independent of steel/aluminum Section 232 trade actions, 301 IPR-related tariff hikes, and the pursuit of export controls and investment restrictions aimed at China. The Trump Administration has indicated it **may move to apply tariffs in this investigation before the November midterm elections** in the United States.

### **Investment Restrictions and Export Control**

**Treasury Secretary Steven Mnuchin has until June 30 to present to the president his department's final recommendations on Chinese investment curbs. In Congress,** Senators continue efforts to include in the National Defense Authorization Agreement (NDAA) an amendment to **restore restrictions on ZTE,** reversing the administration's deal with ZTE. A vote on the NDAA is imminent; the House has no such provision, so a conference to reconcile the two bills would be necessary. The administration is resisting the effort.

Meanwhile, Congress is finalizing legislation, the **Foreign Investment Risk Review Modernization Act ("FIRRMA"),** that would (1) expand the scope of national security reviews of foreign investments in the United States and make mandatory for the first time declarations for some foreign investments, and (2) require the Administration to assess and regulate "emerging" and "foundational" technologies under existing export controls. When/if this process is implemented, some transfers of US technology to certain countries such as China that currently do not require an authorization from the Commerce Department may require an authorization (e.g., license exception; export license).

### **Chinese Hold on Qualcomm's Bid?**

The Chinese **have not yet announced prospective retaliation for any new restrictions**

**on high technology trade, investment, or visa issuance/conditions.** Some media reports suggest Chinese approval of Qualcomm's bid to acquire Dutch chip manufacturer NXP is to be forthcoming, but conflicting reports have ensued given the new context as of today's punch and counter-punch in the ongoing trade battle between Washington and Beijing. It would **seem unlikely Beijing's approval will be forthcoming in the current environment.** We will continue to follow.

#### **Multilateral Action: World Trade Organization (WTO)**

The **US on June 14 asserted third party rights in the EU's WTO dispute settlement case with China regarding its IP/tech transfer practices.** This is **on top of the March 23 WTO consultations request by the United States** on the same topic. Separately, China has requested to join the EU, Canada, and Mexico WTO consultations with the United States over 232 steel and aluminum tariffs.

#### **Conclusion**

**The US and China have accelerated our dash toward more competitive, less cooperative relations.** On the security side, we will continue to work together on the Korean peninsula, but that seems a fragile and perhaps temporary circumstance. Taiwan looms larger in our bilateral relations and could emerge as the topmost concern in US-China ties. Skirmishing in the South China Sea has been restricted to symbols and demonstrations for the moment, but that too seems to be steadily degrading toward more confrontation. Elsewhere, we are working at cross-purposes more than we are aligning on issues ranging from climate change to Iran. Beijing and Moscow recently demonstrated their close relations at the Shanghai Cooperation Organization summit, which stood in stark counterpoint to the US clash with our allies at the G-7 meeting in Canada.

Against that backdrop, the United States battling with China over trade would seem to suggest an **avowed commitment to a strategically important set of well-articulated national interests.** But having mustered the political will to take China on, **the administration needs to answer its critics and the Chinese: what is the objective and how do we get there from here?**