

Chinese-American Misunderstandings, Disputes, and Wars

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A wise Chinese leader who I will keep unnamed told me that it pays to negotiate by finding out what the other party wants most and try to give it to them and to have them reciprocate rather than to find out what will hurt the other party and give that to them because little wars have a tendency to quickly get out of control to become big wars and anyone who has ever gotten into a big war wishes that they hadn't because they are so horrible. He referred to World War I as the classic example, while noting that it was true for most wars. He hopes that the Chinese-US trade disagreement doesn't move from a dispute to a war of any sort.

What is moving the disagreement from a dispute to a war is the fact that there are no international rules or international organizations (like the WTO) that the disagreeing parties are willing to go to for binding arbitration, so they use carrots and sticks to test each other's strengths, pushing each other until one backs down. Because Chinese and American leaders have all sorts of carrots and sticks (e.g., economic, military, cyber, etc.) that they can use, they are now determining which ones to use, how far to push the testing, and how far the other will go in inflicting pain and enduring it. The escalations come in the form of tit-for-tats—i.e., a series of escalations that can become progressively larger and more painful, and that take different forms that can extend beyond trade (e.g., to include capital wars). It's this series of escalations that the wise Chinese leader that I referred to conveyed can easily get beyond anyone's control.

In response to the US putting on its \$50 billion of tariffs, the Chinese responded, saying, "The Chinese side doesn't want to fight a trade war, but facing the shortsightedness of the US side, China has to

fight back strongly. We will immediately introduce the same scale and equal taxation measures, and all economic and trade achievements reached by the two sides will be invalidated." The Trump administration threatened to retaliate to that by adding another \$100 billion of tariffs. Right now, these numbers are very small in relation to the US's nearly \$20 trillion economy and China's economy, which is of comparable size in purchasing power terms, so that the shots that have been fired have been more of symbolic and political significance than of material economic significance. For that reason, it's too early to get excited about them, though, as the previously referred to Chinese leader said, they can escalate to become very serious, so we are all watching intently.

While I and people who are more knowledgeable than I believe the trade-balance issue can be solved so that everyone is better off, the more challenging disputes revolve around how the two countries believe their countries should be run and how that affects their perceptions of what "fair trade" is and how their companies should be supported.

The Fundamental Differences in Values and Approaches

A different wise and high-ranking Chinese official told me the most important cultural difference between Americans and the Chinese arises from the fact that to Americans the individual is of paramount importance while to the Chinese the family is most important. He explained that these deep-seated differences extend to how Americans and the Chinese run their governments, noting that the two characters that make up the word “country” in China are “state” and “family.” As a result of these deep-seated differences in views about what is best, leaders in China seek to run the country the way a family head would run a family, from the top down, putting the collective interest ahead of the individual’s self-interest, with each member knowing their place so the system works in a harmonious way. In the US, the opposite is true. Individuals are of paramount importance so the country is run from the bottom up, putting the interests of the individual ahead of the interests of the collective, with more open conflict and less respect for authority considered preferable. These differences become manifest in all sorts of ways. For example, when a highway needs to go through personal property, individual property rights will more likely stand in the way of that happening in the US than in China, and when leaders are chosen, it’s more from the top down in China while it’s more bottom up in the US. Similarly, leaders in China manage the companies in key industries more from the top down in support of the national interests, whereas the opposite is true in the US, where how companies are managed comes from the bottom up. That’s where the rub lies.

From the US perspective, there are three major criticisms:

1. The Chinese government pursues a wide range of evolving interventionist policies and practices aimed at limiting market access for imported goods, services, and businesses, thus protecting its domestic industries by creating unfair practices.
2. The Chinese offer significant government guidance, resources, and regularly support Chinese industries, most notably including policies designed to extract advanced technologies from foreign companies, particularly in sensitive sectors.
3. The Chinese are stealing intellectual property and/or not adequately protecting it—some of which is believed to be state-sponsored and some of which is believed to be outside the government’s direct control.

In other words, the Chinese government is helping its companies compete in ways that the US doesn’t do and doesn’t like, and it is making plans to do that (e.g., the China 2025 plan) while the US doesn’t make such plans and objects to China making them. While these different approaches exist in most areas, they are especially important in technology because both countries know that the country that is technologically strongest will be strongest in most other ways. While some of these differences can be negotiated to both countries’ mutual satisfactions, the most core ones that are extensions of what each country deeply believes is best can’t be negotiated away.

China Is Now a Competitor and Will Soon Be Much Stronger Than the US

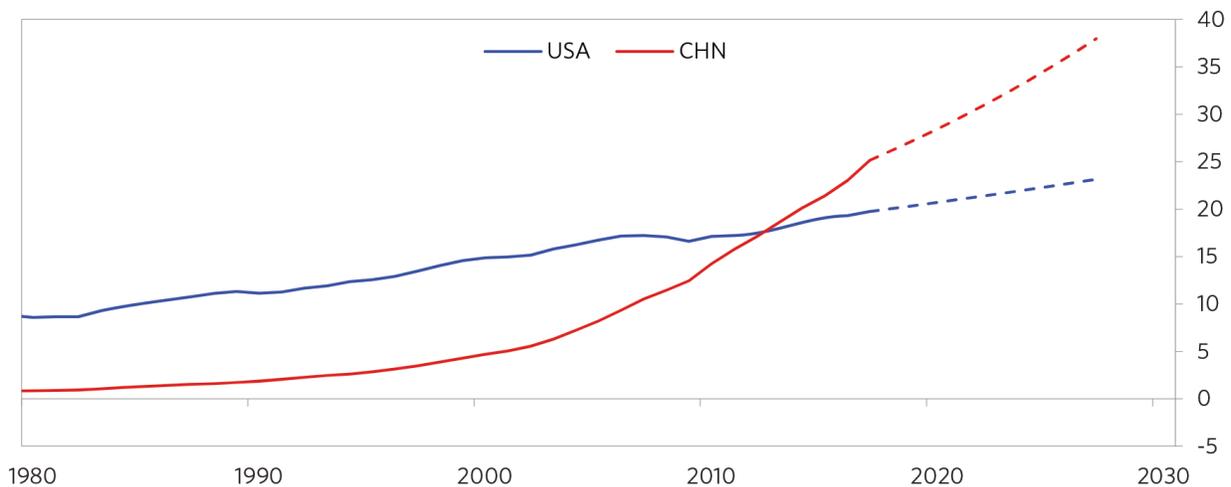
While the trade-balance issue is important, the most important questions are a) how will these countries deal with each other given their different perspectives and b) which system will work best. Most likely (and hopefully) the trade dispute we are seeing won’t lead to a disruptive war, so that both countries will evolve to very different places based on how effective their approaches are. That will have huge effects on their individual well-beings as well as their relative powers. For that reason, it is most important for the leaders of these countries to focus on what they need to do to get their own countries to do well.

In considering the question of how well these two different approaches will work, it’s important to recognize that both “communism” in China and “capitalism” in the US are now very different than they were 30 years

ago and, as a result, they're delivering very different results to their populations. It would be a mistake to think that China is a communist country that works similarly to the way communism has classically worked around the world or in China 30 years ago—i.e., very ineffectively. Instead, think of what's happening in China as being “state capitalism,” in which strategically important companies are being supported to become very competitive while the economy has a lot of entrepreneurship and the markets have quite a lot of freedom. Though different, China is being run much more like Singapore has been run for the last 30 years than how China was run 30 years ago or than how “communist” countries have classically been run. Think of it as being capitalism with the Chinese cultural characteristics previously explained. In comparison to the US, it's more from the top down with the paramount goal to have competent decision makers put into decision-making roles to determine what's best for the whole and to be held accountable for accomplishing those things.

There is no doubt that China's culture/approach has worked remarkably well and is rapidly getting better. When I first went there in 1984, I gave heads of companies \$10 calculators, which they thought were amazing, and people in Beijing and Shanghai lived in what most people would consider slums without hot running water, adequate heat, and basic appliances like washing machines and TVs. Now it is as or more advanced than the US in many ways, and improving faster. There should be no doubt that the Chinese culture/system has been very effective. The chart below shows what has happened and what we expect will happen based on our leading indicators of what make countries succeed and fail (see “Why Countries Succeed and Fail; Productivity and Structural Reforms”).

GDP (Est PPP-Adjusted, 2018 USD, Tln)



While China is a competitor and will soon be significantly larger than the US, and while such rivalries in the form of the Thucydides Trap are dangerous, it is very doubtful that the capacities of either of these countries to inflict immeasurable harm on the other will end for a very long time frame. For these reasons, we hope and expect that rational heads will prevail and tit-for-tat escalations won't accelerate to produce horrible wars.

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