

# How the Trump Administration Should Confront China's Innovation Mercantilism

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# About ITIF

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- One of the world's top science and tech think tanks
- Formulates and promotes policy solutions that accelerate innovation and boost productivity to spur growth, opportunity, and progress
- Focuses on a host of issues at the intersection of technology innovation and public policy:
  - Innovation processes, policy, and metrics
  - Science policy related to economic growth
  - E-commerce, e-government, e-voting, e-health
  - IT and economic productivity
  - Innovation and trade policy

# Today's Presentation

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1 The Problem

2 Proposed Solutions

# Evolution of Chinese Mercantilism

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- Phase 1: 1980-2006: **FDI attraction.**
- Phase 2: 2006-2012: **“Indigenous Innovation.”**
  - “National Medium- and Long-term Program for Science and Technology Development (2006-2020)” sought *absolute advantage*.
- Phase 2.5: 2012-present: **“China Inc.”**
  - “Made in China 2025 Strategy,” The “13th Five-Year Plan for Science and Technology,” The “13th Five-Year Plan for National Informatization,” “The National Cybersecurity Strategy,” and “National Guidelines for Development and Promotion of the IC Industry.”

# The Nature of Chinese Mercantilism

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- IP theft
- Forced tech transfer and joint ventures
- Abuse of anti-monopoly law
- Chinese-only technology standards
- Subsidies to Chinese firms
- Closed markets
- State-enabled acquisitions of U.S. tech companies

# China Is Unique in the Global Trading System

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- Mercantilist strategy
- Seeking autarky
- Focusing on moving up value chain
- Favoring Chinese firms
- State and market are joined
- Lack of rule of law
- Large size enables monopsony



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# Five Choices for Confronting China's Innovation Mercantilism

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1. Wait for conversion to Washington consensus
2. Harangue and implore
3. Resigned defeat
4. Global isolation
5. Constructive, alliance-based confrontation



Source: REUTERS/Aly Song/File Photo



# Constructive Confrontation: Overarching Goal

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- Only the U.S. can lead the collective defense of the market- and rules-based trading system.
- China does not fear repercussions at the WTO or the G20.
- China does fear key actors organized and coordinated in a united front to challenge its subversion of the world trading system.

# Constructive Confrontation: Make the Case and Enlist Allies

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- Build an iron-clad prosecutor's case laying out the bill of particulars.
- Assign top U.S. officials to travel the world lining up allies at the highest levels, including Europe, Commonwealth nations, Japan, and South Korea.

# Constructive Confrontation: Begin Negotiations

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- Focus on specific, performance-based results.
- If, after a reasonable but short period of time, results are lacking, the United States and its partners should begin to ratchet up consequences.
- Should results be forthcoming, measures can be reduced.

# Strengthen U.S. Organizational Capabilities

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- Establish a national industrial intelligence unit within the NIC.
- Create a sub-directorate at NSC responsible for combatting innovation mercantilism.
- Create an Office of Competitiveness at USTR, responsible for, among other matters, creating a Global Mercantilist Index.
- Increase trade enforcement and analysis resources to reflect the scale and importance of the task.
- Expand the network of IP and digital trade attaches.
- Inculcate a more tech- and IP-focused foreign commercial service and PTO.

# Develop Stronger Processes

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- Elevate trade enforcement in the interagency process.
- Strengthen the rules of engagement in negotiations with Chinese negotiators.
- Enhance application of section 337 of the U.S. Tariff Act.
- Revise and use discretionary powers under the U.S. Trade Act to address unfair trade.

# Rethink Key Policies

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- Rethink antitrust policy and push back against China's use of antitrust policies as a tool of industrial policy.
- Ensure reciprocity in IP and technology licensing.
- Reform FDI review and update CFIUS to reflect the nature of Chinese government influence.

# Additional Actions

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- Issue more general fact-finding investigations by the USITC.
- Publish Department of Commerce reports on strategic economic and trade issues.
- Deny use of the U.S. banking system to companies benefitting from stolen IP.
- Do not recognize China as a market-based economy.
- Cut off scientific and other cooperation.

# What About the WTO?

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- Use the WTO's dispute settlement body more aggressively, including filing cases re: transparency.
- But recognize there is a limit to the WTO.
  - WTO's consensus-based approach to negotiations has become untenable.
  - Dispute resolution often does not work because WTO process is premised on adjudicating laws, rules and regulations, not opaque “administrative guidance.”
  - WTO's notification, surveillance, and review of existing and proposed trade-related regulations is weak and ineffectual.



# Won't Confronting China Cause a Trade War?

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- In Davos, Chinese President Xi argued that “pursuing protectionism is like locking oneself in a dark room” in the hope of avoiding danger but, in doing so, cutting off all “light and air.”
- This overlooks that it is China that started—and continues—the trade war.
- What President Xi means by a trade war is another nation challenging unbridled Chinese economic aggression.

# America's Choice: Status Quo?

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- Significantly fewer jobs in U.S. advanced industries (e.g., semiconductors, computers, biopharmaceuticals, aerospace, Internet, digital media, automobiles, etc.) with loss of economic and national security.
- Continued loss of faith in global trade and declining global economic integration.



Source: JMiks, shutterstock

## Or Constructive, Alliance-Based Confrontation?

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- Growth in U.S. (and allies) advanced industries (e.g., semiconductors, computers, biopharmaceuticals, aerospace, Internet, digital media, and automobiles) and increased economic and national security.
- Restored faith in and effective functioning of the global market.

# Thank You!

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