US-China Trade Relations: Imbalance and Overcapacity

The 7th CF40-PIIE China Economic Forum

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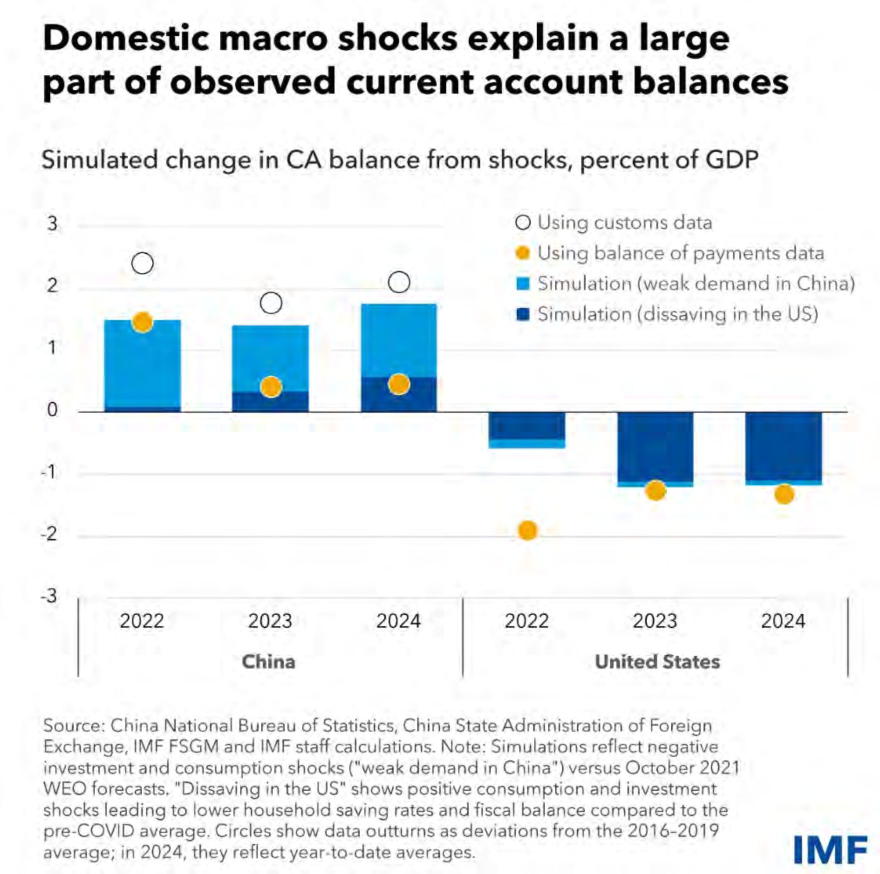
Is there a way out

- Some potential ideas
  - Fighting a full-blown trade war
  - Reducing domestic saving-investment gap
  - Purchasing more soybeans
  - Appreciating renminbi (Plaza Accord II)
  - Adopting voluntary export restraint (VER) or export tax
  - Decoupling in selected sectors
  - (Not) imposing import tariff
  - Helping with geopolitical matters



“Trade Balances in China and the US Are Largely Driven by Domestic Macro Forces”, Pierre-Olivier Gourinchas, Ceyla Pazarbasioglu, Krishna Srinivasan, Rodrigo Valdés, IMF, September 12, 2024.

Changing growth model

- Changes in economic environment and need for an innovation-driven growth model
  - Higher cost
  - Ageing
  - De-globalization

David Dollar, Yiping Huang and Yang Yao, *China 2049: Economic challenges of a rising global power*, Brookings Institution Press, 2020.

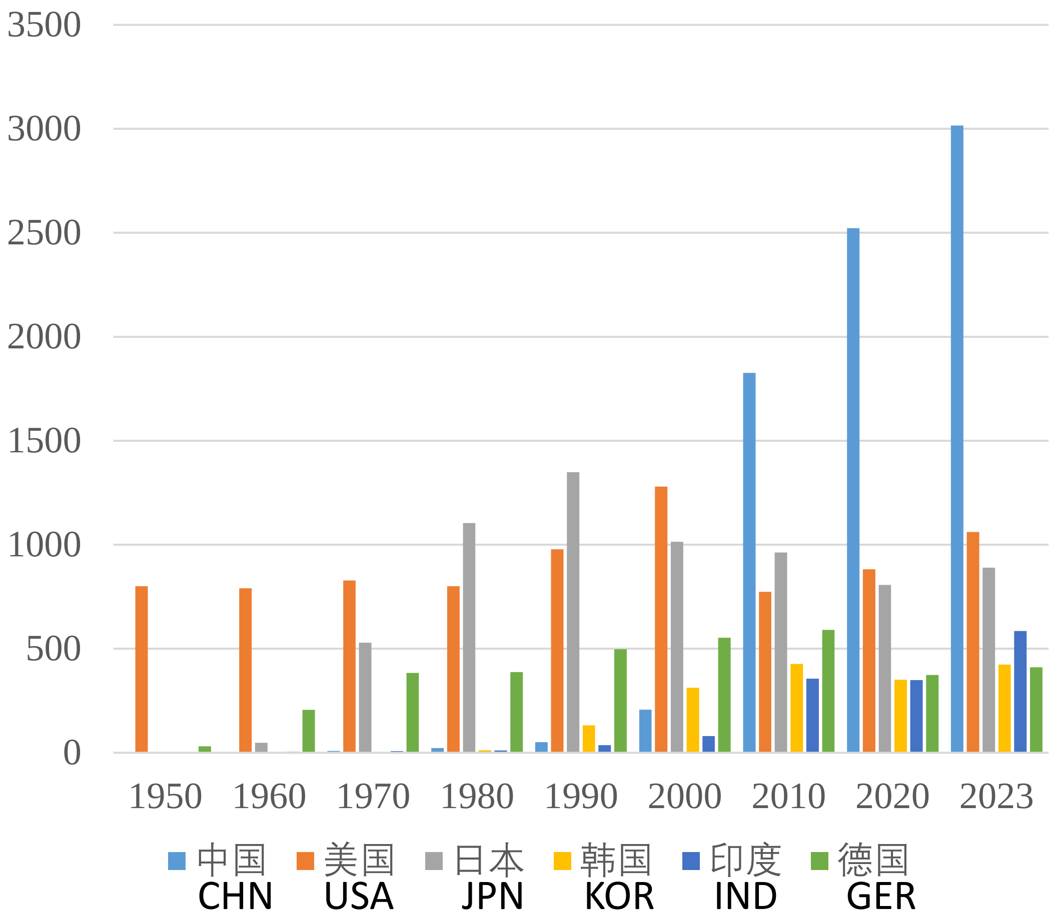
The overcapacity question

- U.S. complaints about overcapacity: state subsidy and state direction
- Policy reactions:
  - Tariffs on EVs
  - “Small yard, high fence” for semiconductors

Janet Yellen dialogue with professors of the National School of Development, Peking University on April 7, 2024

The case of EVs

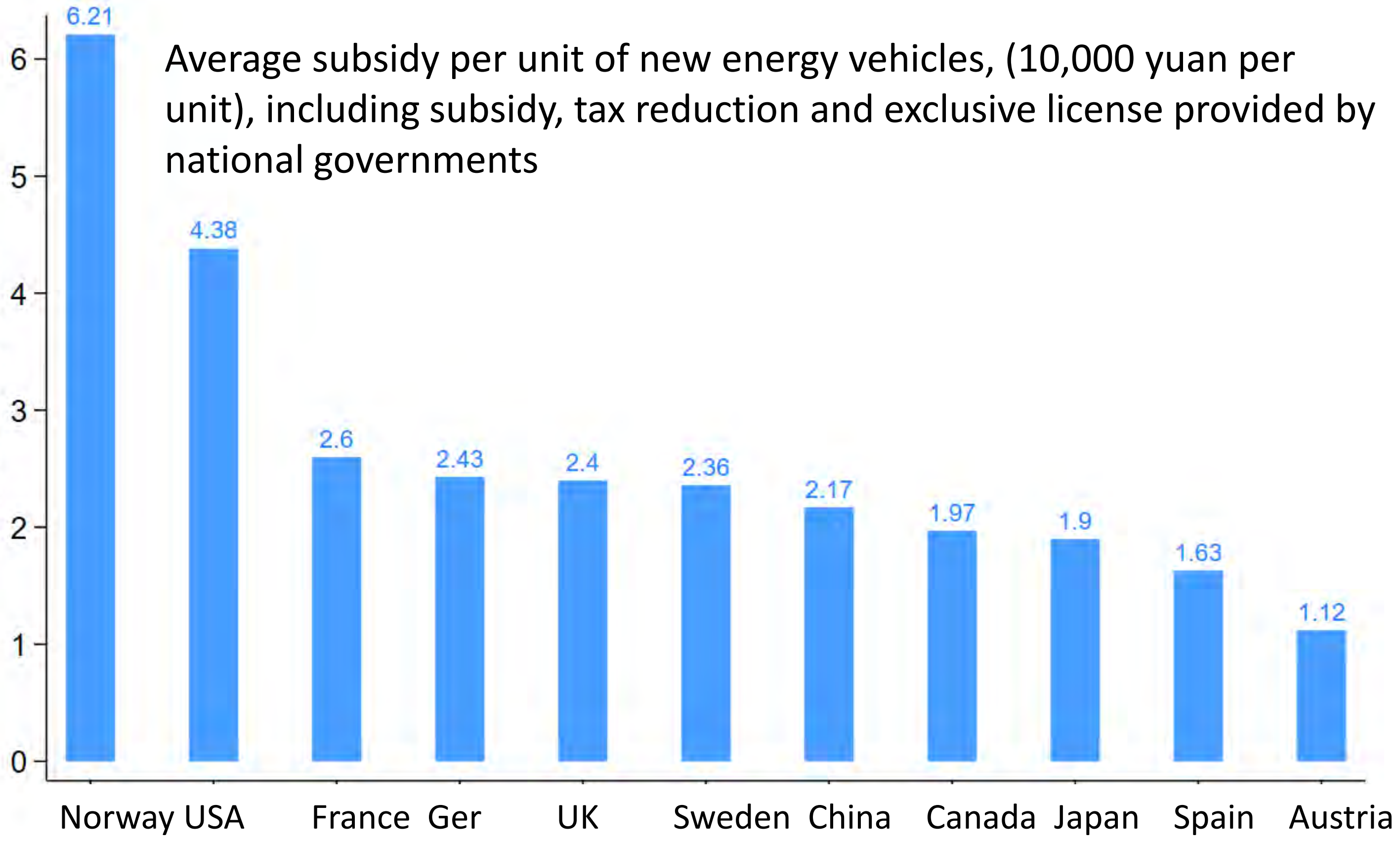
- #1 automobile output and sales for 15 consecutive years; #1 EV output and sales for 9 consecutive years; #1 exporter of vehicles in 2023
- The size factor: a large country economy



Automobile output, 1950-2023 (10,000 units)

State subsidy

- In the US: at the federal level, accelerated subsidy for EVs in 2005; introduced personal income tax reduction and exemption in 2007



Li, Shanjun, Binglin Wang, Muxi Yang, Fan Zhang, "Charging Infrastructure and Consumer Incentives Drive Cross-Country Disparities in Electric Vehicle Adoption." 2022, manuscript, Dyson School of Applied Economics and Management, Cornell University.

Factor cost distortion

- "The Center for Strategic and International Studies concludes that China spends roughly 5 percent of GDP on industrial subsidies, 10 times as much as the United States, Brazil, Germany, and Japan." (Jay Shambough 2024)
- ***But***, they are mostly due to the dual-track liberalization (for SOEs) as transition policy, not as industrial policy (for private companies)

Producer subsidy equivalent (PSE) due to factor market distortions (% GDP)

	Capital	Land	Energy	Total
2000	4.1	0.5	0.0	4.6
2001	3.9	0.5	0.0	4.4
2002	3.9	0.4	0.0	4.3
2003	3.8	1.1	0.0	4.9
2004	3.1	0.9	0.6	4.6
2005	3.0	1.3	1.7	6.0
2006	3.1	2.0	1.6	6.7
2007	3.6	1.2	1.6	6.4
2008	3.4	1.0	0.7	5.1
2009	3.5	0.9	0.7	5.1

Huang, Yiping, "Dissecting the China puzzle: Asymmetric liberalization and cost distortion", *Asian Economic Policy Review*, 2010, 5(2): 281-295.

Investment promotion programs

- Local governments implemented “investment promotion” policies to attract investors, including implicit subsidies on land
- The Third Plenum of the 20th National Party Congress decided to rein in “investment-promotion” policies and to prohibit irregular and illegal subsidies by the local governments

Local governments’ investment promotion programs

Chinese Green Marshall Plan?

- The proposal for China to devise "The Global South Green Development Plan" through market-based investment, policy lending and government aid to support energy transition in the global south
- Potential benefits
  - Helping global green development, especially in the global south
  - Stabilizing the Chinese economy
  - Reducing deficit pressure with the U.S.
- Brian Deese, the former Director of Biden's National Economic Council also called for "Clean Energy Marshall Plan" by the US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Open Questions | China's 'overcapacity' could help Global South in green transition

Frank Chen in Shanghai

Published: 2:00pm, 7 Nov 2024

Chinese economist Huang Yiping says a 'China Marshall Plan' would match excess new energy capacity with the unmet green transformation needs of emerging markets

China economy

This latest interview in the Open Questions series features Huang Yiping, dean of Peking University's National School of Development and director of the university's Institute of Digital Finance. Huang says the jury is out on whether China's economy can engineer a comeback in the last quarter of 2024 and advocates for market forces to be used to steer local Chinese economies back on track.

"Open Questions: China's overcapacity could help global south in green transition", *South China Morning Post*, November 11, 2024.