



Issue 12/2018 (June 15-28, 2018)

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**METRIX**

**2786.90**

Shanghai's benchmark stock index **Shanghai Composite Index** dropped to a two year low on Thursday, driving Asia's largest equity bourse further down into official **bear market territory**, as concerns about a trade war with the United States sent investors scurrying to extract funds from equities.

## TOPIC OF THE WEEK: US-China trade dispute goes to next round

### China fights back against United States in trade war

China is fighting back against the United States after the Trump administration has entered an open confrontation with its largest trading partner. Over the past two weeks, China hit back at a US tariff announcement with tit-for-tat measures. Previous Chinese efforts to compromise have given way to more aggressive posturing in Beijing.

Chinese President Xi Jinping also struck a harsh tone at a [meeting with CEOs of multinational companies](#) in Beijing. Speaking to a group of 20 US and European chief executives at the “Global CEO Council” held at the Chinese government’s Diaoyutai State Guest House, Xi promised to fight “protectionism,” but he also stressed that China would no longer “turn the other cheek,” but strike back against the United States. Executives of US companies UBS, Pfizer, Cargill, Carnival, Hyatt and Goldman Sachs were present at the event.

China’s party-state media have also ramped up the rhetoric against the United States. An [article in the “Global Times”](#) discussed ways to “protect Chinese companies from the attack launched by Trump.” [China experts have warned of the possibility of a boycott](#) against US companies and goods in China should Washington follow through on its threat to impose a ten percent tariffs on 200 Chinese goods – in addition to the tariffs it has already imposed or announced this year.

As the trade war between the world’s two largest economy spirals out of control, the entire global economy is at risk. A further escalation of the US-Chinese trade row could also affect global delivery chains. [European companies with production assets in the United States](#) could also suffer severe consequences. [Stock markets in Europe](#) and [Asia](#) have been rattled amid the increasingly aggressive standoff between Washington and Beijing in recent days.

The Trump administration had fired the first salvo in the trade war on June 15 by imposing tariffs on Chinese goods worth 50 billion USD. [China responded in kind](#) the same day by announcing tariffs amounting to the same value of US imports, on products ranging from meat and tobacco to cars. Just as the US tariffs, the Chinese retaliation is set to happen in two rounds. The [first round, covering goods worth 34 billion USD](#), is scheduled for early July. Similar to retaliatory tariffs imposed on the United States by the EU, they will focus on energy and agricultural products.

At the same time, the White House is considering to impose tougher restrictions on Chinese investment to protect US industries from transfer of sensitive technology and trade secrets to China. It was unclear whether the measures, to be announced before Saturday, will target China specifically or [if the White House would soften its stance](#) and leave it to Congress to strengthen the authority of the Committee on Foreign Investment in the United States, or Cfius, which screens inbound investments for national security implications.

### **A constant tit-for-tat**

Trade war measures of the United States and China



<b>Date</b>	<b>Measures</b>
March 23	US imposes tariffs of 25% on steel and 10% on aluminium imports, including from China.
April 2	China imposes tariffs on 128 categories of products worth 3 billion USD.
April 16	US bans Chinese tech company ZTE from purchasing crucial components from US firms for seven years.
April 17	China announces a 179% import tariff on US sorghum and lifts foreign investment restrictions in the transportation sector.
May 13	President Trump announces deal that would allow ZTE to buy US parts again.
May 17	China retracts the announced tariffs on US sorghum.
May 19	After intense discussions, China and the US agree to resolve their trade dispute through negotiations.
May 22	China announces that it will cut the import duty on all passenger vehicles from 25% to 15%.
June 15	US announces that as of July 6 <sup>th</sup> tariffs on 818 products worth 34 billion USD will take effect. Tariffs on 284 products worth 16 billion USD are still under review.
June 16	China retaliates by imposing 25% tariffs on 545 products, including US produced cars, worth 34 billion USD that will take effect on July 6 and announces additional pending tariffs worth 16 billion USD.
June 18	Trump orders a draft of additional tariffs on 200 billion USD worth of Chinese imports, if China does not retract its countermeasures of June 16 <sup>th</sup> . US Senate reimposes the ban on ZTE.
June 21	The Chinese Ministry of Commerce asserts that China has "no choice but to take comprehensive measures combining quantitative and qualitative ones to resolutely strike back," Xi states that "in our culture, we punch back."
June 25	US is drafting curbs hindering firms with at least 25% Chinese ownership from purchasing US companies that are "industrially significant technology." It remains unclear whether the imposed investment restrictions are focused specifically on China or not.

## CHINA AND THE WORLD

### Xi meets Mattis: Won't give up "one inch" of territory

The visit of Pentagon chief Jim Mattis in China has laid bare mounting tensions not only over trade issues but also over territorial claims. After talks with Mattis, China's President Xi Jinping stressed that China was committed to peace but would not give up "even one inch of the territory left behind by our ancestors," according to reports in Chinese media. Mattis kicked off a three-day visit to China on Wednesday, with North Korea and tensions in the South China Sea at the top of his agenda.

Mattis and his Chinese counterpart Wei Fenghe described their first meeting on Wednesday as "open and honest" and sought to strike a positive note despite Sino-US tensions over several issues. Mattis, the first US defense secretary to visit China since 2014, will also travel to South Korea and Japan.

Before the trip the Pentagon said that Mattis would deliver a "medium tough" message to Beijing. After his talks with Xi and Wei, he stressed that the US was assigning a "high degree of importance" to the military relationship with China.

The US defense secretary is highly critical of China's actions in the South China Sea and has accused Beijing of "intimidation and coercion" when it placed weapons on a number of disputed islands. The US military even withdrew an invitation to China to join a multinational naval exercise that will start during Mattis' visit.

Beijing has been angered by US naval patrols, known as freedom of navigation operations, through the South China Sea. Beijing is also suspicious of Washington's continuous support for the self-governing island of Taiwan. In the run-up to Mattis' visit, Chinese warships held daily combat drills in waters near Taiwan, and the Chinese air force conducted frequent exercises near the island, which Beijing regards as a renegade province of the People's Republic.

Despite these tensions, the US and China have common interests in the region such as ensuring peace and stability on the Korean peninsula. China welcomed the summit meeting earlier this month between US president Trump and the North Korean leader Kim Jong Un.

### Xi outlines vision for foreign policy under CCP leadership

China's president and CCP General Secretary Xi Jinping aims to expand China's global influence through a new form of, "major country diplomacy with Chinese characteristics." In an appearance at the Central Conference on Work Relating to Foreign Affairs on June 22 and 23, the party and state leader struck a confident posture.

According to Xi, the world is undergoing the "most profound" changes in a century. He described China as in the "best period of development in modern history," and affirmed his commitment to the reform of

global governance. Xi spoke before an audience of members of the Politburo Standing Committee, Chinese ambassadors and consul generals from around the world, members of other government agencies as well as financial institutions and large enterprises.

According to a [Chinese extract of his speech](#), Xi stressed cooperation with developing countries, which he described as China's natural allies in the quest to reform "global governance". He also mentioned "far-reaching changes in relations between major powers," which can be interpreted as a sign that China views itself at an advantage compared to the United States.

In a notable shift from the previous work conference on foreign affairs in November 2014, Xi stressed the importance of the CCP and its Central Committee in formulating China's foreign policy. The fact that this is the second such conference in four years underlines the continued importance Xi attaches to foreign policy in his second term. His predecessors Hu Jintao and Jiang Zemin had only held one such event in their entire time in office.

#### News in brief

- [China hosts first China-Africa Defense and Security Forum](#)
- [Kim Jong Un visit Beijing again, discusses economic development](#)
- [Xi calls for an elite maritime force during PLA Navy inspection](#)

## POLITICS, SOCIETY AND MEDIA

### Less internet censorship for foreign tourists – Hainan initiative hits snag

The provincial government of Hainan wants to unblock websites such as Facebook, YouTube and Twitter to make the tropical island more attractive to foreign tourists. The authorities want to set up special areas in the cities of [Haikou and Sanya](#) where censorship would be less strict than elsewhere, the government said. The initiative is part of a three-year plan to promote tourism which was published on the government's website on June 21. A day later though the plan was removed from the site, indicating that the proposal hit a snag.

No official explanation was given for the sudden removal of the plan. But China has tightened internet controls over recent months, and Hainan's move might have been considered too far-reaching. In the past, similar initiatives were also stopped. In 2013, reports suggesting the new free trade zone in Shanghai would allow access to Facebook and Twitter were swiftly denied.

Hainan's plans triggered heated debate on social media platforms. Commentators decried "double standards", discrimination and a "return to feudalism and colonialism." Screenshots of the plan were still circulating online on Tuesday. It is possible that the provincial government wanted to test how far it can go given the central government's plan to open the island to trade and investment and turn it into the country's [biggest free-trade zone](#).

As part of its tourism plans the province also said it would bring 50,000 English-speaking foreign workers to the island and increase the number of foreign students to 3500. The island will place advertisements in international media to attract foreign talent.

### **Restrictions on abortions in Jiangxi province stir controversy**

Jiangxi has become the latest province to introduce tighter rules on abortions, prompting fears among activists that the state could put **further restrictions** on women's choices.

The provincial government issued guidelines on June 20 stipulating that abortions after 14 weeks of pregnancy are only allowed if medically necessary. A woman wishing to terminate a pregnancy at that stage will need signed approval from three medical professionals. Similar rules have been in place in several provinces for years. The measures are meant to help prevent sex-selective abortions, which are illegal but common in China and have left the country with a massive gender imbalance of 30 million more men than women.

As part of China's strict family planning policy introduced in 1979, the authorities have long encouraged abortions alongside contraception and sterilization as means to slow population growth. Restrictions on family size, known as the one-child-policy, were loosened in recent years to allow all parents to have two children. However, the new policies **have failed to** resolve China's demographic problems, including a rapidly ageing society.

### **News in brief**

- **Disciplined: Party punishes 7199 officials in May for violating austerity rules**
- **Deleted: Tencent discloses self-censorship activities for the month of May**
- **Dispersed: Police breaks up protests by military veterans in Eastern China**
- **Dispatched: Chinese military employs bird-drones for surveillance in Xinjiang**

## **ECONOMY, FINANCE AND TECHNOLOGY**

### **China's central bank props up liquidity amid rising economic insecurity**

Following a slowdown in growth, especially in investment and retail, China has taken steps to inject liquidity into its economy. By **lowering the reserve requirement ratio** (RRR) for some banks by 50 basis points, the People's Bank of China (PBOC) freed up 700 billion CNY (108 billion USD) in liquidity. The recent RRR reduction is the third this year. The step is intended to spur lending to small and medium-sized companies (SMEs) as well as to promote debt-to-equity swaps for highly indebted state-owned enterprises (SOEs).

Only a few days earlier, China's **central bank lent 200 billion CNY (31 billion USD) to financial institutions** via its medium-term lending facility (MLF). These moves came after the central bank's unexpected decision earlier this month to not follow the US Federal Reserve in its interest rate increase.

The policy adjustments show that China seeks to balance its recent campaign to decrease debt in its financial system. The campaign is beginning to negatively affect economic growth just as trade tensions with the United States add to insecurity.

The latest reduction in RRR is a targeted adjustment of monetary policy rather than an overall reversal of the deleveraging campaign, but its commitment may soon be put to a test. While the support for SMEs is understandable, the promotion of debt-to-equity swaps for SOEs shows a reluctance to limit inefficient use of capital or to let inefficient SOEs go out of business.

### **China institutionalizes battle against environmental pollution**

The Chinese government and CCP have emphasized their commitment to the fight for a healthier environment. A document **published by the State Council and the CCP Central Committee** on June 24 introduces President Xi Jinping's thoughts on "Ecological Civilization" (生态文明), stressing the need for "a harmonious symbiosis of people and nature." It elaborates on goals for clean air, clean water and clean soil to be reached by 2020. The document calls for reforms of the administrative system, but also of business operations across different sectors requiring, for instance, facility upgrades and a reduction in coal consumption by five to ten percent compared to 2015 levels.

Other goals state that citizens of Chinese cities at prefecture level and above shall enjoy "good air days" 80 percent of the year. Within three years, over 70 percent of the country's surface water is supposed to be drinkable. The ratio of polluted land that can be safely used is to reach about 90 percent. The document further emphasizes the use of "ecological red lines" to protect at least 25 percent of China's land from further exploitation and identify metropolitan regions like the Beijing-Tianjin-Hebei and the Yangtze River Delta as primary battlefields.

The targets build on previous plans such as the Thirteenth Five-Year Plan for Ecological and Environmental Protection. They are, however, very ambitious. During the period covered by the previous five-year plan (2011-2015), almost **half of all Chinese provinces failed to meet** their water quality targets.

### **News in brief**

- **Real estate: Nationwide property database is set up to combat corruption**
- **Alibaba rival: Google makes strategic investment of 550 Mio USD in JD.com**
- **Skills shortage: China plans to build nuclear technology university in Tianjin**
- **Mobile phones: Domestic roaming fees will be scrapped on July 1**
- **Free Trade port: Shenzhen aims to convert its port by 2020**

## THE EUROPEAN VIEW

### China looks set to benefit from Erdogan's election victory

China has welcomed the re-election of Recep Tayyip Erdogan as Turkey's president and could emerge as a clear beneficiary of a possible strategic re-alignment of Turkey in the next few years. Chinese foreign ministry spokesman **Geng Shuang** said on June 25 that Beijing congratulated Erdogan and respected "the choice made by the Turkish people."

Under the leadership of Erdogan Turkey has taken an interest in closer ties with both Russia and China in what some analysts have called an "eastern pivot." At the same time relations with Western partners have soured, especially after the Turkish government imposed sweeping emergency measures in the wake of the attempted coup in 2016. Turkey's military intervention in northwestern Syria targeting Kurdish groups has further complicated relations with its allies within NATO.

As part of its „eastern pivot“ Turkey has repeatedly expressed an interest in the Russia- and China-led Shanghai Cooperation Organization (SCO). Ankara is already a dialogue partner of the SCO but might look more closely at the option of membership. Full membership, however, would most likely be incompatible with NATO membership. Turkey has also endorsed China's Belt and Road Initiative (BRI), Beijing's key foreign policy project. Under his "2023 Vision," Erdogan hopes for an infrastructure building boom that would doubtless benefit from Chinese expertise and finance. China has already completed one high-speed railway project between Ankara and Istanbul and is ready to invest more as it sees Turkey as a country well positioned to fulfill BRI's cross continental ambitions.

## MAD MERIX

### China blocks HBO website after John Oliver mocks Xi Jinping

The Chinese propaganda apparatus was not amused when they heard comedian John Oliver talk about China's president and party leader Xi Jinping in his weekly HBO program "Last Week Tonight." They scrubbed the name of the comedian and the show from the microblogging site Weibo and blocked HBO's website in China, after John Oliver told his audience **on June 17** that Xi hates being compared to Winnie the Pooh by Chinese internet users.

Xi and the censors most probably disapproved of other items in the show, which dedicated almost 20 minutes to recent developments in China, as well: Oliver talked about prison camps in Xinjiang province where tens of thousands of Uyghurs are being held. He satirized this year's plenary session of the National People's Congress at which only two of the roughly 3000 delegates dared to vote against scrapping the term limit for Xi. And he criticized censorship in China, including efforts to silence discussions of late Nobel Peace Prize laureate Liu Xiaobo and his wife who is under house arrest. Last but not least, the British-born comedian mocked a videogame issued by Chinese state media which prompts

players to punish corrupt officials with electric shocks. The censors might have wondered why Oliver did not think the game was funny.

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