The strategic competition between the United States and China has slowly bifurcated the world economy into two ecosystems of economic and trade activities—a process described in the September 2020 Atlantic Council issue brief “One World, Two Systems Take Shape during the Pandemic.” Each side has developed a strategy to compete for security and influence in the new world landscape. The West—including the United States—has adopted a combination of decoupling economic activities from China and reshoring back to the home country—with different scopes, degrees of urgency, and industry emphases by different countries. For its part, China has articulated a “dual circulation” policy to guide its economic development in its 2021-25 Five-Year Plan and beyond. What are the concrete elements of each approach and how have they been implemented in the past four years? How will they affect the United States, China, and the global economy in general?

I. DECOUPLING AND RESHORING

In the United States and more generally the West, the idea of decoupling economic activities from China germinated from growing anti-globalization sentiment. The anti-globalization feeling gathered force after the Great Financial Crisis in 2007-08 and the following Great Recession—when it became clear that the top 10 percent of the population had accumulated even more wealth while most working people endured stagnant wages with little savings. This feeling of being left behind by globalization has fueled a rising wave of populism in many Western countries,

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eventually contributing to the United Kingdom’s (UK’s) vote for Brexit and the success of Donald Trump’s presidential campaign, both in 2016. Trump struck a chord with many working Americans when he identified globalization and free trade as having caused the hollowing out of the US manufacturing base, resulting in manufacturing unemployment and the Rust Belt, and promoted “America First” as a response. From this starting point and with his fixation on the US trade deficit as a measure of the loss the United States has suffered as a result of decades of globalization, Trump quickly turned his attention to China as the major offender, having engaged in unfair trade practices including theft and forced transfer of technologies to the disadvantage of the United States. Anti-globalization sentiment in the United States has been channeled largely through anti-Chinese unilateral policy actions.

### TRADE WAR

The first spate of actions involved unilateral tariffs on a range of imports from China, starting in 2018 and using Section 301 of the 1974 Trade Act against unfair trade practices damaging to the United States. After several rounds of tariff hikes and the signing of the “phase one” trade deal in January 2020, US tariffs on $370 billion in Chinese goods stood at an average rate of 19.3 percent—ranging from 7.5 percent to 25 percent. The United States has also imposed tariffs on imports of steel (20 percent) and aluminum (10 percent) from China, Europe, and elsewhere, under authority of Section 232 of the Trade Expansion Act of 1962 against threats to US national security. China has reacted by raising tariffs on $75 billion in US goods at an average rate of 20.3 percent, but has cut tariffs on imports.

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from non-US members of the World Trade Organization (WTO) to an average of 6.7 percent (from 8 percent previously). China has complained to the WTO about the United States’ unilateral imposition of tariffs, and the WTO has ruled that the United States’ actions are illegal. In addition, complaints by the European Union (EU) and several other countries regarding the US tariffs on steel and aluminum are still pending at the WTO. These WTO rulings and complaints remain symbolic at present since the United States has rejected them and the Appellate Body is inoperative—so no final decisions can be reached. While there are many indications that the Joseph R. Biden Jr. administration will maintain the tariffs on Chinese goods—not least due to anti-Chinese sentiment in Congress—the steel and aluminum tariffs, especially on European countries, could conceivably be lifted sooner as a gesture of goodwill toward the United States’ transatlantic allies.

TECH WAR

The US-Sino trade war using tariffs has quickly expanded to encompass a tech war, triggered by US concerns about the leading role of Huawei, a Chinese high-tech company with the largest global market share in infrastructure and equipment for 5G (fifth-generation) technology. The concern is that Huawei uses its 5G equipment embedded in telecommunication networks in the United States and other countries to collect intelligence and turn it over to the Chinese authorities—a concern exacerbated by the passing of China’s National Intelligence Law in 2017. In addition, the United States has been worried about losing its leading positions in critical technologies. Consequently, it has moved to exclude Huawei and other Chinese high-tech companies like ZTE from being used in US telecom infrastructure, and pushed its allies to do the same. More generally, the United States has proposed a “Clean Network” solution to other countries, promoting the use of non-Chinese equipment in telecom networks on national security grounds.

The United States also passed the Foreign Investment Risk Review Management Act in 2018 to strengthen the Committee on Foreign Investment in the United States (CFIUS) and scrutinize more stringently inward investment, mainly from China, with a broadened mandate. Basically, instead of focusing on investment projects in a few critical areas resulting in majority control by a foreign company, the CFIUS will screen a wider range of cases that give a foreign company access to nonpublic information (for example, through representation on the board of the recipient company). Several US allies have followed suit. The EU has passed a regulation to establish a framework to screen foreign direct investments (FDI) into the Union, including by better coordinating members’ screening mechanisms. The UK has legislated a National Security and Investment Bill to strengthen the screening of foreign investment. The bill is presently going through its third reading in Parliament. Japan has also tightened entry by foreign investors in twelve strategic sectors.

Another recently passed law, the Export Control Reform Act (2018), has tightened the US export control regime, mainly by extending the Entity List of foreign companies and entities for which US persons need to obtain a license to do business with. By now, the Entity List and the Military End User List contain the names of more than four hundred Chinese companies and address a wide range of critical areas, reaching beyond telecommunications to include military and dual-use technologies, which are deemed to pose risks to national security. The ban on doing business with companies on those lists has been extended to cover exports to China by non-US companies using US technologies and inputs.

DECOUPLING AND CONTAINMENT

The measures described above are used to selectively decouple the United States from China—mainly in targeted high-tech areas and, as a result of the Covid-19 pandemic, in critical pharmaceutical and medical products. The main objective is to shift production of those goods back to the United States (“reshoring”) or to countries viewed as friendly and trustworthy to reduce reliance on China and minimize risks to national security. In addition, technological decoupling can also be seen as an effort by the United States to contain China, cutting off its access to US advanced technologies and therefore delaying or derailing its rise to a position where it would be able to challenge the United States technologically and militarily. In this vein, the Trump administration banned US portfolio investment in Chinese companies suspected of having ties with the military or exploiting slave labor in Xinjiang.

It appears that the Biden administration will maintain a tough line on China. It has reaffirmed the view that China is the “most serious competitor” of the United States, and indicated that the current array of tech sanctions on China will stay in place for now. It has also planned to unveil a modular approach to forming alliances with different groups of “techno-democracies” around specific issues of interest to each group—from artificial intelligence (AI) to 5G to export controls—to counter China’s tech ambitions. More generally, it has promised to undertake a critical review of supply chains in key sectors with the view to reducing dependency on China.

In addition to making it more difficult for US companies to do business with China (through tariffs) and with Chinese companies on the Entity and Military End User Lists, the Trump administration and Congress made a range of proposals to increase taxes on US companies’ profits derived from Chinese businesses, and to cut taxes and relax regulations for US companies relocating production facilities back home. However, not many of those ideas have been officially adopted so far.

There have also been talks about forming a T12 group of techno-democracies and there is a proposal from the EU to form a Trade and Technology Council with the United States, all aiming to coordinate tech policies as well as research and development (R&D) efforts within a group of like-minded countries to counter China’s digital authoritarianism. Again, it remains to be seen how far these ideas will move forward under the Biden administration.

OUTCOME OF THE TRADE WAR

After four years, the outcome of the trade war using tariffs is becoming clear: The United States seems to have suffered worse consequences than China. According to a recent study commissioned by the US-China Business Council, the trade war has hurt the US economy and failed to achieve major policy goals—resulting in a peak loss of 245,000 jobs. Specifically, the US tariffs have been paid, not by China as the Trump administration claimed, but by US importers and consumers, especially companies using imported steel, aluminum, and other intermediate inputs whose prices have been lifted by the tariffs. Employment in the US steel and aluminum industries has increased a little bit, but employment in other manufacturing sectors using steel and aluminum has fallen more—resulting in a reduction in manufacturing employment compared with what could have been without the tariffs.

A recent report by the Brookings Institution put it succinctly: “the tariffs forced American companies to accept lower profit margins, cut wages and jobs for US workers, defer potential wage hikes or expansions, and raise prices for American consumers and companies.” In addition, while the US goods trade deficit with China shrunk by 26 percent to $311.8 billion from 2018 to 2020, the total deficit increased by 3.8 percent during the same period to $904.9 billion—or by about 25 percent since President Trump took office in 2017. This confirms the point many economists have made that focusing on bilateral trade deficits is not meaningful and that tariffs just divert trade and trade imbalances to other countries, without reducing the overall trade deficit. By contrast, China’s trade surplus rose to a record high of $535 billion in 2020, especially in the second half of that year as its economy was the first among those of major countries to recover smartly from the pandemic, and was therefore in a position to meet foreign demand for many goods.

In terms of the phase one trade deal, China has purchased about $100 billion (or 58 percent) of the $173 billion in covered products pledged for 2020—and is halfway through the $200 billion (above 2017 baseline levels) committed for 2020-21. It remains to be seen if the Biden administration will still hold China to its commitments to increase purchases by $200 billion by the end of 2021. As part of the deal, China has also opened market access for foreign institutions in three sectors—asset management (worth $14.6 trillion), life insurance (with gross

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written premiums of $393 billion in 2018), and banking (with total assets worth $48 trillion), including allowing wholly owned foreign affiliates in asset management.

OUTCOME OF THE TECH WAR

In contrast to the trade war, the tech war—which involves investment and import and export controls of high-tech goods—will probably have a broader and longer-lasting impact on China and the rest of the world. These restrictive measures have caused considerable difficulties for targeted Chinese companies, probably delaying their business plans for several years. Specifically, Huawei and ZTE equipment has been banned from the 5G telecom networks of the United States and other countries including the UK, Sweden, Australia, Japan, India, and Poland as well as being restricted to noncritical areas of the telecom networks of several more countries. More generally, the ban on US companies and non-US companies using US technologies and other inputs in producing goods sold to China has disrupted to varying extents the business operations of Chinese companies included in the lists. Of particular concern to Chinese companies is their curtailed access to high-end semiconductor microchips. This is a very vulnerable “choke point” for China as it relies on imports to meet over 80 percent of domestic demand for semiconductor products—China’s own production accounts for 7 percent of the global total but its demand makes up 33 percent of the global total.20 In 2020, China stepped up its imports of computer chips to $350 billion (a 14.6 percent increase over 2019) in an effort to build up an inventory of the products subject to the ban.21 The US ban covers practically all of its foreign sources—including especially the market leader in global foundries (which actually manufactures computer chips), Taiwan Semiconductor Manufacturing Company (TSMC), and even the Chinese company Semiconductor Manufacturing International Corporation (SMIC).

China has reacted by launching several projects to boost domestic R&D and accelerate the development of its manufacturing capability in advanced semiconductors and other high-tech products to reduce its vulnerability to US actions. Furthermore, China has also strengthened its screening of foreign investment on national security grounds; established a list of unreliable companies to be monitored and possibly sanctioned; and allowed Chinese companies to sue for damages caused by foreign companies complying with US or international sanctions against China. The US sanctions and China’s countermeasures have led many non-US companies to find ways to separate the supply chains in their US and Chinese businesses, so as not to get caught in the US-Sino conflict. In short, technological decoupling will raise costs and reduce efficiency in the global economy. This will foster a bifurcation of technological and manufacturing activities into US and Chinese ecosystems. In particular, the decoupling in data and standards, which have become the areas of contention, will have a significant impact in the development of new technologies, according to many observers.22

Basiclly, tech decoupling, even if targeted, will be costly to all parties. It will disrupt and delay China’s high-tech production and progress. According to a recent report by the US Chamber of Commerce and the Rhodium Group, tech decoupling also costs the United States in terms of lost sales and market share, results in smaller economies of scale including in R&D, and

strengthens competitors—especially in industries like aviation, semiconductors, chemicals, and medical devices. Furthermore, it should be kept in mind that, while not guaranteed, China’s efforts to develop domestic capabilities to replace the banned US technologies and products could eventually bear fruit. In that case, US influences will be weakened as China becomes independent of US technologies, and is increasingly able to drive the Sino-centric ecosystem. To minimize vulnerability to US extraterritorial sanctions, many non-US companies could also seek to use non-US technologies and inputs to produce for China and other countries sanctioned by the United States. If these possibilities materialize, that would reduce world demand for US advanced technologies and products. Containment can work both ways!

RESHORING

The reshoring effort has produced mixed results. A reshoring index (defined as the percentage of manufacturing imports to gross domestic manufacturing output) developed by the consulting firm Kearny for the United States shows a decline to 12.1 percent in 2019 from 13.1 percent in the previous year. However, this represents a single data point and more observations are needed before concluding that a downward trend in manufacturing imports can be established. In any event, the overall impression so far is that many international corporations have shifted some of their production activities from China, but this is consistent with a broader trend of diversification from China—including by Chinese companies. Dubbed “China Plus

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A Lynas Corp worker walks past sacks of rare earth concentrate waiting to be shipped to Malaysia, at Mount Weld, northeast of Perth, Australia August 23, 2019. Picture taken August 23. REUTERS/Melanie Burton
One, this strategy is popular among many companies that have invested in China and has been in motion for the last ten years or so, driven by rising labor costs in China. This accounts for the fact that most of the diversification moves have been to countries with lower production costs relative to China—such as Vietnam, Malaysia, Indonesia, and Mexico (thanks to its membership in the United States-Mexico-Canada trade agreement)—rather than back to their home countries in the United States or Europe. In a targeted effort, Japan launched a reshoring fund worth ¥243 billion ($2.3 billion) to help its companies repatriate—but the fund is minuscule compared with the stock of Japanese FDI in China—estimated to be $130 billion—so nothing much has come of it. Moreover, any repatriated manufacturing activity will likely be performed to a large extent by robots instead of humans, limiting the extent to which manufacturing jobs will be created—a goal sought by Western policy makers.

Basically, the fact that modern production has been globally integrated, relying on sourcing numerous inputs from many countries depending on their comparative advantages, it makes more sense to think of the movements in production bases as diversifying from concentration risks in China rather than moving everything back to the home country.

One example of the potential for, and the international dimension of, the decoupling/reshoring approach is the case of rare earths—a group of seventeen minerals critical to the production of many high-tech and defense-related goods. China used to practically monopolize the mining and processing of rare earths, accounting for 98 percent of their global production in 2010. China has been willing to weaponize its exports of rare earths, as it did during its dispute with Japan over a group of small islands in the sea between the two countries in 2010. In response, to develop a non-Chinese supply chain in rare earths, Japan Oil, Gas and Metals National Corporation, a state-owned enterprise, funded Australian company Lynas Rare Earths Ltd. to extract rare earths at the Mount Weld mine in Australia and process them in Malaysia, producing twenty thousand metric tons a year—much more than the five hundred tons per year the US Defense Department needs. In addition, the Pentagon has funded other groups to produce and process rare earths at the Mountain Pass mine in the United States. As a result of those developments, China’s share of global rare earths production fell to 58 percent in 2020.

In any event, despite the ongoing debate about reshoring, FDI continues to flow into China, helping it surpass the United States in terms of FDI inflow in 2020—$163 billion versus $134 billion for the United States. It is also noteworthy that outward FDI from China to other countries has risen substantially in recent years, almost matching the magnitude of the inward FDI flows—reflecting a move overseas by Chinese companies. Portfolio capital inflows into China also reached a record level of more than $160 billion in 2020, driven by large inflows to China’s domestic fixed income markets following liberalization moves by the authorities.

BIDEN’S APPROACH

Under the Biden administration, selective decoupling efforts in security-sensitive technologies and critical healthcare products will probably be maintained and refined. The reshoring efforts will fit into the “Build Back Better” agenda to invest in infrastructure and training and provide other incentives to revive the US manufacturing base and improve its productivity. Or, as President Biden said, “We will compete from a position of strength by building

back better at home.”\(^{32}\) Concretely, he just signed an executive order to strengthen Buy American provisions for the federal government (however, the order’s impact is likely to be minimal as about 96 percent of federal procurement is already domestically sourced), and reaffirmed his support for the Jones Act, which mandates that only US-flag vessels carry cargo between US ports (even though many economists have long criticized this as being costly for US and international trade).\(^{33}\) The administration has also made clear that its focus is on increasing jobs and wages in the United States, instead of pushing China to open markets for major US financial services companies or concluding new trade agreements—as part of its foreign affairs and trade policy designed to work for the middle class.\(^{34}\)

II. CHINA’S DUAL CIRCULATION STRATEGY

In response to the US-initiated trade and tech wars and under pressure from the Covid-19 pandemic, China has articulated a “dual circulation” strategy to guide its economic development in its 2021-25 Five-Year Plan, as part of its efforts to achieve long-term objectives set for 2035.\(^{35}\) While some observers in the West have dismissed this as sloganeering, or just another name for import substitution, the dual circulation approach actually builds upon previous policy initiatives to address China’s “unbalanced, uncoordinated and unsustainable” growth pattern that former Premier Wen Jiabao succinctly warned about in his speech in 2013.\(^{36}\) China also seeks to generate synergies between international and domestic economic activities to promote overall growth.

Essentially, China’s leaders have tried to rebalance their economy to reduce the country’s dependence on fixed asset investment and export as key engines of growth in favor of stronger private domestic consumption including of services. Much progress has been made in these rebalancing efforts, but more remains to be done. Foreign trade in terms of exports plus imports has declined as a share of China’s gross domestic product (GDP) from a peak of 65 percent in 2006 to 35 percent at present—a ratio just a bit higher than the United States’ 27.5 percent, but much lower than 90.7 percent for the EU.\(^{37}\) Meanwhile, domestic consumption in China accounted for 39.1 percent of GDP in 2019, having risen from 30.6 percent in 2010, and the service sector has grown significantly in recent decades to account for 46 percent of GDP.\(^{38}\) Nevertheless, both of these ratios are still much lower than those in most other countries. Generally speaking, it is important to note that these rebalancing efforts have been consistent with long-standing policy recommendations by international organizations such as the International Monetary Fund (IMF) and the World Bank.

In addition, the dual circulation strategy aims to balance globalization with self-sufficiency, which a recent Center for Strategic and International Studies’ report referred to as “hedged integration.”\(^{39}\) Basically, China wants to encourage globalization—to access international markets for capital (especially FDI), financial services (especially asset management skills), and high technology to benefit China but on terms acceptable to it—while at the same time promoting self-reliance, especially in technology, to reduce its vulnerability to foreign (in particular US) pressures and to international economic and financial cyclical fluctuations generating negative spillover effects.

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34 The White House, “Remarks by President Biden on America’s Place in the World.”


INTERNATIONAL CIRCULATION

One leg of the dual circulation strategy is international circulation. The main objective here is to diversify China’s foreign trade to reduce its reliance on any one country, especially the United States. China has made good progress on this front with its foreign trade well diversified geographically. Specifically, during the past four years of trade war, China has raised tariffs on US goods in retaliation to US moves but has reduced tariffs on non-US trading partners and increased imports of soybeans from Brazil and Argentina. Recently, China signed two major agreements to encourage the shift from the United States—namely, the Regional Comprehensive Economic Partnership with Asia and the Comprehensive Agreement on Investment with the EU. It has also upgraded its free trade agreement (FTA) with New Zealand to extend coverage to new sectors and abolish tariffs on most goods; tried to revive the trilateral FTA negotiations with Japan and South Korea; expressed its intention to negotiate entry to the Comprehensive and Progressive Agreement for Trans-Pacific Partnership; and reaffirmed its commitments to the Belt and Road Initiative (BRI). Consequently, China’s trade with the United States has declined while trade with other countries has increased, boosting China’s foreign trade overall, and increasing its trade surplus. In fact, the United States became the third-ranked trading counterpart to China with a two-way trading volume of RMB 4.06 trillion ($628 billion—about 14 percent of China’s foreign trade) in 2020, behind the Association of Southeast Asian Nations and the EU, which were slightly ahead. However, each of the three blocs pales in comparison with China’s trading volume of RMB 9.3 trillion ($1.4 trillion) with the BRI participating countries. Overall, this represents a “politically correct” ranking of trading counterparts from China’s point of view.

More importantly, China has also wanted to improve the quality of its foreign trade in terms of raising the share of domestic

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value added in its exports—in other words, moving up the value chain in exports. This goal was flagged in the “Made in China 2025” plan launched in 2015 targeting ten critical sectors—aiming to raise the share of domestically produced key components from 40 percent in 2020 to 75 percent by the end of the plan. In general, China seems to have made good progress in its efforts to increase local content, having reduced the share of foreign value added in its exports by 3.5 percentage points during 2014-18 to around 15 percent currently, similar to the United States and below the global average. Furthermore, China has been able to increase the share of its own value added in the exports of third countries to around 30 percent, a bit less than the United States but ahead of Germany. This has helped China capture more value in international trade for its domestic economy, but has reduced its import demand for intermediate goods including from other emerging market and developing countries. This shift will create some headwind in the development pathways of these countries. To some observers, the “Made in China” campaign looks like import substitution, but it is smart import substitution in the sense that China does not just try to erect protectionist walls to shelter inferior producers at home—like India has done with its automobile industry—but strives to move up the value chain by capturing high-end value added for the domestic economy. In this context, China’s model going forward seems to be Germany as a producer and exporter of high-quality capital and consumer goods, instead of just being the world’s factory of mass consumer goods.

**DOMESTIC CIRCULATION**

Domestic circulation means relying more on domestic activities, especially private consumption, to drive the economy. Specifically, China aims to enhance domestic supply chains, promote indigenous innovations, and strengthen its “military-civil fusion” (MCF) strategy, all to increase and improve the quality of domestically driven growth. Improving domestic supply chains implies reducing China’s dependence on foreign imports, especially in critical areas such as food, energy, and advanced technologies. To enhance food security, China has diversified the sources of its imports away from the United States (despite commitments to purchase in the phase one deal) to other countries such as Brazil and Argentina. To lessen its need to import fossil fuels and address its serious air pollution problems, it has pushed forward in developing renewable and clean energy. At present, China is already leading the world in generating electricity using renewable energy sources, which account for 26 percent of its electricity generation compared with 17 percent in the United States, the second-ranked country.

Finally, decreasing reliance on foreign technologies is important to reduce the risk of foreign disruptions to China’s efforts to build out the infrastructure for a digital and high-tech economy—including for 5G connections and usage, AI, quantum computing, new energy, electric vehicles and charging stations, new materials, and digital commerce and e-payments, including the soon-to-be-launched digital yuan (called Digital Currency Electronic Payment, or DCEP). This goal will be buttressed by plans to promote indigenous innovation. Several long-term plans have been launched to mobilize resources—including the $1.4 trillion five-year digital infrastructure program—to invest in advanced technologies. Equally important for this high-tech push is the promulgation of the “China Standards 2035” plan to develop technological standards and wage a coordinated campaign to get them adopted as global standards by international standard-setting bodies. This would facilitate the development of Chinese technologies and help Chinese high-tech companies compete for leading positions in international markets. Underpinning all these steps is the fact that China’s R&D expenditures have risen significantly in the past decade to around 2.2 percent of GDP, or $468 billion in absolute terms, second only to the United States at 2.8 percent of GDP, or $582 billion—and China aims to close the gap in the foreseeable future.

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Furthermore, since the new technologies are amenable to dual uses, China will try to better implement its MCF policy to promote the sharing of technologies and talents between the military and civilian sectors, thus stimulating both economic development and military modernization.\(^\text{49}\) Reflecting the importance of this initiative, the Communist Party of China (CPC) has established a national Military-Civil Fusion Commission, chaired by President Xi Jinping himself. More concretely, since 2015, about thirty-five investment funds totaling $68.5 billion have been launched to invest in MCF-related companies.\(^\text{50}\) Some observers have viewed China’s MCF policy as an attempt to imitate the successful US defense production ecosystem built around the collaboration between the Defense Advanced Research Projects Agency, private companies, universities, and research institutions—which has been responsible for transformative innovations with widespread commercial applications such as integrated circuits, the Global Positioning System (GPS), and the internet. Nevertheless, China’s MCF policy has triggered US efforts to better control the export of military and dual-use technologies and products.

**CORPORATE REFORM WITH CHINESE CHARACTERISTICS**

Underpinning the domestic circulation element is the ongoing emphasis on corporate reform—not to become more like companies in the West but to make state-owned enterprises “stronger, bigger and better” with the goal of becoming more productive.\(^\text{51}\) Indeed, Xi has taken this concept of reform further, by ushering in a new development paradigm—featuring enhanced “blending of the public and the private, market and planning,” for example, by integrating CPC cells in public and private firms and shifting the exercise of public ownership of companies from “managing enterprises” to “managing capital” through a series of government guidance investment funds.\(^\text{52}\) Experiences show that China’s state capitalism is good at mobilizing vast resources to build infrastructure, but it is too early to say if Xi’s doubling down on that model can deal with the enormous complexity and required timely responsiveness inherent in steering a modern economy.

More generally though, it is important to realize that it is simplistic and misleading to view Xi’s centralization of power as a reversal of his predecessors’ emphasis on pro-market reforms, in the way many observers in the West have interpreted it. In that narrative, those reforms were responsible for China’s phenomenal growth over the past four decades, while Xi’s policies represent a backward move to the Marxist-Leninist control and central planning of the past, thus dooming the country to poor economic performance, if not failure. The reality is that the CPC from Deng Xiaoping to Xi Jinping has always used the same playbook: build a “socialist market economy” with political control where necessary, and market mechanism where useful.\(^\text{53}\) This is something that the former Soviet Union never got the hang of, but China has implemented the strategy pretty well so far. The only difference among successive Chinese leaders has been in terms of degree, or where precisely the line has been drawn between the “necessary” and the “useful.” Clearly Xi Jinping has moved the needle toward more political control, which has been made more pervasive and effective by the digital revolution (beyond the dreams of Mao Tse-tung), but market mechanism is still being maintained—most conspicuously in the market for high-tech venture capital funding, as pointed out by well-known venture capitalist Lee Kai Fu. According to Lee, China has caught up with the United States in AI thanks to its ability to harvest big data and maintain “an entrepreneur ecosystem.”\(^\text{54}\)

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III. CONCLUSION AND OUTLOOK

On balance, Biden’s prioritized emphasis on making investments in physical and human infrastructure (including affordable healthcare for all citizens, education reforms, and vocational training that can effectively prepare most workers who do not have a college degree for the jobs of the future) is the right approach to deal with the various crises facing the United States. However, this is a defensive posture as the country struggles to repair the damages done to its economy and society by the combination of globalization, technological changes, the Covid-19 pandemic, and years of inadequate public investment in infrastructure. Moreover, given the rampant partisanship exhibited in the US Congress, it will take time for any remedial programs to get enacted, and even longer for those programs to bear fruit. During this period, the United States will be inward-looking and likely not be in a position to mobilize popular enthusiasm and resources for any grand international gestures—for example, offering developing countries a more than $60 billion credit limit from the recently reconstituted US International Development Finance Corporation to compete with the promises of China’s Belt and Road Initiative, which has invested about $575 billion in participating countries with more to come.55

In comparison, China’s dual circulation strategy is based on past progress, but entails significant implementation risks given its ambitious goals. It aspires to prepare China for the digital and high-tech economy, reducing its vulnerability to foreign pressures by trying to reshape the modality of international interactions to suit and benefit its endeavors. It will aim to do this by consolidating and enhancing its influences in existing international organizations such as the United Nations and its affiliated organizations, such as the WTO and World Health Organization, as well as developing new international institutions where it plays the key role, such as the Asian Infrastructure Investment Bank, the BRI Forum, and the Forum on China-Africa Cooperation. This will have a substantial impact

on the course of international relations in the years to come, including by inciting pushback from other major countries.

Generally speaking, the chosen strategies seem appropriate for the challenges and circumstances each country finds itself in, seen from the perspective of each. The economies of the United States and China will recover in the year ahead, outperforming other major countries over 2020-2021 according to the IMF, but owing to different reasons: massive fiscal stimulus in the United States and early control of Covid-19 and resumption of almost normal economic activities in China.\(^56\) This is a window of opportunity for the two countries to roll out their respective strategies. However, it remains to be seen how well they will implement them in an environment filled with tension and downside risks. The progress (or lack thereof) in implementation will determine whether they can succeed in tackling the challenges facing them. Interestingly enough, several of the challenges are common to both: aging populations and declines in labor force growth (with China’s demographics deteriorating at a faster pace than those in the United States), high levels of indebtedness (with high and rising public debt relative to GDP in the United States and corporate debt in China), sustained declines in productivity growth (albeit from a higher level in China), and widening inequality in income and wealth distribution (the Gini coefficient of income distribution in China is 0.465, not far off from 0.48 for the United States).\(^57\)

While the jury is still out on the effectiveness of either strategy, one thing is already clear: The difficult tasks of the United States and China have been made much more so by the bifurcation of the global economy into two competing ecosystems, driven by the mutually reinforcing effects of their strategies—selective decoupling/reshoring and dual circulation. As the division deepens, the global economy will incur increasing costs of doing business and become less efficient. Its potential growth rate risks falling below the World Bank’s estimate—made after the Covid-19 pandemic began—of 1.7 percent for the next ten years, a downgrading of its estimate of 2.4 percent made in 2019.\(^58\) Slowing growth is quite harmful in that it exacerbates the challenges facing many countries, making it more difficult to find solutions to them—particularly for low-income developing countries. The costs of strategic competition and the resulting division are already here and will continue to increase going forward.

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