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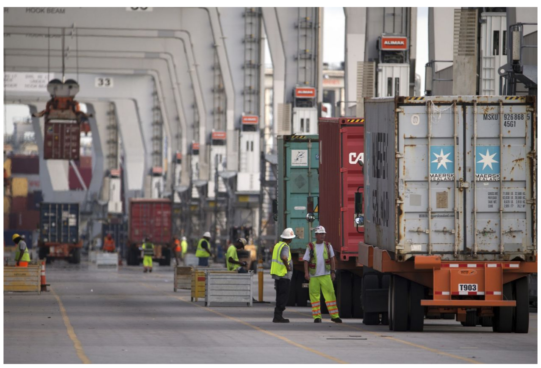
CHINA

U.S. Pivots to China, With Nafta Deal in Hand

White House officials say a strong North American trade deal gives them an advantage in talks with Beijing



Dockworkers at the Port of Savannah in Georgia. Trump administration officials are hopeful that trade volumes will rise.
PHOTO: STEPHEN B. MORTON/ASSOCIATED PRESS

By Bob Davis
Oct. 1, 2018 6:00 p.m. ET

WASHINGTON—White House officials are betting that concluding a trade deal with Mexico and Canada will give them more ammunition in their high-stakes battle with China on economic issues and national security.

A renegotiated North American Free Trade Agreement, Trump advisers argue, removes the possibility that a trade war could break out on the continent and will make North America a more attractive place for investment.

When combined with U.S. tariffs against China, which boost the costs of production there, foreign companies will start moving investment out of China, the administration calculates. That would weaken China's ability to produce next-generation technology and put additional pressure on Beijing to make trade concessions sought by the U.S.

The U.S. will "reclaim a supply chain that has been off-shored to the world," President Trump said at a press conference Monday.

Former White House strategist Steven Bannon said the Trump strategy from the outset was to pull investment out of China and remake global supply chains, but then the effort got thrown off track when administration deputies battled over steel and other trade issues and the U.S. launched fights with Europe, Canada and other allies.

"Nafta was the key to pick the lock on the global supply chain," he said.

Some big technology companies have said privately that they have begun weighing whether to shift some production out of China to avoid U.S. tariffs.

What's in the New Nafta

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Josh Kallmer, senior vice president at the Information Technology Industry Council, a trade group representing high tech companies, said that parts of the new Nafta, called the U.S.-Mexico-Canada-Agreement, would appeal to tech firms, particularly provisions which liberalize digital trade in North America and encourage services trade.

"That could accelerate their thinking that maybe they should shift production of some widgets to Mexico," he said.

In addition to the new Nafta, the U.S. has started trade talks with the European Union and Japan. That puts aside—at least for now—most of the Trump trade fights with traditional allies and makes it easier for the White House to recruit partners to confront Beijing on issues including intellectual property protection to subsidized competition from Chinese state-owned firms.

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One provision of the new Nafta says that if any of the nations conclude a free trade deal with a "nonmarket economy"—meaning China—the others can pull out of the North American pact.

Currently the U.S. has placed levies on about $250 billion of Chinese goods, roughly half of their imports to the U.S. Mr. Trump made clear at the press conference that he continues to consider tariffs as an important part of the U.S. trade arsenal.

The administration has said before that it was getting the upper hand in U.S.-China talks because the American economy was humming as China's slows. But that hasn't stopped Beijing from retaliating against the U.S. with tariffs, or on canceling negotiating sessions in response to U.S. pressure. The Trump administration strategy also risks igniting a nationalist, anti-U. S. reaction among ordinary Chinese—or one fanned by the government.

Cornell University China scholar Eswar Prasad warned that if the U.S. expands its tariffs, "then China would disengage and probably start implementing its playbook of making life miserable for American businesses" in China, he said. "They have been restrained so far."

The U.S. has been meeting regularly with European Union and Japanese trade officials to work out a common strategy to deal with China. While the talks haven't yet produced a uniform strategy, they are meant to signal to Beijing that it would be difficult to divide its three major trading partners.

"We're sending China a message," said National Economic Council Director Larry Kudlow to reporters. "They're not going to break up the allies." Mr. Kudlow also said on Fox Business Network that Mr. Trump may meet with Chinese leader Xi Jinping at the Group-of-20 leaders summit in Buenos Aires at the end of November.

Some provisions of the new Nafta give a sense of what the U.S. would want out of trade deals with China or other nations. For instance, the three nations agreed to "avoid manipulating exchanges rates or the international monetary system." Disagreements would be referred to a dispute resolution panel and could lead to tariffs.

The economic struggle between the U.S. and China has spread to other areas. Later this week, Vice President Pence is expected to make a speech highlighting what the U.S. claims are Chinese efforts to meddle in U.S. politics and the coming election. Over this past weekend, a U.S. Navy warship sailed near at least two Chinese-held outposts in the Spratly island chain the South

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China Sea, challenging Beijing's claims there. Meanwhile security talks between the U.S. secretary of defense and his Chinese counterpart, expected this month, have been canceled.

Hudson Institute China scholar Michael Pillsbury, who consults regularly with the White House, compared the Trump strategy to the Chinese game of Weichi, better known as Go, where the goal is to surround the opponent. "There's a peculiar Chinese sense that when you're being encircled, it's time to settle," Mr. Pillsbury said.

Currently, there are no formal negotiations under way with China. At a press conference, Mr. Trump said the time wasn't ripe for talks and once again threatened to put tariffs on the remainder of Chinese imports into the U.S.

Intermediaries continue to try to get talks going between the two nations. An effort involving Blackstone Group LP chief executive Stephen Schwarzman flopped last month after the U.S. announced its latest round of tariffs.

Mr. Pillsbury, the China scholar who Mr. Trump has touted as "the leading authority on China," has been meeting with Wang Huiyao, the president of the Center for China and Globalization, a Beijing think tank, who is seen as close to China's ruling Communist party.

At a recent Hudson Institute conference, Mr. Wang announced a set of recommendations to end the trade fight including firm commitments for China to purchase an additional $70 billion in U.S. goods, encourage Chinese consumers to buy more U.S. goods online and allow foreign companies a role in China's big technology development effort, called "Made in China 2025."

Mr. Wang's proposal was "constructive, but woefully inadequate," said Mr. Pillsbury, who says he relayed to the White House the parts that he thought could make a difference.

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