AGGREGATE COSTS Fact Sheet

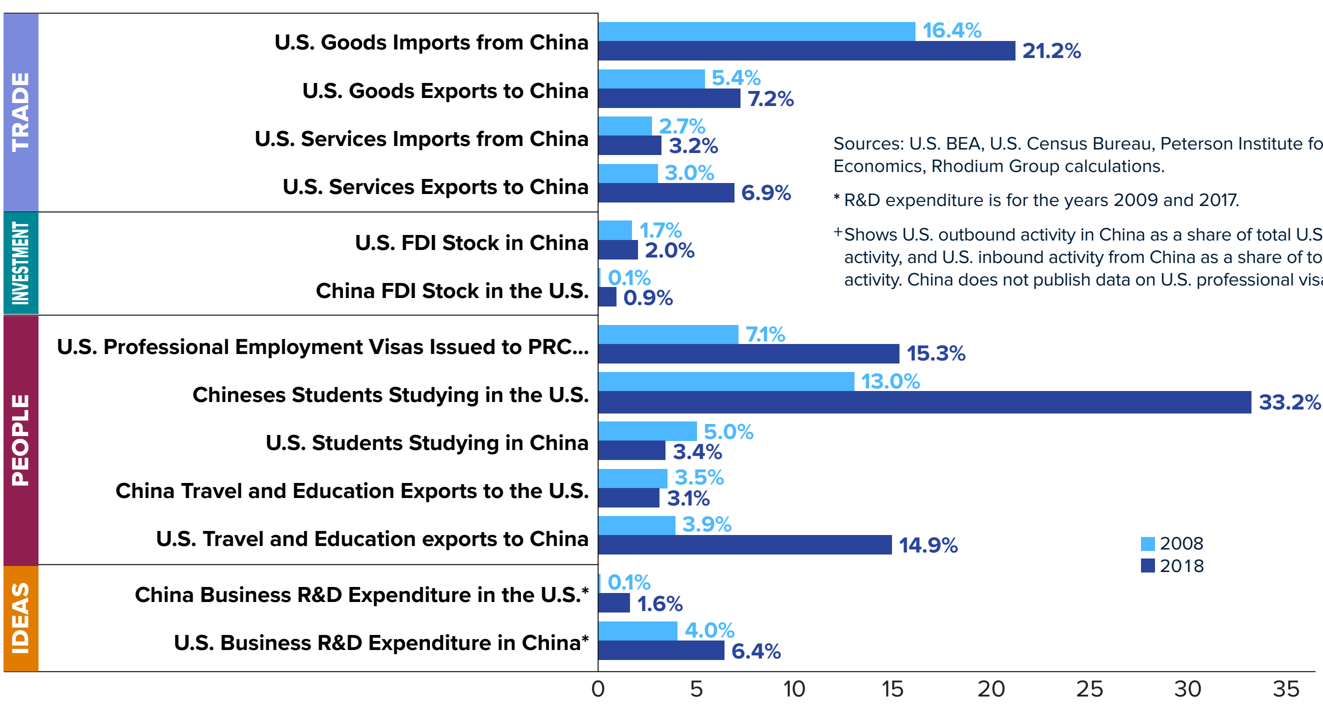
Competition between the U.S. and China in advanced technology is intensifying. At the same time, economic and national security concerns are becoming more intertwined as China's rise raises alarm bells in Washington and U.S. policymakers respond to years of Chinese protectionism. Against this backdrop, the deeply integrated economies of the U.S. and China are showing signs of coming apart as policymakers in both countries advocate for barriers to the flow of goods and services, capital, people, and ideas between the two markets. While there are real and legitimate reasons for the two countries to consider changes to their relationship, it is necessary to understand the costs of the world's two largest economies systematically closing off economic engagement—in a word, *decoupling*.

BACKGROUND AND BILATERAL TRENDS

In recent decades, U.S.-China economic engagement has expanded drastically and appeared set for further integration.

- In 2018, the U.S. and China traded $737 billion in goods and services, and the cumulative value of two-way direct investment since 1990 surpassed $386 billion. R&D cooperation was increasing, and China was the largest source of international students in the United States.
- The U.S.' $21 trillion economy (2018) and China's $15 trillion economy (2018) were becoming more integrated across main channels of engagement, with potential for further growth.

U.S.-China Engagement in Four Channels as a Share of Total U.S. Activity+



Sources: U.S. BEA, U.S. Census Bureau, Peterson Institute for International Economics, Rhodium Group calculations.

* R&D expenditure is for the years 2009 and 2017.

+Shows U.S. outbound activity in China as a share of total U.S. outbound activity, and U.S. inbound activity from China as a share of total U.S. inbound activity. China does not publish data on U.S. professional visas issued.

THE COSTS OF DECOUPLING

Decoupling risks a complete rupture in the economic relationship. Policymakers need a better picture of the costs of decoupling to determine the optimal path forward. We consider costs across four channels of activity: trade, investment, ideas, and people. This is not comprehensive of the bilateral economic relationship but covers the major elements.

Decoupling Aggregate Costs

Estimated costs of decoupling across four channels of engagement reveal significant costs that should be considered in pursuing economic decoupling policies.*

TRADE	INVESTMENT	PEOPLE	IDEAS
$190 billion annually by 2025 in forgone U.S. GDP if 25% tariffs are placed on all two-way trade.	**$25 billion** annually in lost capital gains and one-time GDP losses of up to $500 billion if U.S. companies reduce cumulative FDI in China by 50%	**$30 billion** annual loss to U.S. services trade exports if Chinese students and tourists coming to the U.S. drop by 100%	**Billions** in reduced R&D spending in the U.S.; diminished access to Chinese talent and science; and greater competition with China for global innovators.

*Estimates are not comprehensive, not adjusted to the same base year, nor compatible with each other. See full report for details.

It is clear from these estimations that the costs of a hard (partial) decoupling scenario could amount to hundreds of billions of dollars annually, while a full decoupling scenario (engagement plummeting to zero) would be even more costly. Other long-term costs to the U.S. are more difficult to quantify but include the following:

- Loss of competitive advantage: As U.S. firms lose market share to firms from other nations that remain engaged with China, those firms will increase their economies of scale and scope at the expense of U.S. firms.
- Loss of power to set global standards: As decoupling policies reduce economies of scale, U.S. companies will lose the ability to set global standards on everything from energy and technology to health care and transportation.
- Supply chain replacement costs: As U.S. companies are forced to shift supply chains out of China, they will incur substantial capital costs and face reduced efficiency.
- Loss of international trust: As the U.S. erects barriers to economic engagement with China, third countries will view U.S. firms as less reliable partners.

EVOLUTION OF DECOUPLING POLICIES

Over the past five years, U.S. policymakers have begun responding to Beijing's industrial policies that create barriers to bilateral economic engagement and disadvantage U.S. businesses.

China's Drivers and Policies: China's drive for indigenous innovation dates back more than a decade, as Beijing has deployed a mix of market access limits, industrial policies, and regulatory restrictions to support the competitive position of domestic companies and reduce dependence on foreign technology and expertise. The U.S. Chamber of Commerce has closely tracked emerging decoupling policies from China over the years, including the following:

- **The National Medium- and Long-Term Plan for the Development of Science and Technology (2006-2020)**, which mandates localization of ICT
- **An Anti-Monopoly Law regime** that prioritizes industrial policy over competition law
- **A foreign direct investment regime** that is the most restrictive of all G20 economies
- **The Made in China 2025 plan (2015)**, which intensifies Beijing's state-led approach, defines market share targets for Chinese companies in 10 strategic sectors, and details preferential treatment for Chinese companies
- **A restrictive data governance regime** that protects local companies, enhances state control, and subsidizes national champions

United States' Drivers and Policies: Policymakers in the U.S. have grown increasingly concerned that China's state-led, protectionist policies are exploiting the openness of the U.S. system in order to foster Chinese companies and technologies that will ultimately overtake their U.S. competitors. The economic concerns are accompanied by concerns about national security, values, and China's increasingly aggressive geopolitical posture. In large part as a response to China's increasingly illiberal tendencies, the U.S., starting during the second Obama administration and intensifying during the Trump administration, undertook several defensive measures. A sample of U.S. decoupling policies includes:

- **The Export Control Reform Act (2018)**, which broadens export restrictions on *emerging* and *foundational* technologies, restrictive rule changes to the Export Administration Regulations (e.g., Foreign Direct Product Rule, Military End User Rule), and the addition of hundreds of Chinese companies to the Department of Commerce Bureau of Industry and Security's Entity List
- **Reforms to the Committee on Foreign Investment in the United States** that strengthen the review process for inbound investments deemed harmful to national interests
- **Section 301 tariffs** that cover more than two-thirds of the value of bilateral trade
- **A presidential proclamation restricting Chinese researchers** with ties to the Chinese military from studying certain fields in the U.S. at the graduate level and above
- **Proposals to restrict capital flows** between the U.S. and China, including the cancellation of plans for federal retirement funds to invest in funds that include Chinese equities
- **A prohibition on the federal acquisition of telecom equipment** from five Chinese suppliers
- **Executive Orders addressing China-related supply chain vulnerabilities** in rare earths, pharmaceuticals, medical devices, and the bulk power system, and congressional proposals to reduce dependence on China for a range of products