IFANSFOCUS
Institute of Foreign Affairs and National Security
IF2020-35E
April, 2021

China's "Dual Circulation" amid U.S.-China Strategic Competition: Overview and Implications

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In 2020, China unveiled its "dual circulation" economic strategy, a shift brought on by a deepening strategic rivalry with the United States that began in earnest after the 2018 U.S.-China trade conflict. It was the widening trade deficit with China that sparked the trade rift between the two sides, but Washington has begun questioning the way China practices state capitalism. For instance, America has accused China of continuing a state-backed campaign of intellectual property theft including the use of forced technology transfer and providing subsidies to Chinese state-owned enterprises (SOEs). China under President Xi Jinping has put aside serious market reform and made efforts to strengthen its SOEs to further embrace state capitalism. This development was far from what the U.S. had expected when China joined the WTO and gained access to world markets. Washington believed that China's accession to the WTO would make the country's economic system market-friendly, but Beijing went in the opposite direction. Politically, China took sharp turns toward hard authoritarianism, a move that eventually led to conflicts between the two great powers. The Trump administration, based on the belief that the WTO system is not sufficient enough rein in China's state capitalism, took a go-it-alone approach to pressure China and deepened the U.S.-China trade rift. The administration demanded China be fair on trade; it asked Beijing to drift away from state capitalism and drop its mercantilist economic model centered on SOEs. Yet, the Trump administration failed to get the desired response from China, and U.S.-China economic relations have been on a downward spiral ever since. The two sides are undergoing economic "decoupling" as a result. Owing to this growing rift between the two great powers, globalization as well as China-centered global value chains (GVCs) which produce products that enter the U.S. market are facing challenges.

And as the U.S.-China conflict has expanded beyond trade and morphed into strategic rivalry, technological competition between the two countries is intensifying, especially in cutting-edge sectors like 5G, artificial intelligence (AI), and advanced semiconductors for dual-use - both military and civilian purposes. The U.S. has focused on channeling efforts to pressure and keep China in check in these sectors. Washington regrets its past interdependent relationship with China, which has eventually locked itself in a strategic competition with Beijing. It is therefore pushing for financial and institutional decoupling, especially in the cutting-edge sector. It is hard to say that China's recent technological advancement was made possible only through illegal practices, such as forced technology transfer or theft. It is in a way attributable to China's open-door policy; the country would not have been able to make advancements in cutting-edge technology by relying solely on significant R&D investment without the exchange of advanced technologies with the outside world. This explains why the U.S. is ramping up efforts to thoroughly decouple from China to maintain its lead in the technology race amid growing rivalry with China.

With the U.S. heading toward decoupling, China has pushed for "internal circulation" (the domestic cycle of production, distribution, and consumption) as the country's new growth engine, and linked it up with external markets to create the abovementioned "dual circulation" strategy. Hence, the crux of China's dual circulation is about how to successfully spur its domestic demand. As a country's domestic demand consists of investment and consumption, attention is drawn to whether China's dual circulation strategy can lift its economy by rebalancing it from investment-led growth to consumption. Giving a boost to consumption can increase imports, and under such a scenario, the U.S. trade deficit with China can be reduced, which will in turn ease tensions between the two sides. Consumption, however, has made up only a small portion of the Chinese economy, and the country's economic resources have been channeled into helping Chinese companies increase their investment as the Chinese government has pursued investment-driven economic growth. Accordingly, China's push for a consumption-driven economy could be a politically sensitive decision, as it would hurt entrenched vested interests that have become powerful under Xi Jinping's presidency with the rise of state capitalism – which favors SOEs. This explains why it is not easy for China to rely more on consumption rather than an investment to spur its domestic demand.

The Chinese government suggested that China's investment in 2020 would focus on "New Infrastructure," "New Urbanization," and conventional gigantic infrastructure construction ( ). China looks set to focus the country's investment on existing massive infrastructure programs as well as on building up innovative infrastructure to prepare for the fourth industrial revolution. China sees the acquisition of cutting-edge technologies as a key to successful new infrastructure projects and sustainable economic development. The problem is that America's decoupling moves have made it difficult for China to gain access to advanced technologies, putting Beijing in a difficult position. In the face of the U.S. decoupling campaign, China intends to establish its industrial supply chain to form an economic system that can operate with as little external impact as possible to the Chinese economy. Taken together, China's "dual circulation" is a strategy aimed at establishing an industrial supply chain that allows the country to operate new industries backed by state capitalism, as part of an effort to navigate U.S. efforts to decouple from China. To this end, China has tried to spur domestic demand by increasing investment in technological innovation. The country also has unveiled new action plans to open up its financial markets to attract foreign investment, given its promise to step up global financial integration under its dual circulation" strategy. This plan is part of an effort to manage risks stemming from America's broad-scale decoupling efforts.

A shift in focus toward investing in new infrastructure projects targeted at cutting-edge technologies from investing in traditional huge infrastructure projects and real estate development could be viewed as a positive development. But this shift does not mean the country is transitioning toward more consumption-driven growth, so it will show limited effect addressing both internal and external imbalance of the Chinese economy. China's attempts to spur domestic demand under its "dual circulation," therefore, are hardly likely to address the U.S.-China trade deficit. After all, "dual circulation" reflects China's apparent political determination to maintain its state capitalism even in the face of growing decoupling pressure, rather than to compromise with the United States, suggesting that the pace of the U.S.-China decoupling could accelerate in the coming years. This will disrupt Korea's close economic relationship with China that Seoul was able to maintain when the level of economic interdependence between Washington and Beijing remained high. Hence, Beijing's push for "dual circulation" indicates that Korea's strategy of "strengthening alliance with the U.S. while deepening economic cooperation with China (安美经中)" is no longer a viable option. The U.S.-China relationship is currently precarious, and the strategic competition between the two sides is intensifying. Against this backdrop, Korea must contemplate ways to advance its national interest to navigate its path forward.

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