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U.S.-China Relations and its Impact  
on National Security and Intelligence in a Post-COVID World

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## U.S.-China Relations and its Impact on National Security and Intelligence in a Post-COVID World

Chairman Schiff, Ranking Member Nunes, and distinguished members of the House Permanent Select Committee on Intelligence, thank you for the invitation to speak on U.S.-China relations in the context of the coronavirus pandemic, how other nations are being impacted, and their likely response.

Specifically, my opening remarks will focus on the shifting economic and trade landscape in the post-COVID world, its impact on other nations and their response to the U.S. and China, and what steps the United States should take to safeguard its interests, drawing from our strengths of open economic and political systems. It is my hope that these comments will be useful in the context of the Committee's deliberations on U.S. national security decision-making, and to the Intelligence Community's many contributions to that decision-making more broadly.

### I. Impact of COVID-19 on the economic and trade landscape

The pandemic is *accelerating* structural trends that have been in play notably since the 2008 Global Financial Crisis, and it is having a deleterious effect on economies. These trends include:

- Rising inequality, notably in developed market economies, which is contributing to increasing populism and nationalism;
- An uptick in protectionism, including by G20 economies, which is increasing costs of trade to companies and developing market economies; and
- An erosion of multilateralism, which is causing countries to pursue regional or bilateral trade agreements and forego pursuit of global macro convergence in trade and investment policy.
- The pandemic-induced hard shift to the digital economy is also leading companies to automate faster, creating significant technological displacement that threatens to leave a much larger chunk of the workforce behind in both developed and emerging market economies.

All of this is happening against the backdrop of a pandemic that is deepening economic dislocation within and between countries. Absent a vaccine that is produced and globally distributed, market economies are at risk of stop-start-stop-start openings that will act as a persistent drag on growth and commercial activity. Eurasia Group analysts anticipate a global recession to persist into 2021 along with negative global growth (-2 to -7% for all of 2020).<sup>i</sup> While economies will come back in stages, it will take two to three years for economic activity to return to pre-crisis levels.<sup>ii</sup>

The pandemic is having a downward effect on both developing and emerging market economies, but it is the emerging markets—which are core sources of growth for the global economy and for U.S. companies—that are the more vulnerable by far. Emerging markets tend to have weaker

political capacity to get ahead of virus spread. They also tend to have more limited fiscal or monetary resources to cushion economies from pandemic shocks. They are far more reliant on trade for growth. The period 2020-2021 will see companies swiftly repattern and shorten trade flows in the face of persistent uncertainty with plant disruptions and border closures. Emerging markets that experience persistent challenges gaining control over their outbreaks during this period will struggle. They will find themselves outside of newly formed supply chains. This will lead to deepening economic dislocations over the medium term.<sup>iii</sup>

The economic and trade landscape will be different six months from now, and rapid change will remain constant until a vaccine is globally distributed. The one thing we know for certain is that there will be much more socioeconomic inequality due to the pandemic. This will place unprecedented stress on country governments to provide for their populations at a time when they will be fiscally constrained by low- or negative growth, slowing investment, and disrupted trade.

In the developed world, much of the inequality will come on the back of those that are not part of the knowledge economy—workers who are most easily displaced by technology and automation. In the developing world, the increase in inequality will be the result of the globalization slowdown – just-in-time supply chains being shortened and rerouted, leading to higher unemployment within the global middle class.

## II. Impact of COVID-19 on other nations and their response to the U.S. and China

In this context, country governments will prioritize economic security and resiliency to recover their economies and to rebuild their COVID-hit societies. Economic security will be the new national security over the next several years. It will drive national decisions about how countries relate to the United States and China. Recognizing this imperative will be critical to correctly assessing a country's interests in its relationship with both major powers.

This context is important because it suggests that our national security lens should be adjusted to place greater emphasis on economic factors—of trade, commerce, investment, infrastructure, and autonomy to pursue national interests without facing economic coercion—when assessing relative levels of influence. The United States has much to offer and I would argue a better deal to offer other countries in almost all of these categories, save infrastructure. Yet the U.S. continues to emphasize national security arguments to countries fighting for economic security. That disconnect risks the United States failing to capitalize on its strengths.

This is not to say that, for example, Association of Southeast Asian Nations (ASEAN) leaders are not concerned about freedom of navigation in the South China Sea and China's more aggressive behavior there. A greater emphasis on the imperative of economic security, however, will focus U.S. policymakers on what is of more immediate concern to government decisionmakers: bringing prosperity and opportunity to their people. What keeps most ASEAN leaders up at night is how to meet the rising needs and expectations of the world's largest

emerging middle class at a time when the pandemic is undercutting governments' ability to deliver. These leaders are struggling to restore to the region's 350 million workers the livelihoods being hit by the pandemic, disrupted trade, negative growth, or all three.<sup>iv</sup> They face the risk of pandemic-induced inequality and slower growth in the years ahead.

There will also be more inequality globally, for example, between those countries with the resources, strategic industries, and infrastructure critical to the 21<sup>st</sup> century post-COVID global economy, and those without. With rising levels of government intervention in industry, there will be an increasing divide between countries with robust technology sectors, advanced industries and systems, and those without. For those countries lucky enough to be in the "have" category, it will be ever more difficult to not pick sides so long as the U.S. and China continue to seek technology decoupling. For most countries in the "have not" category, they will seek to avoid choosing sides, but they will take from whatever power—the U.S., China, or other—that is willing to invest in their industries and infrastructure to bring them closer to being a "have".

A greater emphasis on economic power in U.S. national security strategy and assessments would lead decisionmakers to recognize the shortcomings of over-reliance on U.S. military power as a source of primary attraction when other national governments are consumed by economic recovery. It would lead decisionmakers to focus more on the formidable economic power of the United States and of the American promise of *opportunity* as our primary influence and attractiveness, particularly when that power is deployed for shared prosperity. It would lead decisionmakers to recognize that forcing countries to choose between the world's two largest economies is a false choice and one that is counterproductive to US interests and values. In our COVID-strained world, country governments want *freedom* and *agency* to recover their economy by any possible means; they will demand *choice* as they try to build pandemic resilience. Weakened markets that already have close ties to China will become more dependent, but they are not lost. They want choice, too. Ultimately, whichever major power becomes seen as the most effective partner in supporting a country government's imperative to deliver prosperity to its people without restraint will garner the greatest influence.

### III. Safeguarding U.S. interests in the post-COVID 19 world

The U.S. and China in years ahead will be the two strongest powers by far, measured in terms of the size of their economies, their global influence, and military power. But neither will be wholly dominant. Neither will be able to dictate the actions of the other or crowd the other out of international fora. The outcomes of the competition between these two powers will be heavily influenced by the actions and decisions of others, namely the European Union (as a far weaker third global power) and second tier powers, including Germany and France (individually), Japan, India, Brazil, Russia, Saudi Arabia, South Korea, Canada, Indonesia, and the U.K. The combined influence of these second tiers could tip the scales in favor of one power or the other, as we are currently seeing with Europe's emerging stance on 5G.

As such, the U.S. will be unable to secure its interests with regard to China by acting solely on its own.

Moreover, China's state-backed industrial policy will remain largely unchanged regardless of the tariffs imposed by the United States. American and European officials have become increasingly alarmed at the perceived success of China's state-backed model, and what it means for the long-term viability of the Western market-based model. Chinese officials are not surprised at the pushback on its model, which contrasts with Western norms of the "level playing field" for private enterprise. But for China, shoring up the legitimacy of state-backed model, which it believes sustains its political model, is an existential issue.

With the U.S. and China both set to be the leading powers emerging from the pandemic, and increasingly at odds with one another, we should expect much less international alignment on norms, standards, and policies relative to the Western market-oriented consensus of decades past. There is active debate on whether intensifying U.S.-China rivalry will result in new cold war blocs, spheres of influence, or just a more fragmented world. Even with these uncertainties, it reasonably can be forecast that global growth and innovation will decelerate the more that trade and investment policies become securitized and decoupling of high-technology and strategic sectors gains momentum.

A key definitional feature of competition in the 21<sup>st</sup> century world order therefore will be between the more open market-driven and state-directed economic systems. Other countries will seek to preserve access to – and benefits from – the United States and China. They will watch closely the performance of both major powers and draw lessons from each countries' relative successes. This is not the political ideology-driven cold war of the past, but rather a competition over which economic model delivers greater prosperity and more opportunity to more people in the years ahead. The COVID-19 pandemic is bringing this competition into sharp relief.

In our historical moment, power is indeed shifting to a country with different priorities, capabilities, and political and economic systems than those that led the post-World War 2 order. But the United States must recognize that this shift, which was happening before Covid-19, is neither absolute nor irreversible. The best way to strengthen the United States influence abroad is to strengthen the functioning of our model at home.

The relative success of the Western model of market-based capitalism will depend not upon a containment or isolation strategy of China; rather, our success will depend upon the extent to which the U.S. demonstrates the strength of its economic model in delivering broad-based prosperity and opportunity, both at home and abroad. The United States should have confidence in its model and invest in it. Rather than focus our energies on trying to change China, the U.S. should instead focus on domestic renewal with significant investments in R&D, education, healthcare, infrastructure, and readying our workforce to excel in a 21<sup>st</sup> century post-COVID American economy. We should do more to support U.S. companies competing for consumers in overseas markets, including the new middle classes in emerging market economies. Such

concentration on domestic renewal and external contest would shift the U.S. approach from trying to change China's model to viably competing with it.

The U.S. economic model is being challenged. American policymakers cannot build strategies on the assumption that other countries or companies will abandon China, even when they disagree with Beijing's economic or political behavior. Despite the risk of intellectual property theft, increased state intervention, and technology decoupling, global companies are not abandoning China.<sup>v</sup> Rather, they are working to find ways to make their products interoperable, effectively bridging the gap between China and U.S. and Western markets. The United States will likewise need to find new ways to compete but do so drawing from its strengths. The U.S. will need to demonstrate itself as the responsible actor, the party making it possible for countries and companies to pursue their interests without fear or favor, the country that champions protection of intellectual property, and the country that leads efforts to expand market access for broad-based prosperity. This is no small challenge. But it is what this moment demands.

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<sup>i</sup> Eurasia Group, "Revised global scenarios show later case peak, staggered recovery," 15 April 2020.

<sup>ii</sup> Eurasia Group in this assessment focuses on the roughly 30 politically or economically significant countries that cumulatively represent over 80 per cent of global GDP (please see appendix). Even among these countries, the return of their economies over the next two years could be uneven depending upon how effective the government working with society is in stopping the spread.

<sup>iii</sup> Eurasia Group, Geopolitical Risk Index, Outlook for Emerging Markets, June 2020.

<sup>iv</sup> See World Bank, International Labour Organization ILOSTAT database (March 2020): <https://data.worldbank.org/indicator/SL.TLF.TOTL.IN>

<sup>v</sup> See Center for Strategic and International Studies "Decoupling of Washington and Western Industry," 10 June 2020:

<https://www.csis.org/blogs/trustee-china-hand/decoupling-between-washington-and-western-industry>; American Chamber of Commerce 2020 Business Climate Survey, <https://www.amchamchina.org/policy-advocacy/business-climate-survey/>; and the European Chamber of Commerce "Business Confidence Survey 2020," <https://www.europeanchamber.com.cn/en/publications-business-confidence-survey>.