The Impact of China-US Trade Conflict on Foreign Investment in China

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Abstract. The trade war between China and the United States, as the two largest global economies, has had a profound impact on both countries. However, China, being a developing nation that has attracted significant interest from investment companies worldwide, has been particularly affected by this conflict. The trade war has presented numerous challenges for companies looking to invest in China, but there have been notable improvements in recent years. This study aims to delve into the examination of the influence of objective changes and subjective changes experienced by investors on the ultimate outcomes of their investments. By analyzing both the tangible and intangible factors affecting investment decisions and outcomes, a comprehensive understanding of the trade war's impact on investment in China can be gained. Objective changes refer to the concrete alterations in trade policies, tariffs, and regulations that have been implemented as a result of the trade war. These changes may include increased tariffs on certain products, revised import and export regulations, or modifications to investment laws. These objective changes can directly impact the costs, profitability, and feasibility of investments in China. On the other hand, subjective changes pertain to the perceptions, attitudes, and sentiments of investors toward investing in China amid the trade war. These subjective changes can be influenced by factors such as geopolitical tensions, market uncertainty, and the perceived risks associated with investing in a country engaged in a trade war.

Keywords: Trade war; tariffs; risks.

1. Introduction

Since the onset of 2018, China and the United States have initiated a fresh round of trade disputes, leading to a persistent state of trade friction between the two nations. Since the year 2018, the United States has implemented a series of tariff escalations on China with the aim of mitigating the trade deficit. [1] In response, China has reciprocated by imposing further tariffs on some American commodities. As per the information provided by U.S. Customs and Border Protection, the United States has implemented a 25% import tax on the initial group of 818 Chinese items, with a total value of $34 billion. This tariff went into effect at 00:01 local time on July 6, 2018 (equivalent to 12:01 Beijing time on July 6). In response, China reciprocated by implementing a 25 percent tariff on a comparable range of American goods on the same day. The ongoing issue of reciprocal sanctions between China and the United States persists, particularly in the industrial sector. The United States has imposed sanctions on Chinese steel companies, citing unfair competition due to steel imports from China. Additionally, the US government has implemented various measures such as Agricultural Trade Barriers, Digital Trade Barriers, Industrial Policies, and Technical Barriers. The United States government has implemented several measures such as Agricultural Trade Barriers, Digital Trade Barriers, Industrial Policies, and Technical Barriers to Trade in order to address the trade deficit with China. [2] Since the unilateral announcement of the results of the "301 investigation" by the United States on March 23, 2018, the economic and commercial relations between China and the United States have progressively approached a significant impasse. Since the unilateral announcement by the United States of the findings of the "301 investigation" on 23 March 2018, the economic and trade relations between China and the United States have progressively approached a significant state of stagnation. The Political Logic and Dilemma of the US Trade War with China in the Trump Era. The economic and trade tensions between China and the United States stem from a clash between their short-term and long-term interests. The United States has

progressively implemented comprehensive measures to impede China's economic growth, leading to an escalation of both trade and non-trade disputes. Consequently, these disputes have heightened the uncertainty and risk associated with China's economic and trade development. The accelerated process of China's integration into the global economy, coupled with its deepening involvement in the global value chain and the increasing integration of its capital market with the international community, may lead to an elevated risk of major conflicts between China and the United States within the global capital market. The escalation of major conflict events between China and the United States is likely to heighten the vulnerability of global capital markets. This is substantially harming foreign investment in China, according to the China Foreign Investment Report 2019 published by the Ministry of Commerce of the People's Republic of China revealed a 13 percent dip in global cross-border investment in 2018, the third consecutive year of decline But China's foreign investment absorption broke the trend with a 1.5 percent year-on-year growth. While this figure does appear to be an increase, according to the 2018 China Foreign Investment Report 2018 published by the Ministry of Commerce of the People's Republic of China, China had a year-on-year growth of 2 percent in 2017. There has been a notable decrease in the level of foreign investment attracted by China since the initiation of the US-China trade war in 2018. This finding demonstrates that the ongoing trade dispute between the United States and China has influenced the mindset of foreign corporate investment managers, leading to a decrease in their investments in China. This thesis examines the impact of the trade conflict between the United States and China on foreign investment from China's standpoint. Additionally, it explores the psychological factors that foreign investment managers may consider while making investment decisions and evaluating their correctness. This analysis offers potential assistance to investors in future instances of significant trade conflicts between the two countries. It aims to assess the impact of psychological activities on investors' decision-making processes, thereby aiding them in making informed choices. [3] By analyzing the total value of investments, the different types of investments available, and other aspects that are pertinent, the purpose of this article is to investigate the shifts that occurred in the amount of money that was invested in China by overseas investors while the United States and China were engaged in a trade war. To begin, people will provide an overview of the United States' imposition of sanctions on China, which have been in existence for a period of time totaling seventeen years as of this writing. After that, people will investigate how the implementation of China's retaliatory actions led to changes in the total value of a variety of China's industries, and people will compare these findings to the findings of previous studies. In the end, people will proceed to evaluate the probable repercussions of various policies on investors so that people may make an informed decision.

2. Type of Foreign Investment

Following the commencement of the trade dispute between the United States and China in 2018, there has been a notable decline in the influx of foreign investments into China, particularly within the primary industry where the fall in investment is most pronounced.

2.1. Primary Sector

In the agricultural, forestry, animal husbandry, and fishing sectors, there was a notable surge of 29 percent in the establishment of 579 newly formed foreign-invested firms, as compared to the previous year. [4] The utilization of foreign capital amounted to 790 million U.S. dollars, reflecting a decrease of 52.1% compared to the previous year. In the year 2018, there was a 10.4% increase in the establishment of 639 new foreign-invested firms in the agriculture, forestry, animal husbandry, and fishing industries. However, there was a 10.0% drop in the actual utilization of foreign capital, amounting to US$710 million [5].

2.2. Secondary Sector

In the year 2017, there was a notable increase of 24.3 percent in the establishment of new foreign-invested firms within the manufacturing sector, resulting in a total of 4,986 such enterprises. However, the actual utilization of foreign capital experienced a decline of 5.6 percent year-on-year, amounting to US$33.51 billion. In the year 2018, there was a notable increase of 23.4 percent in the establishment of new foreign-invested enterprises within the manufacturing sector, resulting in a total of 6,152 such enterprises. These newly established enterprises accounted for 10.2 percent of the overall number of new foreign-invested enterprises during that year. Additionally, the actual utilization of foreign investment in this sector experienced a significant growth of 22.9 percent, reaching a total of US$41.17 billion [6].

2.3. Tertiary Sector

In the year 2017, there was notable growth in the establishment of new foreign-invested firms in the service sector, with a 28.4% increase compared to the previous year. [7] Additionally, the utilization of foreign capital in this sector reached a total of 95.44 billion U.S. dollars, reflecting a 7.5% increase compared to the previous year. In the year 2018, there was a significant increase of 78.6% in the establishment of new foreign-invested enterprises in the service sector, resulting in a total of 53,696 such enterprises. These new enterprises accounted for 88.7% of the overall number of new foreign-invested enterprises during that year. However, the actual utilization of foreign capital in this sector experienced a decrease of 3.8% from the previous year, amounting to US$91.85 billion.

2.4. High-tech Industries

In the year 2017, China's high-tech service industry had a significant increase in the establishment of new foreign-invested firms, reaching a total of 5,990. This marked a substantial growth of 81.9 percent compared to the previous year. Furthermore, the actual utilization of foreign capital in this industry amounted to US$26.07 billion, reflecting a remarkable year-on-year increase of 106.4 percent. [8] The high-tech manufacturing industry had significant growth in 2018, as seen by the substantial increase in the number and size of foreign-invested firms. Specifically, there were 1,478 newly established enterprises, representing a year-on-year growth rate of 43.2%. Additionally, the actual utilization of foreign capital in this industry amounted to US$13.79 billion, reflecting a year-on-year increase of 39.4%. In the year 2023, President Biden enacted an additional legislative measure that imposed limitations on investments within China's technology sector.

3. Policy

Following the escalation of tensions between the United States and China in the trade war, China has implemented various measures to encourage increased foreign investment. These initiatives are aimed at promoting high-quality economic development and attracting overseas investors. One of the key steps taken by China is the facilitation of the growth of the service sector. The Chinese government recognizes the importance of the service industry in driving economic growth and has implemented policies to support its expansion. These policies include reducing restrictions on foreign investment in service sectors such as finance, healthcare, education, and entertainment. By opening up these sectors to foreign investors, China aims to attract more capital and expertise, stimulating innovation and productivity. Additionally, China has been actively promoting the "release of services" reform. This reform focuses on removing barriers and streamlining administrative procedures for foreign investors in sectors such as telecommunications, transportation, and professional services. By simplifying processes and reducing bureaucratic hurdles, China aims to create a more business-friendly environment that encourages foreign investment and fosters economic growth. Furthermore, China has implemented a range of diverse policies to attract foreign investment. These policies include providing financial incentives, tax breaks, and preferential treatment to foreign investors. China has also established numerous free trade zones and economic development zones,

offering special regulatory frameworks and preferential policies to attract foreign businesses. In contrast, the United States has taken a different approach by imposing tough restrictions on Chinese investment. One notable restriction is the ban on investments in China's semiconductor industry. This restriction aims to protect sensitive technology and intellectual property from potential threats posed by Chinese investors. The ban reflects the United States' concerns about national security and its desire to maintain a competitive edge in critical industries. Overall, while the United States has tightened restrictions on Chinese investment, China has responded by implementing measures to encourage increased foreign investment. By promoting the growth of the service sector, facilitating reforms, and implementing diverse policies, China aims to attract overseas investors, stimulate economic development, and enhance its global competitiveness.

3.1. China's Policy on Foreign Investment

Based on the State Council's emphasis on the active and efficient utilization of foreign investment to facilitate high-quality economic development, it is evident that the utilization of foreign investment is a fundamental aspect of China's national policy on openness and the establishment of a new open economic system. This indicates the continued significance of foreign investment for China. However, it is worth noting that China's policy towards foreign investment has recently undergone certain targeted adjustments in response to the current international context. To enhance the appeal of China as an investment destination for foreign investors, the Chinese government has implemented measures to loosen market access, increase investment liberalization, and gradually deepen the opening of the financial sector. The Chinese government has implemented measures to relax the regulatory constraints surrounding the construction of financial institutions supported by foreign entities. Additionally, the scope of operations for foreign-funded financial institutions in China has been enlarged, and the range of collaborative opportunities between Chinese and foreign financial markets has been widened. The objective is to enhance and refine the existing regulations pertaining to Qualified Foreign Institutional Investors (QFII) and Renminbi Qualified Foreign Institutional Investors (RQFII). This entails the establishment and enhancement of an open and transparent QFII system that is operationally convenient and entails controlled risks. The ultimate aim is to attract a greater influx of foreign long-term funds into the domestic capital market. In the case of foreign-invested firms with a cumulative investment below US$1 billion listed in the negative list of foreign investment access, the responsibility for approval and oversight is with the provincial governments. This can enhance the convenience of foreign investment and lessen the necessity of undergoing the approval process, hence augmenting the attractiveness of foreign investment. The implementation of public risk control measures can enhance the confidence of foreign investors in investment analysis by providing them with reliable data and reducing uncertainties associated with the TO segment. [8] The objective of this study is to explore strategies for minimizing logistical expenses incurred by foreign-invested firms. In the central and western areas, as well as the historic industrial bases in the northeast, there are plans to establish combined land and air open ports and multimodal transport hubs. Additionally, efforts will be made to expedite the advancement of intermodal transport systems such as river-sea, rail-air, and rail-water connections. Advocating for the expansion of both international and domestic routes and frequencies in the central and western areas, as well as the historic industrial bases located in the northeast. By adopting this approach, people may simultaneously facilitate the advancement of the Western region and encourage foreign investment, thereby mitigating the hindrances posed by suboptimal logistics efficiency and elevated transportation expenses for international entrepreneurs.

3.2. U.S. Policy Investment Policy

As of the 10th of August, Reuters reported that On Wednesday, President Joe Biden issued an executive order that would put restrictions on new investments made by the United States in China. These restrictions are intended to target particularly sensitive technologies, such as computer chips. In addition to that, the regulation stipulates that the government must be notified of any investments

made in any other technical industries. The United States government places a high priority on American companies expanding their operations overseas by investing in China. As a consequence of this, the imposition of constraints by the government of the United States has the potential to result in a significant reduction of commercial activity conducted by foreign companies within China. The bill targets high-profit industries like semiconductor manufacturing and other high-tech fields with the specific restrictions that it imposes on foreign investment from the United States. As a direct result of this, nearly fifty percent of China's investments in high-tech industries may be subject to limitations. The United States of America is making preparations to impose a revenue-based criterion in order to limit the scope of the investment restriction it has placed on China.

4. Psychological Activities of Foreign Investors

Foreign investors may encounter several psychological phenomena when engaging in investment activities, such as experiencing uncertainty and exercising caution, evaluating trade-offs between opportunities and risks, and expressing concerns on potential policy changes. The presence of doubt can be attributed to the prevailing sense of caution arising from the indeterminate nature of the future relationship between China and the United States. This uncertainty stems from the ambiguity around the potential for heightened conflict or the prospect of peaceful progress. The trade-off between opportunity and danger arises from China's remarkable economic growth, positioning it as one of the world's fastest-growing nations. [9] Consequently, foreign investors are drawn towards the undeniable allure of high returns on investment. However, it is important to acknowledge that the ongoing rivalry between the United States and China has contributed to an escalation in risk levels. Policy modifications can have a profound impact on the market, exemplified by the imposition of limitations on investments within a certain industry. Consequently, such constraints might result in investment failures attributable to the injection of capital that is not sustainable [10].

5. Conclusion

As the trade battle between the United States and China continued to escalate without abating, foreign investment in China experienced a decline in the two years after 2018. However, there are indications of a gradual easing of this trend now. The stringent limits imposed by the United States on corporations investing in China have had a significant impact on various sectors, including high-tech industries such as semiconductors. This has resulted in great harm to the profitability of investment companies. Indeed, investment firms are actively seeking strategies to navigate around the U.S. embargo, including the exploration of investment opportunities in Chinese enterprises as a means to access the high-tech industry supply chain. The mindset of investment managers and investors has a significant impact on a company's investment in China, particularly in light of the ongoing trade conflict between China and the United States. The policy uncertainty surrounding this conflict, coupled with the widespread dissemination of theories predicting the collapse of China's economy, has led some investors to adopt a pessimistic outlook on China's future economic development. Consequently, there has been a decrease in investment. However, it is important to note that such statements are currently misguided. Due to the implementation of COVID-19 lockdown measures, there has been a progressive decline in foreign investors' financial commitments in China. In conclusion, the subjective assessment and potential misjudgment of risk by investors can result in diminished investment returns. However, a cautious approach towards risk can assist investors in mitigating the possibility of investment failure. From an objective standpoint, investors should not solely concentrate on a specific country's government and news-related information. Instead, they should gather a broader spectrum of information and employ it for research purposes.

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