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After COVID-19: Reflections on the International Political Economy

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Abstract

This article makes three points about the post-COVID international political economy, the first of which is that the pandemic is far from over. Rather, it is moving into a completely different phase when developing countries, rather than advanced industrial states, will be its victims. The consequences include not only more severe public health risks, but also a wave of debt crises in both low-income and middle-income countries. The second point is that the pandemic is likely to generate ideational changes. Despite populist backlashes, publics will demand that governments develop the capabilities to protect them, not only from health shocks but from economic ones as well. State capacity will come to the fore. Finally, looking at the US-China relationship, we should not count on a snapback under a Biden administration. Although we can expect a shift toward more multilateral approaches to the Asia-Pacific, Democrats have their own reasons to limit risks from China; the trade war—broadly conceived—will continue even if on new turf.

Will the world look different in the aftermath of the COVID-19 pandemic? This contribution to the journal focuses on some of the implications of the crisis for the international political economy. First, it is important to note that as of this writing—in July 2020—the pandemic is actually not over; speculation

about a post-COVID world is premature. Indeed, the pandemic appears to have entered a new phase. I begin by considering the implications of the spread of the virus to developing countries including the possible reversal of the decades-long progress in world poverty reduction as well as the prospect of a succession of debt crises.

I next turn to the ideational effects of the crisis, and argue that COVID has demonstrated the risks of a laissez-faire approach to the state. The thinking about the relationship between states and markets is likely to shift, and unorthodox macroeconomic ideas as well as industrial policy are getting a political boost.

Finally, I turn to the US-China relationship, considering issues of both hard and soft power and the ongoing economic conflicts. As in the financial crisis of 2008-9, the difference in growth rates between China and the US will once again widen markedly, generating more anxiety in the US about the prospects of a power transition. With respect to image, neither China nor the US was shown in their best light by the pandemic. But the US is paying the higher price for its mistakes, which are extraordinarily difficult to cover up. Trump's mismanagement of the epidemic already appears to be costing the US in terms of its soft power appeal.

But no one should bank on the idea that a post-Trump world will snap back to normalcy between the two countries—whatever that means—or resolve the issues that have been exacerbated by the crisis. Focusing on the economic dimensions of the bilateral relationship, I show that the campaign against China is rooted in an important sea-change in US views of the country, a change which crosses the political aisle and engages Democrats as well as Republicans. A Biden administration will soften the edges of the Trump approach in important ways, most notably in a re-embrace of multilateralism. But it will look similar in important respects with respect to the need to reduce China risk through subtle steps toward decoupling.

The Pandis Global

It may sound like a cliché to say that pandemics are global, but COVID-19 spread in a way that has distorted our thinking about the scope of the challenges it poses. The virus had its origins in China, a country which for all practical purposes should be considered an advanced industrial state. China has a solid universal health care system and the underlying scientific resources to contribute to tackling the virus, including thorough testing and vaccine development. It then spread within East and Southeast Asia and to Europe. Again, most of the incidence in this phase was in advanced industrial states: the European countries, and Korea, Japan, Taiwan, and Singapore. Even the middle-income countries of Southeast Asia had relatively high per capita incomes.

Yet we are now seeing the spread of the virus elsewhere in the developing world. Daily global deaths peaked in mid-April, with over 90 percent at that point in the US and Western Europe. But after falling from that peak, global daily deaths started to increase again from around June 1, 2020. By July 1, fully 50 percent of new deaths were coming from Latin America alone. Although the disastrous response of Bolsonaro's Brazil grabbed headlines, Mexico, Peru, Chile, and other countries in the region were facing increased numbers as well. South Asia, the Middle East, and Africa were also starting to see rising case counts, bringing not only middle-income countries into the pandemic but low-income countries as well.

Any consideration of the risks in this next phase of the pandemic must consider both the unique public health challenges faced by emerging markets and developing countries, as well as the economic fallout.² As COVID-19 works its way down the world income ladder, it is striking countries with fundamentally different economic structures: greater levels of absolute poverty; a higher

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share of the workforce in the informal sector; a smaller share of jobs that can be done from home; and—in the world’s failed states—the problems of civil war, internally-displaced persons and refugees. Moreover, the most vulnerable countries and regions—sub-Saharan Africa, the poorer parts of South Asia, civil war cases such as Syria, Afghanistan, and Yemen—have health care systems that are much weaker than the countries the virus hit first.

Consider one strand of this complex of problems: the prevalence of informal sector employment in large, densely-populated cities. Even a country as well off as Singapore faced difficulties containing the spread of the virus in dormitories for Malaysian workers. We are now seeing the risks of spread in the large shanty towns in and around the major cities in Latin America, South Asia, and Africa where social distancing poses profound challenges. Moreover, informal sector workers have less to fall back on, and are more likely to return to the countryside to buffer their incomes. As a result, cities are seeding the virus to smaller cities and towns and rural areas. These, and other factors noted above, raise the risk of truly catastrophic spread.

Compounding the misery is the fact that these countries also face highly uncertain economic prospects. Moreover, these arise not only from the purely domestic effects of the crisis, but from the global contraction as well. The effects on global supply chains and commodity



exports are clear, and some countries are witnessing a virtual collapse in demand for crucial services, most notably in smaller tourism-dependent countries. But the problems are not only on the trade front: the crisis has affected remittance income and resulted in tightening credit conditions as well.

Looming debt problems and how to manage them provide one focal point for understanding the risks. Most emerging markets and even poorer developing countries went into the 2008-09 Global Financial Crisis with relatively modest levels of debt, partly a result of lessons learned from earlier crises. Over the last decade, however, low interest rates and greater access to financing contributed to a build-up in public debt in developing countries, with median public debt in developing countries rising from 35 to over fifty percent gross domestic product (GDP) of in the decade prior to the pandemic.³ As of this writing, more than 90 countries have approached the International Monetary Fund (IMF) in quest of support; this is clearly not a problem limited to low-income countries even if they are the most vulnerable.

It is one thing for China or the advanced industrial states to fail to coordinate among themselves; after all, they generally have the resources to address the problem,

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2. See Simeon Djankov and Ugo Panizza, *COVID-19 in Developing Countries*. London: Center for Economic Policy Research, 2020.
 3. United Nations Department of Economic and Social Affairs, “COVID-10 and Sovereign Debt.” *UN/DESA Policy Brief #72*, May 14, 2020 at <https://www.un.org/development/desa/dpad/publication/un-desa-policy-brief-72-covid-19-and-sovereign-debt/>.
 4. Homi Kharas, “What to Do About the Coming Debt Crisis in Developing Countries,” *The Brookings Institution*, April 13, 2020 at <https://www.brookings.edu/blog/future-development/2020/04/13/what-to-do-about-the-coming-debt-crisis-in-developing-countries/>.
 5. Francis Fukuyama, “The Pandemic and Political Order: It Takes a State,” *Foreign Affairs*, 99, 4 (July/August 2020): 26-33.



even if they do so more or less effectively. For developing countries, however, external assistance will have to play a larger role if the gains in poverty reduction over the last decades are to be maintained. In April, the IMF announced a raft of initiatives through existing and new facilities. It also promised to fully exploit its power to borrow, although with some doubts about whether even that borrowing power was adequate. Also in April, the G20 countries agreed to a debt service standstill from all official bilateral creditors, but the beneficiaries of this initiative were small and the standstill is only temporary. More will almost certainly need to be done as a string of debt crises begin to hit the international financial system.⁴

In sum, a more global view of the pandemic forces a number of shifts in our thinking about the crisis. First and most importantly, it is by no means over. It is too soon to even talk about a second wave when we have yet to see the full impact of the first one. Second, the spread of the virus to developing countries is likely to pose a more important test of the ability of the existing multilateral organizations to coordinate a joint response where needed. That they have sprung into action in a timely fashion is encouraging, suggesting that there is some capacity for existing organizations to lead even when their members are preoccupied. Yet the spiteful

decision on the part of the US to step away from the World Health Organization (WHO) is a reminder that the ability to coordinate through existing institutions ultimately depends on the commitments of the major powers.

Finally, the longer-term impact of the crisis on developing countries could be even more pronounced than in the advanced industrial states. Recent history has seen a remarkable reduction in world poverty and despite challenges in failed states, measured optimism about the ability to move towards the UN Sustainable Development Goals. This progress is now vulnerable, and at a time when multilateral cooperation has been most challenged.

New Ideas? Rethinking the State

In thinking through a post-COVID world, it is worth asking whether the crisis has generated any fundamental ideational changes: whether it has forced a rethink of existing public policy paradigms. The 2008-9 Global Financial Crisis resulted in a synchronized—if not necessarily coordinated—Keynesian response. Faced with an alarming shock, governments and central banks responded with flexibility. Yet this crisis is much deeper and will reopen debates about the appropriate relationship between states and markets, and the importance of state capacity in particular.⁵

The issue can be framed by looking briefly at South Korea's relative success in addressing the virus. We now know that responses to the virus not only need to be strong but timely; acting quickly is everything. The government responded rapidly in part because it had an adverse experience with MERS in 2012; during that pandemic, it was the most-seriously affected country outside the Middle East. As a result, however, South Korea changed a number of laws governing access to phone and credit card data for public health purposes.⁶ That data permitted the government to pursue a strategy

that focused on containment through extensive testing, quarantine, and invasive monitoring of the movement of cases, down to the individual patient. Avoiding the massive shutdowns in Europe, the US, and elsewhere, the government used highly targeted information campaigns to inform the public of the location of outbreaks, trusting citizens to use their own judgment in assessing risk.

The Blue House also quickly centralized crisis response but relying on input from the private sector and medical establishment. Within a week of the first case, the government had reached out to the local medical and pharmaceutical sector to incentivize development of testing; within two weeks, the country had an incipient testing capacity.

What comes out of this narrative bears an uncanny resemblance to organizational factors associated with the so-called “developmental state.”⁷ First, Korea showed the advantages of state capacity, including the innovative use of information technology. Second, the Korean response was by no means top-down, but sought meaningful engagement with—and incentives to—private sector actors around sharply defined goals, such as testing.

Finally, a striking outcome of the crisis among all of the advanced industrial states—including but not limited to Korea—has been the innovative use of government finance. Central banks were surprisingly aggressive during the Global Financial Crisis. The fundamental tools are now the same—quantitative easing through a variety of asset purchases—but have been pushed to new levels. The assets on the balance sheet of the US Federal Reserve, for example, increased by \$3 trillion from March

through the end of June 2020.

What has been equally, if not more surprising, however, is the unorthodox approach to fiscal policy that has emerged from the crisis. Governments have cut taxes and increased spending with abandon, while central banks have proved willing to absorb the resulting debt, further driving down interest rates. Although the US has distinctive advantages in pursuing this strategy—in the continued standing of the dollar and the depth of its capital markets—the US is not alone as other advanced industrial states and emerging markets have pushed deficits into uncharted terrain.

What lessons—if any—might be learned from these experiences? In 2009, the Tea Party Movement proved a surprisingly influential grassroots response to these Keynesian and industrial policy ideas in the US, focusing its ire on government bailouts of large firms, the expansion of health care, and efforts to offset mortgage losses. Such libertarian ideas might well resurface. Yet the apparent absence of inflation and the pressing demands to offset income losses are likely to raise a subversive question. Why should not a strengthened state, working with the private sector and seeded by strong government finance, be “thinking big” and focusing not only crisis response to a pandemic, but on infrastructure, broader health care needs, or a Green New Deal?



6. Brian Kim “Lessons for America: How South Korean Authorities Used Law to Fight the Coronavirus,” *Lawfare* March 16, 2020 at <https://www.lawfareblog.com/lessons-america-how-south-korean-authorities-used-law-fight-coronavirus>.

7. Stephan Haggard, *Developmental States*. Cambridge University Press, 2019.

The Return of Great Power Rivalry: The Economic Dimensions

The fact that COVID-19 originated in China and was managed so poorly in the US meant that the virus was bound to get caught up in larger geo-political considerations. How will COVID affect the political economy of the US-China relationship? Answering this question requires a consideration of underlying structural factors—the power transition problem—as well as more elusive questions of status and soft power. The most important question to pose, however, is how policy in Washington might have been changed as a result of the crisis, and the answer may well be “not much.” The strains between the two countries were apparent well prior to 2020 or even 2016 and are not likely to disappear under a Biden administration.

The Structural Issues: Power Transition Redux

Perhaps the most important point to take away from the COVID-19 pandemic is that the effects on countries are proving highly uneven. Of course, all countries are experiencing declines in their growth rates. Not even the most well-managed countries can escape the downdraft from a shock of this magnitude, and particularly given that it struck the major economies—China, Japan, the US, and the EU—at pretty much the same time. But the differences are as striking as the commonalities.

The IMF's June 2020 projections show the world economy as contracting by 4.9 percent in 2020 and rebounding strongly (5.4 percent) in 2021. For our purposes, however, the issue of interest is not the actual growth rates, but the differences in outcomes across countries. According to the IMF, China will experience a decline in growth from its suspiciously stable 6 percent growth trajectory to 1 percent growth in 2020, before rebounding strongly (8.2 percent) in 2021. Indeed, more

granular data suggests China's V-shaped recovery has already begun, with the decline in output concentrated in the first quarter as the government shut the economy down before posting positive growth in the second quarter. Walking around the rest of the region, we see other Asian economies generally doing relatively well: in descending order, the Association of Southeast Asian Nations (ASEAN) –5 at -2.0 percent in 2020, Korea -2.1 percent (May estimate), and Japan at -5.8 percent (and with a weaker 2.4 percent recovery).

Compare those numbers with the US, with a projected decline of 8.0 in 2020 or—among the worst performers in the world—the Euro Area, anticipated to contract by over 10 percent in 2020, with the hardest hit countries—Spain and Italy—seeing negative growth in excess of 12 percent. For those preoccupied with a power transition, these numbers are accelerants: China's relative economic heft will increase even more rapidly during this time of crisis than it was prior to it.

On the one hand, the world economy owes China a debt of gratitude; helping to pull Asia out of the COVID-19 recession is a service to the rest of the world as well. On the other hand, two immediate results will be seen as worrying for the other advanced industrial states. First, China will become a more significant actor for all of those countries that currently depend on it. Even if China's ambitious Belt and Road Initiative (BRI) pauses, Chinese demand is itself a source of leverage the other advanced industrial states implode.

Second, psychological factors—in effect, overconfidence—must also be taken into account. The Global Financial Crisis led a number of Chinese analysts to proclaim that the US was entering a period of significant decline that provided strategic opportunities. There is now a similar concern in the US that China will see an opportunity to move on controversial fronts while the US is internally distracted: with respect to Hong Kong, where a new security law is being put in place as this is being written;

in the South China Sea; and with respect to disputed territory vis-à-vis India to cite only the more visible flash points. Even if these Chinese actions are not strategically exploiting the opportunity, they are likely to be read as such, contributing to the rising alarm over China in the US.

Status and Standing: The Propaganda Wars

The problems in the US-China relationship are not just structural. Status and standing in international relations have always been elusive factors, but they can be given a relatively precise definition. To what extent do both elites and publics see the US as an effective leader, worthy of trust and emulation? Conversely, is the US seen as self-absorbed, uncooperative, or even exploitative? Although neither China nor the US was shown in their best light by the virus, the US is paying the higher price for its ineptitude.

Because China ultimately did such a remarkable job in shutting down the virus, it is worth walking through some of the country's early missteps. They do not sit comfortably with Beijing's subsequent efforts to burnish its international image by papering them over⁸ and indeed are directly connected with the downsides of dominant party rule. The country had set up a Contagious Disease National Direct Reporting System in 2004 to prevent a repeat of the slow response to the SARS epidemic.

When the first cases appeared in Wuhan, however, deference to local party officials on the part of medical staff slowed the early response as those officials sought to tamper with numbers that made them look bad. Doctors seeking to raise their voices were effectively silenced and even persecuted. Local officials sought to downplay the role not only of overall caseload but of the likelihood of human-to-human transmission, an absolutely crucial bit of information in seeking to craft a response. Beijing refused offers from the US Centers for Disease Control and Prevention to share expertise on epidemiology and virology and was slow to share transmission data and biological samples to the WHO. And as Beijing was moving toward a much more aggressive lockdown on domestic travel out of Wuhan and Hubei, as late as early February, the Civil Aviation Administration was still requesting that international flights be maintained to countries that had not yet closed their borders. China was effectively seeding the virus internationally more than a month after it had been identified.

The story cannot—and should not—be told in black and white, as there were also a variety of efforts on the part of China ultimately to warn the US of the risks and to share information on the methods it had used to contain the virus. But in the end, the meandering approach of the Trump administration to the virus and its failure to bring cases and deaths under control will dominate assessments. In a striking poll conducted by Dalia and the Alliance for Democracies in 2020, nearly 150,000 citizens from 53 countries were polled on whether China or the US had done a better job in controlling the virus.⁹ Citizens of virtually all countries rate China's response as much better; indeed, the only countries that think the US's response was better were Japan (+17% more in favor) and the US itself (+13%).

Yet what is also interesting is the gap in confidence within the two countries. Citizens were asked what they thought of their own government's response to the crisis.

8. See *State Council Information Office*, *Fighting COVID-19: China in Action*, June 7, 2020 at http://english.scio.gov.cn/whitepapers/2020-06/07/content_76135269.htm.

9. *Dalia for Alliance for Democracies*, "Democracy Perception Index, 2020," at <https://daliaresearch.com/blog/democracy-perception-index-2020/>.

10. For example, *Pew Research Center*. "Around the World, More See the US Positively Than China, but Little Confidence or Trust in Xi," January 10, 2020 at <https://www.pewresearch.org/fact-tank/2020/01/10/around-the-world-more-see-the-u-s-positively-than-china-but-little-confidence-in-trump-or-xi/>.

China (and Vietnam) topped the list, with 95 percent of respondents believing their government had done a good job. By contrast, only 53 percent of Americans did, only marginally higher than the five most disaffected publics (Japan, Spain, France, Chile, and Brazil).

Going into the COVID crisis, the US was generally seen more positively in much of Europe and elsewhere in Asia than was China.¹⁰ But it is hard to disentangle the effects of the management of COVID from the wider hit to world public opinion that the US has taken as a result of the Trump presidency. In the Pew poll conducted in 33 countries, fully 18 reported that they lacked confidence in both Xi and Trump. The management of COVID was a crucial test that the US has, so far, utterly failed, not only harming its own citizens but largely draining a reservoir of good will that the US had enjoyed.

The Shift in US-China Policy

In the end, the nature of the US-China relationship depends not only on structural issues or the short-term public relations cycle but on how the two countries will move their relationship forward. Unfortunately, that question is being posed as the US is moving toward a much more alarmist view of China. To understand that shift, I focus on the economic issues as those have been central to the Trump administration's approach. I start,

however, by revisiting what might be called the orthodox approach and then considering how it has changed.

After the normalization of relations, the US approach to China emphasized China's role as a "responsible stakeholder" in a global system of which it had been an enormous beneficiary. The US encouraged China to sign up to international institutions with binding rules or to negotiate transparent bilateral commitments. These were coupled with dispute settlement mechanisms for enforcement. In addition, foreign actors—including but not limited to the US—presumed that an evolving legal and administrative system in China itself would keep the reform process moving forward.

In the years between 1978 and 2005, there was enormous progress in this direction, culminating in China's World Trade Organization (WTO) membership. This progress encouraged hopes that China might actually converge toward a mixed but market-oriented economy. Trade disputes would be reduced to the same sorts of conflicts that exist among the advanced industrial states. Integration through a complex network of institutions and bilateral arrangements would serve to manage if not altogether prevent conflicts from escalating: through the WTO, through the Strategic and Economic Dialogue (created in 2009, after China's help in managing the Global Financial Crisis was acknowledged), through ad hoc bilateral agreements





(such as the agreement about cyber issues coming out of the 2013 Sunnylands summit), or through new instruments such as a bilateral investment treaty (BIT).

The bilateral relationship with China was nested in a broader multilateral approach to the region that mirrored in some ways the formal alliance structure. The Trans-Pacific Partnership (TPP) and US bilateral free trade agreements (FTAs) (with Singapore, Australia, and Korea) played a role in the strategy toward China, albeit indirectly. By laying down markers for “high quality” trade agreements, these arrangements signal the issues on which the US and the other advanced industrial states had strong material interests: intellectual property, competition policy, the role of state-owned enterprises, regulated sectors such as finance and telecom and labor and environmental issues.

This liberal institutionalist approach could rely on a modicum of bipartisan consensus on both strategic and economic grounds, albeit with dissent from the nationalist wing of the Republican Party, among labor constituencies in the Democratic Party as well as those focused on human rights in both parties. Support for the relationship was anchored by a coalition of powerful American firms with strong vested interests in the low-cost sourcing networks for a vast range of goods and access to the rapidly-growing Chinese domestic market. The US also benefitted from inflows of official Chinese

capital to keep government borrowing costs low. At the grand strategic level, engagement was seen as a strategy that would ultimately moderate China’s wider foreign policy as well.

This general approach had already started to erode during the Obama years, beginning around 2010 and the initiation of the so-called “pivot” to Asia. However, it became apparent with respect to economic issues in Hillary Clinton’s decision to walk away from the TPP during the 2016 election campaign, an agreement she herself had touted as Secretary of State. There is growing evidence of a partisan realignment around trade issues, with the Republican base now more skeptical of globalization than its Democratic counterparts. But recent polling on perceptions of China during 2019-20 shows that views of China have turned sharply unfavorable in 2019 before the onset of the pandemic (60% unfavorable) with that number only rising in early 2020 (66% unfavorable). Although Republicans were more negative than Democrats (72 percent to 62 percent unfavorable), the animus was clearly bipartisan.¹¹

Trump’s impulses on trade with China were initially held in abeyance during the first year of his administration, in part through tacit agreements reached at Mar-a-Lago in April 2017. The president’s trade policy seemed to be flying off in a variety of different directions, targeting close allies as much as adversaries: Korea,

Japan, Canada, Mexico, and Europe, among others. Over the course of 2018, though, some truces were called. Negotiations were completed on the KORUS FTA, leading to largely cosmetic changes, and of the North American Free Trade Agreement (NAFTA), which ironically incorporated a number of elements from the failed TPP. Negotiations were opened with both Europe and Japan on more limited agreements, and a deal reached with Tokyo in September 2019.

With these truces reached, the focus on China became more apparent and left China exposed. In August 2017, President Trump issued a memorandum directing the US Trade Representative (USTR) to determine if China's policies regarding intellectual property rights theft and forced technology transfers warranted retaliatory action under Section 301 of the 1974 Trade Act. This choice of policy instrument was telling as it had been used throughout the late 1970s and 1980s to go after Asian trading partners and was widely seen as exemplary of US "unilateralism." These actions ultimately culminated in the roll-out of an escalating set of tariffs, a prolonged tit-for-tat phase over the course of 2018-19, and the conclusion of a partial "Phase 1" deal in December 2019. This "win" on the trade front was sorely needed as Trump was entering an election year, and was struck just as the pandemic had become visible in Wuhan.

This story would appear to be one in which Trump's idiosyncratic views and exploitation of executive prerogatives were largely responsible for the shift in US policy. But presumptions about China were undergoing a much broader change in the US, and as the political

campaigns of both Hillary Clinton and Bernie Sanders showed were by no means limited to the Republican Party. Those who had taken strong pro-engagement views in Democratic administrations were also raising doubts about the benefits of the approach.¹²

First, while China continues to be a relatively open economy for its size—measured by trade as a share of GDP—its hybrid model is clearly not trending in a more liberal direction. The commitment of resources to industrial policy accelerated steadily even before the ascent of Xi Jinping. The roll-out of a series of policy tools mobilized to support these programs was emblematic of the new state-led push to foster indigenous innovation and upgrade manufacturing. Moreover, these developments were taking place in sectors that not only had relevance for China's economic position but for its military modernization as well.

The formalization of the Strategic Emerging Industries program in 2010 marked a new stage of resource mobilization. Subsequently, the broadening to an "Innovation-Driven Development Strategy," wrapped up a huge share of industry in policy initiatives. The Made in China 2025 plan (MC2025) launched in 2015 attracted a disproportionate share of the attention abroad, but was in fact, just one of a series of related plans that reflected the new industrial policy focus. These included the "Internet (Plus)" and initiatives with respect to artificial intelligence, smart manufacturing, biopharmaceuticals, and many other sectors. As with other Asian countries earlier in their developmental trajectories, the approach combines a continued focus on exports with strategic efforts to substitute for imports and develop local capabilities – in short, a "neo-mercantilist" or "developmental state" approach. For example, by 2025, the MC2025 plan foresees China domestically producing 70% of key components for industrial robots (such as servo-motors and display panels).

The policy tools that have been deployed to support

11. *Pew Research Center*, "U.S. Views of China Increasingly Negative Amid Coronavirus Outbreak," April 21, 2020 at <https://www.pewresearch.org/global/2020/04/21/u-s-views-of-china-increasingly-negative-amid-coronavirus-outbreak/>.

12. See particularly Kurt M. Campbell and Ely Ratner, "The China Reckoning: How Beijing Defied American Expectations," *Foreign Affairs* (March/April 2018).

MC2025 run up against the rule-based approach outlined above at virtually every turn: in the mobilization of state-controlled financial resources, in restrictions on market access for foreign firms in targeted sectors; in the frequent unbalanced use of competition policy to target foreign competitors; in renewed use of government procurement to support national champions; and in government-supported acquisitions of foreign technology, including through aggressive acquisition strategies. Lurking behind all of these discrete developments is the aggressive use of the state-owned financial system.

Second, the liberal presumption that the existing institutions constitute the only meaningful game in town was also challenged. While the US and Western Europe clash over their commitments to a rule-based approach and whether global institutions can be reformed, China is building its own international institutional alternatives. These include its tacit alliance with ASEAN on the Regional Comprehensive Economic Partnership (RCEP), a more-or-less explicit alternative to the TPP. By far, the most significant Chinese initiative, however, is the BRI, which is neither rule-based nor even really multilateral. Rather, it emphasizes investment in physical capital, including but by no means limited to infrastructure. Moreover, it is structured around a set of bilateral, “hub-and-spoke” deals—none of which is particularly transparent—in which China can negotiate very particular interests. These include agreements with strategically significant countries that would, for example, provide land access through Southeast Asia or a presence on the Indian Ocean, naval basing rights, and even a foothold in Europe (for example, in Greece and even Italy).

Some of these projects have generated controversy, and have been pulled back or even canceled. But these emergent problems actually underscore the underlying reality: China now wields substantial leverage over its trading partners, leverage it has not hesitated to wield. Nor is that leverage simply through the constraints of



manipulating trade ties or even resorting to sanctions. It also comes through the ability to dispense largesse and, at a deeper level still, to set its own standards: from the nature of its trade agreements to product and other commercial standards that lock in competitive advantage. Particularly significant may be China’s ability to spread a new set of telecom, data, and internet protocols that will be attractive to many countries, and supported by dynamic and highly cost-competitive Chinese companies.

What effect will the COVID shock have on this broader bilateral landscape? While both countries now have vulnerability to continued hostilities, COVID has probably shifted those vulnerabilities toward the US.

There can be little question that the Trump approach generated significant nervousness in Beijing. China is still significantly dependent on world markets, even if the US share of China’s exports is now far below its peak in the 1990s, and the Chinese leadership is vulnerable to a growing investor class. But the COVID shock provided cover for the leadership, and as we saw above, it has had some domestic success in touting its management of the crisis. Freed from the shackles of a 6 percent growth target, the Xi administration can focus on the country’s rapid rebound compared to the weak performance in the US.

The US—and the Trump administration—is now more

exposed to the risks of a continued standoff. The key factor strengthening President Trump's bargaining hand prior to the onset of the pandemic was the robust growth in the American economy, which masked the costs of the trade war. Even with those advantages, the Trump tariffs and Chinese retaliation began to bite over the course of 2018 and 2019, particularly in the agricultural sector. By the time the partial deal was struck, the Trump administration was clearly looking for an exit ramp. The administration reached an agreement that banked heavily on targeted purchases by China while side-stepping a number of the complex issues around the country's industrial policy.

During the early days of the pandemic, Trump and his administration struggled with messaging: at times, Trump hailed his friend Xi and the historic deal they struck; at other times, he would pivot to China's responsibility for the pandemic. It is now pretty clear which of these approaches won out: over time, blaming China was revealed to be an organized, self-conscious, and concerted strategy of the Republican Party.¹³ With time running out on the Trump administration's ability to negotiate Phase II, the administration will continue its strategy of incrementally ramping up actions against China. To simply list a few of these additional measures, they include: the broader effort to revise the investment screening process to include outward as well as inward investment; proposed limits on sales to Huawei; the use of emergency powers to block equipment sales to power plants and transmissions systems; new scrutiny of academic collaboration; and—for the first time—a venture into restrictions on capital flows by placing limits on what assets American public pension funds can purchase. And, it should be emphasized, this short list is by no means exhaustive.

The implications of chronic system conflict for the world economy were serious even prior to the onset of the pandemic; now such conflicts pose even greater

economic risks. Yet there are reasons to believe that both sides might reject significant concessions which they see as having negative long-run strategic consequences for what the Chinese call "core interests." For China, these include the ability to pursue industrial policies in sectors deemed to have long-run strategic significance, and to maintain the Communist Party's freedom of action domestically. For the US, these interests include a desire to maintain a degree of primacy on the global scene. The US view has hardened that the conflicts with China are increasingly systemic in nature: that China is competing with the US on the basis of a neo-mercantilist or developmentalist strategy that is fundamentally at odds with a rule-based system. Moreover, China seeks to build international institutions that not only pose challenges to a rule-based order but that exclude the US altogether.

Will this view reverse under a Biden administration? The answer is yes, but not perhaps to the extent expected. A Biden strategy will be more strategic and nuanced, being clear on the desire to carve out areas of cooperation while simultaneously competing in other domains; there will be an olive branch. And clearly, a major reversal from the Trump approach will be an embrace of multilateral approaches in the Asia-Pacific and globally, and precisely as a means of balancing Chinese influence.

But a look at the output of some of the think tanks more closely aligned with the Democratic Party suggests continuity in a number of the measures that the Trump administration has initiated and indeed even pressing them in new directions.¹⁴ There is support in both parties, for example, for the strategic use of tariffs, and particularly

13. See for example O'Donnell and Associates *Corona Big Book: Main Messages*, April 17, 2020, which outlines a concerted strategy to focus blame for the coronavirus onto China.

14. For example, Ely Ratner et al. "Rising to the China Challenge: Renewing American Competitiveness in the Indo-Pacific," *Center for a New American Security*, January 28, 2020. <https://www.cnas.org/publications/reports/rising-to-the-china-challenge>.

against products and firms that are reaping benefits from China's massive industrial subsidy programs. The agenda set by the Trump administration has clearly not been resolved, and a Biden administration will certainly seek to address the outstanding issues left to a Phase II agreement.

It is also widely recognized that technological competition between the two countries requires both the aggressive use not only of trade policy instruments—cutting off Chinese companies that steal technology—but a much more aggressive domestic industrial policy to bolster the US position in sectors such as semiconductors that provide key points of American leverage. Chinese investment in the US, and acquisition of US companies, has benefitted from lax rules of disclosure with respect to the formation of companies, allowing front companies to purchase US assets or technology and threaten critical sectors, data, and infrastructure. Proposals have been floated for more aggressive steps toward Chinese companies that do not meet audit and disclosure requirements, such as delisting from US exchanges. A Biden administration could well look at options with respect to financial leverage as well, such as even more aggressive collaboration with partners to provide financial alternatives to the BRI and limiting investments into and out of the US that pose strategic risks. A Biden administration will not simply go back to the halcyon Obama-era approach; the ground has fundamentally shifted even prior to the COVID shock.

Conclusion: Looking Forward

What effect will COVID have on the international political economy? I have taken three cuts at the question. The first is not to forget the development agenda raised by the crisis. More than the Global Financial Crisis, the pandemic is likely to have major repercussions for developing countries, and it is precisely in that space that more robust international cooperation

is needed. Such cooperation must not only focus on the health problems, but the potential financial fallout for countries who cannot simply print money or easily access international financial markets. Expanded credit facilities, debt standstills, and a workout process are going to be needed to smooth the coming shock and allow emerging markets and poorer developing countries to recover if the pandemic continues to spread.

Second, I argued that the crisis will generate a conversation on the relationship between states and markets more generally. Those governments that did well—both authoritarian and democratic—drew on competent bureaucracies, innovative collaborative relationships with the private sector, and novel approaches to the conduct of macroeconomic policy. The advantages of long-run investments in crisis management and public health were on clear display in countries that did well, while in others—from the US, to Brazil, to the UK—these assets were revealed to be thinner than thought or were squandered in executive mismanagement. But the crisis raises the question of why these focused efforts might not be now used to manage a myriad of other, even more dire, crises that are on the horizon such as those posed by climate change.

Finally, I speculated on the US-China relationship post-COVID and post-Trump. Clearly, China appears to have gained both from its performance in shutting down the disease, in the recovery of its economy and with respect to image. Despite important—and even critical missteps—China's performance only served to highlight the dysfunction of the Trump administration. Yet I also argued that there has been a fundamental rethink of the US-China relationship in the US and a return to an unqualified engagement with China is highly unlikely. If anything, a Biden administration will pursue a more targeted strategic approach to US-China relations that will seek to decouple—if only at the margin—from the dependencies that have emerged since the 1980s.