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US-China Rivalry 2022

An Israeli Perspective

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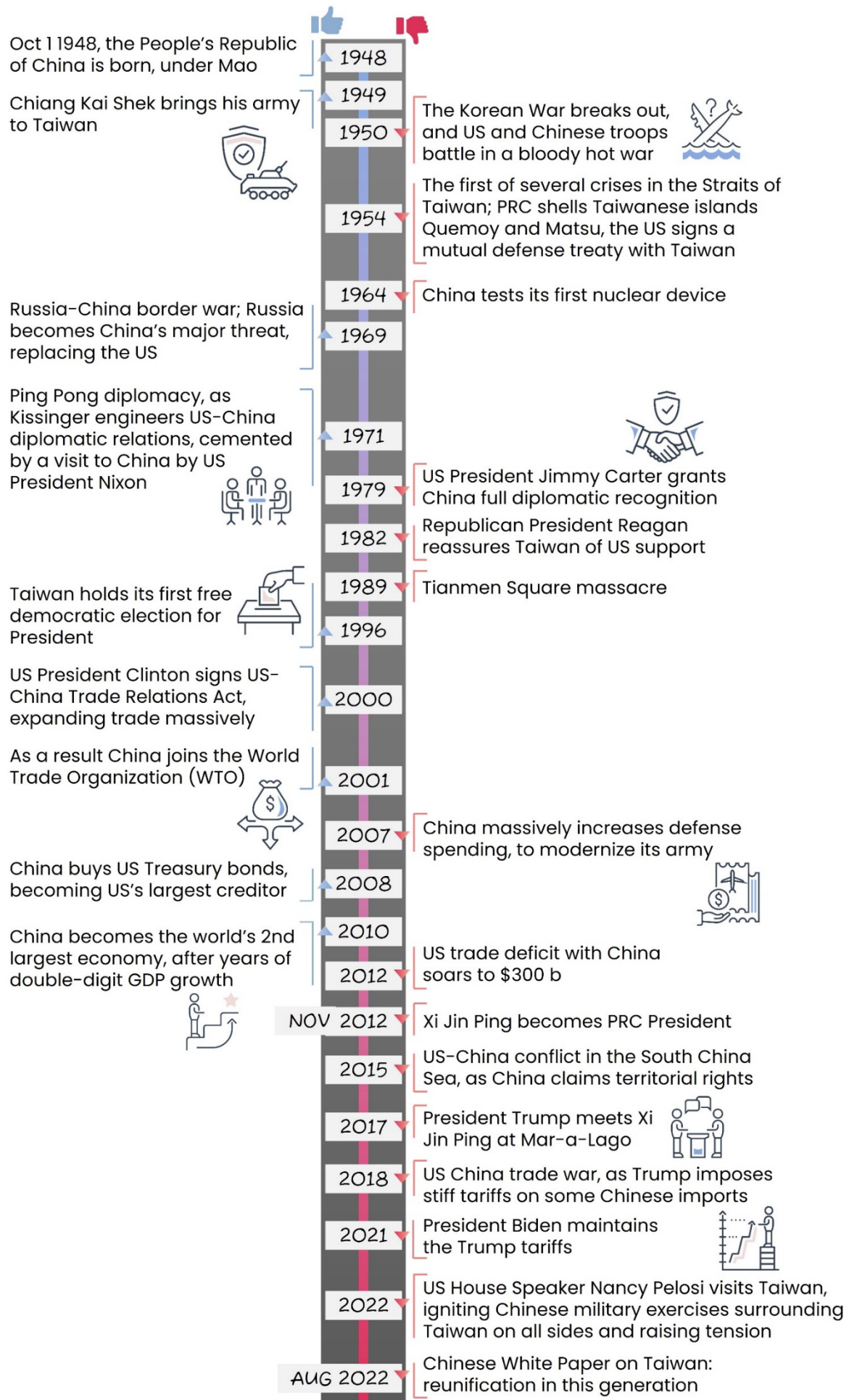
Abstract

This survey paper reviews recent research in the rapidly changing relations among the triangle of Israel, China and the United States. Israel has long enjoyed a special relationship with the US, in trade, investment and technology, and in recent years, has benefited from trade and infrastructure investment with China. US-China rivalry has greatly complicated this triangular context. We review studies, with emphasis on Israel as a small nation somewhat threatened by the rivalry of two major countries with which it has good relations, requiring new strategic thinking on its part.

Introduction

International relations among the Great Powers resemble semi-dormant volcanoes. There are rumblings, that attract little attention – until the volcano (conflict) erupts, often through miscommunication and unintended missteps. And, to mix a metaphor, Great Power relations are also like the shifting dunes in great deserts. Today's friend, tomorrow's foe.

This is especially true of US-China relations. A one-paragraph summary of US-China political, economic and trade relations might go as follows^{1,2} (note the resemblance to a roller coaster ride, with severe ups  and downs ): [See figure below]



In just a few years, China has become the world's premier infrastructure expert, using modern technology, diligent workers, deep pockets and skilled engineers.³ But there is a fly in the ointment. China leveraged its own huge domestic infrastructure projects to create superior competitive advantage globally and geopolitical advantage, notably in its ambitious Belt and Road projects, a revival of the ancient Silk Road.

It was Napoleon who two centuries ago famously observed, "China is a sleeping giant, let her sleep, for when she wakes, she will shake the world."

China has indeed awakened. Its rivalry with the US is rapidly heating up. For Israel, stuck between these two giants, this creates a tough dilemma. When these two elephants rumble, the mice at their feet face danger.

Truthfully, US-China conflict was inevitable. The honeymoon had to end. American consumers benefited massively from offshoring low-cost manufacturing to efficient Chinese plants. But American reliance on Chinese manufacturing has become a friction point, as Russia and China align against the West, in the wake of the Russia-Ukraine War, launched on Feb. 24. A small but significant example is the production of electric batteries for automobiles. China's Contemporary Amperes Technology Co. Ltd., the world's biggest maker of electric-vehicle batteries, is said to be considering building factories in Mexico, to supply Ford and Tesla, in response to US-China hostility.⁴

In this survey, we review recent research and reports on US-China rivalry, all from an Israeli perspective, as a small technology-intensive nation that has benefited from both US and Chinese investments and trade^{5,6} and finds itself 'monkey in the middle' in their growing rivalry. China, newly self-confident, is 'recalculating'. And as a result, so must the US, and Israel with it.⁷

The Crucial Role of Semiconductors

A watershed event occurred on Wednesday July 27. US Senate passed the Chip and Science Act, including a landmark \$280 b. Industrial Policy bill, where 52 B\$ are dedicated to build up US production of semiconductors. Debate took over 18 months. The bill quickly passed the House of Representatives and was signed by President Biden. Senate Republican leader Mitch McConnell, in a rare burst of bipartisanship, noted "the criticality of getting the chips legislation funded".⁸ The US government has been touting a so-called Chips Alliance proposal to chip manufacturing powerhouses in the Asia-Pacific region, now a formal grouping of the US, Japan, Korea and Taiwan, and the US has committed to support that alliance following the Industrial Policy bill.

While this debate lingered, China was acting, as countries unhampered by democratic wrangling can do. It lags seriously in semiconductor technology and has invested massively to close the gap. Semiconductors, “the new oil”, will be a major fault line in the US-China rivalry, with Taiwan, the world’s technology leader in this area, deeply involved. See Trabelsi⁹ and Meng et al.¹⁰

Semiconductor sales are booming. The Semiconductor Industry Association (SIA) announced that worldwide sales of semiconductors totaled \$152.5 billion during the second quarter of 2022, an increase of 13.3% over the second quarter of 2021 and 0.5% more than the first quarter of 2022. Much of this increase in sales represents price increases, as producers bid for scarce chips. Production lines have been halted for many products - e.g. cars and trucks – owing to shortages of chips during the pandemic.

In January, US-based firm Intel announced plans for an initial investment of over \$20 billion in two new leading-edge chip factories in Ohio, even before the semiconductor bill passed the US Congress. Almost immediately, the White House reported that “... companies have announced nearly \$50 billion in additional investments in American semiconductor manufacturing, bringing total business investment to nearly \$150 billion since President Biden took office”.¹¹

US-China rivalry will face off in many realms, including semiconductors. At present the US leads – but China has shown huge capabilities in closing gaps. Peaceful rivalry over technology may be preferable to military rivalry in, for instance, the South China Sea.

Infrastructure: Belt & Road

The Silk Road was an ancient trade network that connected China and the Far East with countries in Europe and the Middle East, for 1,400 years. It included trading posts and markets that helped to store, transport and exchange goods.

Modern China has revived the Silk Road, with its Belt & Road project, a global infrastructure development strategy adopted by the Chinese government in 2013. The project will invest in 150 countries as part of President Xi Jin Ping’s strategy, which calls for China to assume a greater leadership role for global affairs. As of August 2022, 149 countries were listed as having signed to join the project.

In 2020 a “New Infrastructure” program was initiated, which includes huge investments in 5G networks, industrial internet, inter-city transportation (e.g. rapid trains), inner-city rail systems, data centers, artificial intelligence, high voltage and vehicle charging stations.³ Since 2012, China has invested over \$200 b. in 70 countries, on Belt & Road

projects – harbors, container ports, rail lines, etc. Belt & Road accounts for half of China's outbound foreign direct investment.¹² Belt & Road will, by some experts, "diminish US global diplomatic power"¹²; that is a major goal.

Modern China has gained superior competitive advantage and efficiency in infrastructure investment. It seeks growing influence in the Middle East, among other regions, and its Belt & Road project is a keystone in its evolving relations with Egypt, Turkey and Israel¹³.

China has been able to engage in massive infrastructure investments, both within China and abroad, in part owing to its vast and persistent trade surpluses. For over a decade, China has exported \$50 billion a month more than it has imported, piling up foreign exchange used in part for investment abroad.

The Great Rivalry: Tech, Military, Economic

Harvard University's Belfer Center for Science & International Affairs has issued three comprehensive reports on the US China rivalry, in three key areas: technology¹⁵, military¹⁴ and economic¹⁵. The studies were done under the rubric: "Avoiding Great Power War". The overall title itself suggests growing concern that the rivalry may transform from 'cold' to 'hot'.

Regarding technology rivalry, the report quotes TIME magazine, which in 1992 claimed "China cannot grow into an industrial giant in the 21st C." – a picture that changed rapidly by 2010, when China had already, in just a decade, become a low-cost manufacturing site for multinationals. China's rivalry with the US in technology is now what US CIA Director William Burns calls "the main area for competition and rivalry with China", as China displaces the US as the world's top high-tech manufacturer, producing 250 million computers, 25 million cars and 1.5 billion smartphones in 2020.¹⁵ Former Google CEO has claimed that "in the 2030s we will be competing with a country that has a bigger economy, more research and development investments, better research, wider deployment of new technologies and stronger computing infrastructure" than the US.¹⁵

Militarily, "for decades the US has enjoyed uncontested or dominant superiority in every operating domain", noted former US Defense Secretary James Mattis, a former general. "Today, every domain is contested – air, land, sea, space and cyberspace."¹⁴ The report warns that if there is a 'limited war' over Taiwan...the US would likely lose – or having to escalate to a wider war.¹⁴

Economically: “for the first time, since the US overtook Great Britain in the 1870s to become the leading economy in the world, the US now faces an economic rival that is as large and by some measures, larger, than it is.”¹⁵ China has closed the gap in GDP, trade, business and investment, and finance. And nations that have larger GDP’s have historically exercised greater power in international relations.

China’s economy has grown astoundingly, from GDP of \$420 b in 1980 to \$14.6 trillion in 2020; and per capita GDP rose from \$430 (1980) to \$10,400 in 2020.¹⁵

US-China Trade War

Under ex-President Donald Trump, the US launched a trade war with China, noted as “an abrupt departure from its historical leadership in integrating global markets’. By late 2018, the US had imposed tariffs on roughly \$350 b. of Chinese imports, and China retaliated similarly. It is widely believed that this policy failed. NBER experts¹⁶ note that “US consumers bore the brunt of the policy through higher prices”, and the trade war “lowered aggregate real income in both the US and China” (a lose-lose policy).

President Biden has chosen not to reverse the Trump tariffs, maintaining economic rivalry as part of overall US-China rivalry. While economic rivalry is greatly preferred to military rivalry, the win-win benefits of trade (though asymmetrically benefiting China, with its huge trade surplus) have given way to hostility in the realm of economics as well.

Israel-China Trade & Investments

China’s investments in Israel have grown rapidly, at an annual growth rate of 15%, from \$20 m. decades earlier to \$200 m. yearly in 2020. China’s top foreign direct investment areas include mobile, artificial intelligence, healthcare, biotechnology, media and entertainment.¹ Israel has a large trade deficit with China, as does the US, with \$4.4 b. in exports during 2021 against \$16.64 b. in imports.

In contrast, the 1985 US-Israel Free Trade agreement led to a boom in trade between these two countries, as trade rose tenfold!¹ Trade between the two countries now totals over \$50 billion yearly. Israel now invests \$24 b. in the US, triple its level a decade earlier. Among Israel’s 300 foreign R&D centers established in Israel, 200 are US.

Quantitatively, then, US trade with Israel exceeds that of China in importance. However, this is changing. Berman¹⁷ projects that “China could eclipse the US as the single

largest investor in Israel in the coming years". This was written in 2020, well before US-China friction grew, and threatened Israel-China economic relations.

Berman posits that "Israel's government needs a paradigm shift in its thinking about the People's Republic of China, one that begins to view Chinese investment as a whole as a national security problem..." At the same time, Berman argues, "The US...requires a more nuanced policy that differentiates between the types of Chinese investments in Israel.... Many of these implicate few, if any, legitimate national security concerns." Nor is Israel alone in this dilemma. Korea and Taiwan too face growing, often intense, pressure, in relation to the destinations of their key chip production.

The US uses "dual technology" arguments (technology with both military and civilian applications) to pressure Israel against virtually any Chinese project. This pressure goes back two decades to the US veto over sale of Israeli defense technology to China -- the Phalcon Airborne Early Warning System, which has been greatly expanded to include non-military technology.

What has become clear, as political commentator Anshel Pfeiffer notes in the daily Haaretz¹⁸ is that "remaining on the sidelines is going to become increasingly difficult for Israel if the tensions between the US, Russia and China continue to rise. And pressure may come not only from the Americans," he observes.

Writing for the Axios website on August 17, Barak Ravid¹⁹ reported that a top Chinese diplomat warned Israel "not to allow US pressure to damage Israel's relations with Beijing." Ravid notes this was "the most unequivocal and direct message Israel has received from Beijing, about the US-Israel-China triangle."

As expected, the geopolitical temperature is rising. Global 'warming' is not solely confined to greenhouse gases.

Israel's friction with China emerges just as friction grows with Russia.²⁰ Shavit urges Israel "to strive to agree on rules of the game with Russia" regarding the conflict in Syria, where Israel has apparently operated to destroy Iranian forces and weapons. Russia and China increasingly form a cooperative axis. This, too, presents a strategic dilemma for Israel.

Israel's Strategic Options

A report by the Israeli Knesset's economic team²¹ notes that in 2019, Israel's political-defense Cabinet (team of senior ministers and the Prime Minister) agreed to establish a mechanism, to examine national security implications of foreign investments in Israel,

in companies with strategic importance. This is clearly directed in part, though not in whole, to Chinese investments. It indicates a stricter future policy toward such investments. A RAND study²² in 2019, on Israel-China relations, strongly recommends that Israel not sacrifice its relations with China. "Above all, Israel must not endanger its special relationship with the US, but also it must ensure that it does not endanger its important interests regarding relations with China. Both nations can gain from such relations."

The RAND study observes that most US allies behave thus, in promoting entrepreneurship that benefits China.

"The wisest move for Israel", it notes, "would be to build an independent capability to evaluate cost-benefit in its relations with China, and to establish a government mechanism to build an appropriate strategic policy, that permits Israel to benefit from relations with both leading economic superpowers in the world."

Our research is aimed at understanding better the Israeli options and preparing the Israeli industry policies options.

Postscript: Update on Evolving Issues

Writing on the "Breaking Defense" website, Arie Egozi reports (Sept. 20) that the White House is pressuring Israel to cut research ties with China "over dual-use concerns".ⁱ [Dual use concerns refer to technologies that have both civilian and military implications and applications – which covers virtually all technology]. "The move comes," Egozi reports, "as Israel is moving to create stronger bonds with Chinese research agreements", including efforts to attract excellent Chinese students to come to Israel.

Egozi notes that "Israeli officials were surprised by the focus from Washington" – another indication of the urgent need for an immediate strategic audit of Israel-China relations. The pressure from Washington was described by Israel's Ministry of Defense as a "request that cannot be rejected".

ⁱ White House pressuring Israel to cut research ties with China over dual-use concerns. Breaking Defense. September 29, 2022 [\[source\]](#)

Writing on the Asia Times website, Jacob Leon observes (quoting Newsweek) that “China views Israel as a pivotal technological superpower it wishes to exploit”.ⁱⁱ He notes that “...many Israelis in relevant policy and economic positions have been either lethargic or reticent in their responses to the China threat”. He concludes, “Israel’s swelling economic muscle must not come at the cost of vigilance toward the role it may play in the global security threat China poses.”

Finally, Ahmed Moamar reports that the Lapid government “agreed to the urgent US request to place restrictions on the development of relations between Tel Aviv and Beijing and to provide *an opportunity for American oversight*”.ⁱⁱⁱ The question arises: When a clash emerges between perceived US interests and Israeli interests – which will prevail? And how will the clash be resolved?

There is urgent need to explore and define in depth Israel’s strategic options.

ⁱⁱ On China, US and Israel should talk tech, not trade. Asia Times. September 30, 2022 [[source](#)]

ⁱⁱⁱ Israel Caves into US Request to Reduce Relations with China. SEE. September 30, 2022 [[source](#)]

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