



What's Next for China's Geopolitical Relations?

Tensions remain elevated, but expect a return to more multilateral negotiations.



May 2021

KEY INSIGHTS

- China remains keen to engage and trade with the rest of the world, but we anticipate technology competition and supply chain self-security tensions to continue between the U.S. and China.
- We believe the Biden administration brings a more strategic and holistic approach to the U.S.-China relationship. We expect the U.S. to rely on diplomacy and the development of allies in negotiating with Beijing.
- Public concerns over China provide U.S. lawmakers with the political incentive to pursue tougher measures. As a result, decisions like tariff relief may not prove viable in the near term.

Market participants have closely monitored China's constantly evolving relationship with the United States. Tensions between the U.S. and China have been exacerbated by trade wars, sanctions, human rights violations, and threats of delisting of Chinese companies on U.S. exchanges.

Despite signs of economic protectionism, China continues to express a desire to engage with the rest of the world. The recent 14th Five-Year Plan (FYP) (2021–2025) finalized at the National People's Congress in March 2021 called for promoting a high-level opening of the Chinese economy, targeting new trade pacts, and aggressively recruiting foreign investment both in industrial and financial services. These opposing dynamics have led investors to question whether further escalation in geopolitical tensions will detract from China's efforts to pursue new

relationships alongside a more developed economy by its 2035 goal.

U.S.-China Relations to Remain Strained, but Biden Administration Should Offer a More Strategic Approach

The early months of Joe Biden's presidency prioritized recovery from the coronavirus pandemic—both through vaccine rollout and significant fiscal relief spending (USD 1.9 trillion). Though the pandemic represents President Biden's first and foremost priority, he has explicitly and implicitly communicated the importance of national security and economic competition with China. Although the Biden administration has signaled a clean break with its predecessor on most issues, its rhetoric on the U.S.-China relationship has often sounded familiar.



Katie Deal

*Washington Analyst,
U.S. Equity Division*



Chris Kushlis, CFA

Asia Sovereign Credit Analyst

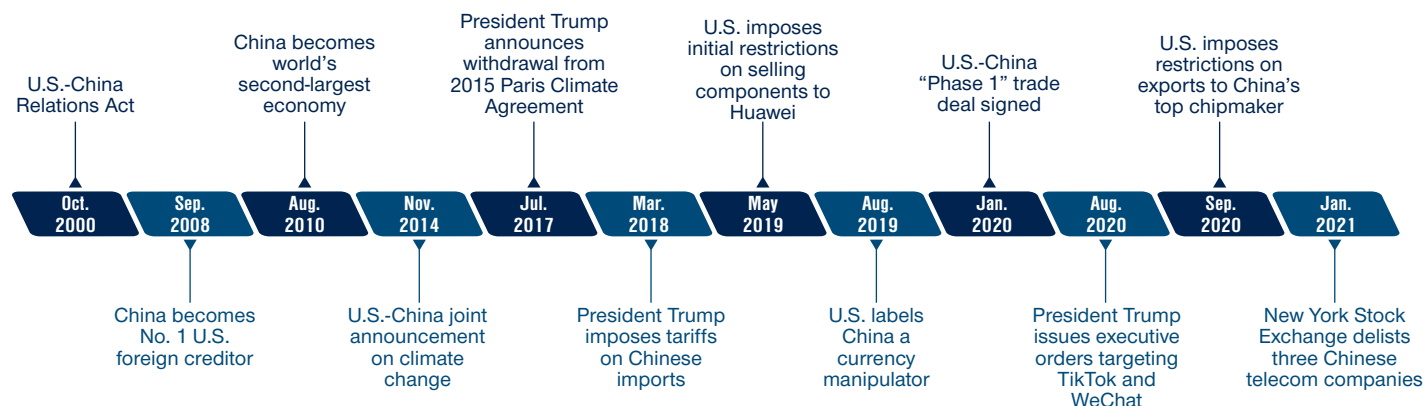
“...[President Biden] has explicitly and implicitly communicated the importance of national security and economic competition with China.

— **Katie Deal**

*Washington Analyst,
U.S. Equity Division*

Timeline of U.S.-China Relations

The Biden administration will likely bring a more strategic and holistic approach, while highlighting America's competitiveness



Source: T. Rowe Price.

The new administration, however, is likely to take a more deliberate and multilateral approach to trade negotiations, meaning that U.S. trade policies may become more rules-based and predictable—lowering the market risk premium. But a more thoughtful approach will not completely remove the risk of escalation, particularly given continued skepticism felt by both the White House and Congress.

While President Biden's approach toward China as a "strategic adversary" reflects some of the concerns held by Trump administration officials, the Biden White House will likely employ a broader, more coordinated set of policy tools in addressing different facets of the relationship. Congress likely will continue bipartisan scrutiny over Chinese market practices, government actions, and geopolitical risks in the region—likely pursuing a new legislative package related to the U.S.-China relationship in the near term. Public opinion further supports this more assertive posturing, providing lawmakers political room to pursue tougher measures. As a result, decisions like tariff relief may not prove viable in the near term—particularly without a more comprehensive series of negotiations between the U.S. and China.

Throughout the Trump administration, U.S.-China relations were marked by pugilistic rhetoric from the White House. We anticipate the Biden administration's messaging will veer from open hostility and confrontation toward diplomatic negotiations that incorporate regional allies and partners. Additionally, we could see the Biden administration pursue distinct areas of cooperation with China, particularly related to climate change and specific matters of national security.

Europe's Relationship With China Will Likely Remain Complex

To accomplish its goal of negotiating effectively with China, the U.S. must partner with the European Union (EU) while finding common ground in its relationship with Beijing—a complex and nuanced foreign policy challenge. While opinion toward China has hardened in many countries, European allies seem reluctant to get drawn into a cold war-style confrontation with China. Although we have seen a broad desire for dialogue and discussion, most EU member states have supported a careful, step-by-step approach, especially as they seek to engage with China on upcoming infrastructure projects like 5G rollout. After Biden spoke at a recent Munich

“...the U.S. delay to reengage in more substantive talks with China is an attempt to establish a broader public-facing front among allies...”

— Katie Deal

Washington Analyst,
U.S. Equity Division

conference, Chancellor Angela Merkel and President Emmanuel Macron both gave remarks with more emphasis on the need to cooperate with China, signaling that an incremental approach may be the best method to develop a U.S.-EU partnership.

We believe that the U.S. delay to reengage in more substantive talks with China is an attempt to establish a broader public-facing front among allies, enabling more leverage in any talks when contrasted with a bilateral approach. Generally, we anticipate that U.S. officials will pursue accord with Europe on issues such as Beijing’s treatment of Muslim Uighurs, the government’s actions in Hong Kong, and market access issues facing multinational firms. But technology issues, such as the 5G debate that strained transatlantic relations during the Trump administration, have the potential to stall progress and buy-in.

China Remains Keen to Engage and Trade With the Rest of the World

While the Biden administration views China with a critical eye, Beijing has

also taken a more careful approach with Washington, suggesting that relations will remain choppy. China is acutely aware of the current U.S.-China dynamic, and these tensions were visible during the first high-level meeting between Chinese and U.S. officials in the new administration.

Though Beijing hopes to benefit from a change in rhetoric from the Biden administration, it is unlikely to make any major unilateral concessions—particularly without comprehensive negotiations. It is also important to recognize that Beijing has undergone a strategic shift in technology and innovation policy, with a more open discussion of longer-term rivalry with the U.S.

More broadly, China is seeking to build its position within the global economy. Beijing sees a large and well-developed renminbi-denominated onshore financial market as crucial for its long-term plan of currency internationalization. Capital markets reform is a core part of the 14th FYP, and the prospect of larger foreign inflows is crucial to achieving that goal.

China Seeking to Build its Position Within the Global Economy

Securing trade pacts and forging new partnerships to help open up their economy



Belt and Road Initiative (2013)



- The Belt and Road Initiative (BRI), set up in 2013, seeks to connect **Asia with Africa and Europe** via land and maritime networks with the aim of improving regional integration, increasing trade and stimulating economic growth.
- Examples of BRI infrastructure investments include ports, buildings, rail, roads, dams, and airports.
- The project has a target completion date of 2049, which will coincide with the centennial anniversary of the People's Republic of China founding.

RCEP Agreement (November 2020)



- China and 14 other countries in the **Asia-Pacific** region signed one of the largest free trade deals in history, with the combined gross domestic product (GDP) of the signatories representing around 30% of global GDP.

CAI Agreement (January 2021)



- International investment agreement signed between **China and EU** to formalize better market access.
- The EU stated that the agreement will be the most ambitious agreement that China has ever concluded.
- As part of the agreement, China is committed to guaranteeing a higher level of access for manufacturing, which makes up half of total EU investment. For Beijing, the deal will lock in existing market access rights while securing some openings in the areas of manufacturing and renewable energy.

Source: T. Rowe Price.

“Beijing has been stepping up its efforts to secure trade pacts with other countries while aggressively opening sectors for foreign investment.

— Chris Kushlis, CFA
Asia Sovereign Credit Analyst

The FYP, despite external challenges, also calls for promoting a high-level opening of the Chinese economy—through more trade and investment liberalization—to “enhance global cooperation.” Beijing has been stepping up its efforts to secure trade pacts with other countries while aggressively opening sectors for foreign investment. Recent agreements include the Regional Comprehensive Economic Partnership (RCEP), signed between 15 Asia-Pacific countries in November 2020, and the EU-China Comprehensive Agreement on Investment (CAI). The CAI agreement is particularly important for the EU as it significantly opens China’s internal market to EU companies.

This is all on top of the already-established plan to build influence in the EM world via the Belt and Road Initiative (BRI). The BRI itself is evolving from a heavy focus on infrastructure to more economic connectivity via supply chain integration and digital/IT integration. Cooperation on vaccine distribution is another area that can be incorporated under the flexible BRI header. China has embarked on vaccine diplomacy pledging 500 million doses of its vaccines to more than 45 countries. Four of China’s vaccine producers have asserted that they could produce at least 2.6 billion doses this year.

China’s Economic Strength Incentivizes Broader Diplomacy

Despite escalated tensions over the past several years, China’s role in the global economy remains prominent, presenting a significant opportunity for investors. However, the geopolitical environment is both fluid and prone to escalation, requiring consistent monitoring over time. Businesses exist within the backdrop of geopolitical risk; and when relationships are tense, it can be more difficult to navigate normal operations. With most international companies seeing Asia—particularly China—as their main growth opportunity going forward, assessing China’s role in global diplomacy will prove valuable in risk assessment.

Market fundamentals remain encouraging for further investment, and we continue to see several elements of the Chinese economy reopening after the coronavirus pandemic, along with an increasing number of international companies expanding their operations in China. Ultimately, the economic opportunity presented by investment in China may incentivize improved relations with other global partners, especially as other economies begin to recover from the pandemic. In an increasingly integrated global economy, the prosperity of countries depends not only on the progress of their own economies, but also on global economic development.

*This is part of a series of **TRP Insights** focusing on **China**. The aim in our series **Investing in China** is to explore the key drivers for China’s economy, market opportunity, outlook, and our strategy for investing.*

T. Rowe Price focuses on delivering investment management excellence that investors can rely on—now and over the long term.

T.RowePrice®

Important Information

This material is being furnished for general informational and/or marketing purposes only. The material does not constitute or undertake to give advice of any nature, including fiduciary investment advice, nor is it intended to serve as the primary basis for an investment decision. Prospective investors are recommended to seek independent legal, financial and tax advice before making any investment decision. T. Rowe Price group of companies including T. Rowe Price Associates, Inc. and/or its affiliates receive revenue from T. Rowe Price investment products and services. **Past performance is not a reliable indicator of future performance.** The value of an investment and any income from it can go down as well as up. Investors may get back less than the amount invested.

The material does not constitute a distribution, an offer, an invitation, a personal or general recommendation or solicitation to sell or buy any securities in any jurisdiction or to conduct any particular investment activity. The material has not been reviewed by any regulatory authority in any jurisdiction.

Information and opinions presented have been obtained or derived from sources believed to be reliable and current; however, we cannot guarantee the sources' accuracy or completeness. There is no guarantee that any forecasts made will come to pass. The views contained herein are as of the date written and are subject to change without notice; these views may differ from those of other T. Rowe Price group companies and/or associates. Under no circumstances should the material, in whole or in part, be copied or redistributed without consent from T. Rowe Price.

The material is not intended for use by persons in jurisdictions which prohibit or restrict the distribution of the material and in certain countries the material is provided upon specific request. It is not intended for distribution to retail investors in any jurisdiction.

Australia—Issued in Australia by T. Rowe Price Australia Limited (ABN: 13 620 668 895 and AFSL: 503741), Level 50, Governor Phillip Tower, 1 Farrer Place, Suite 50B, Sydney, NSW 2000, Australia. For Wholesale Clients only.

Brunei—This material can only be delivered to certain specific institutional investors for informational purpose upon request only. The strategy and/or any products associated with the strategy has not been authorised for distribution in Brunei. No distribution of this material to any member of the public in Brunei is permitted.

Canada—Issued in Canada by T. Rowe Price (Canada), Inc. T. Rowe Price (Canada), Inc.'s investment management services are only available to Accredited Investors as defined under National Instrument 45-106. T. Rowe Price (Canada), Inc. enters into written delegation agreements with affiliates to provide investment management services.

China—This material is provided to specific qualified domestic institutional investor or sovereign wealth fund on a one-on-one basis. No invitation to offer, or offer for, or sale of, the shares will be made in the People's Republic of China ("PRC") (which, for such purpose, does not include the Hong Kong or Macau Special Administrative Regions or Taiwan) or by any means that would be deemed public under the laws of the PRC. The information relating to the strategy contained in this material has not been submitted to or approved by the China Securities Regulatory Commission or any other relevant governmental authority in the PRC. The strategy and/or any product associated with the strategy may only be offered or sold to investors in the PRC that are expressly authorized under the laws and regulations of the PRC to buy and sell securities denominated in a currency other than the Renminbi (or RMB), which is the official currency of the PRC. Potential investors who are resident in the PRC are responsible for obtaining the required approvals from all relevant government authorities in the PRC, including, but not limited to, the State Administration of Foreign Exchange, before purchasing the shares. This document further does not constitute any securities or investment advice to citizens of the PRC, or nationals with permanent residence in the PRC, or to any corporation, partnership, or other entity incorporated or established in the PRC.

DIFC—Issued in the Dubai International Financial Centre by T. Rowe Price International Ltd. This material is communicated on behalf of T. Rowe Price International Ltd. by its representative office which is regulated by the Dubai Financial Services Authority. For Professional Clients only.

EEA ex-UK—Unless indicated otherwise this material is issued and approved by T. Rowe Price (Luxembourg) Management S.à r.l. 35 Boulevard du Prince Henri L-1724 Luxembourg which is authorised and regulated by the Luxembourg Commission de Surveillance du Secteur Financier. For Professional Clients only.

Hong Kong—Issued in Hong Kong by T. Rowe Price Hong Kong Limited, 6/F, Chater House, 8 Connaught Road Central, Hong Kong. T. Rowe Price Hong Kong Limited is licensed and regulated by the Securities & Futures Commission. For Professional Investors only.

Indonesia—This material is intended to be used only by the designated recipient to whom T. Rowe Price delivered; it is for institutional use only. Under no circumstances should the material, in whole or in part, be copied, redistributed or shared, in any medium, without prior written consent from T. Rowe Price. No distribution of this material to members of the public in any jurisdiction is permitted.

Korea—This material is intended only to Qualified Professional Investors upon specific and unsolicited request and may not be reproduced in whole or in part nor can they be transmitted to any other person in the Republic of Korea.

Malaysia—This material can only be delivered to specific institutional investor upon specific and unsolicited request. The strategy and/or any products associated with the strategy has not been authorised for distribution in Malaysia. This material is solely for institutional use and for informational purposes only. This material does not provide investment advice or an offering to make, or an inducement or attempted inducement of any person to enter into or to offer to enter into, an agreement for or with a view to acquiring, disposing of, subscribing for or underwriting securities. Nothing in this material shall be considered a making available of, solicitation to buy, an offering for subscription or purchase or an invitation to subscribe for or purchase any securities, or any other product or service, to any person in any jurisdiction where such offer, solicitation, purchase or sale would be unlawful under the laws of Malaysia.

New Zealand—Issued in New Zealand by T. Rowe Price Australia Limited (ABN: 13 620 668 895 and AFSL: 503741), Level 50, Governor Phillip Tower, 1 Farrer Place, Suite 50B, Sydney, NSW 2000, Australia. No Interests are offered to the public. Accordingly, the Interests may not, directly or indirectly, be offered, sold or delivered in New Zealand, nor may any offering document or advertisement in relation to any offer of the Interests be distributed in New Zealand, other than in circumstances where there is no contravention of the Financial Markets Conduct Act 2013.

Philippines—THE STRATEGY AND/ OR ANY SECURITIES ASSOCIATED WITH THE STRATEGY BEING OFFERED OR SOLD HEREIN HAVE NOT BEEN REGISTERED WITH THE SECURITIES AND EXCHANGE COMMISSION UNDER THE SECURITIES REGULATION CODE. ANY FUTURE OFFER OR SALE OF THE STRATEGY AND/ OR ANY SECURITIES IS SUBJECT TO REGISTRATION REQUIREMENTS UNDER THE CODE, UNLESS SUCH OFFER OR SALE QUALIFIES AS AN EXEMPT TRANSACTION.

Singapore—Issued in Singapore by T. Rowe Price Singapore Private Ltd., No. 501 Orchard Rd, #10-02 Wheelock Place, Singapore 238880. T. Rowe Price Singapore Private Ltd. is licensed and regulated by the Monetary Authority of Singapore. For Institutional and Accredited Investors only.

South Africa—T. Rowe Price International Ltd ("TRPIL") is an authorised financial services provider under the Financial Advisory and Intermediary Services Act, 2002 (FSP Licence Number 31935), authorised to provide "intermediary services" to South African investors.

Switzerland—Issued in Switzerland by T. Rowe Price (Switzerland) GmbH, Talstrasse 65, 6th Floor, 8001 Zurich, Switzerland. For Qualified Investors only.

Taiwan—This does not provide investment advice or recommendations. Nothing in this material shall be considered a solicitation to buy, or an offer to sell, a security, or any other product or service, to any person in the Republic of China.

Thailand—This material has not been and will not be filed with or approved by the Securities Exchange Commission of Thailand or any other regulatory authority in Thailand. The material is provided solely to "institutional investors" as defined under relevant Thai laws and regulations. No distribution of this material to any member of the public in Thailand is permitted. Nothing in this material shall be considered a provision of service, or a solicitation to buy, or an offer to sell, a security, or any other product or service, to any person where such provision, offer, solicitation, purchase or sale would be unlawful under relevant Thai laws and regulations.

UK—This material is issued and approved by T. Rowe Price International Ltd, 60 Queen Victoria Street, London, EC4N 4TZ which is authorised and regulated by the UK Financial Conduct Authority. For Professional Clients only.

USA—Issued in the USA by T. Rowe Price Associates, Inc., 100 East Pratt Street, Baltimore, MD, 21202, which is regulated by the U.S. Securities and Exchange Commission. For Institutional Investors only.

© 2021 T. Rowe Price. All rights reserved. T. ROWE PRICE, INVEST WITH CONFIDENCE, and the bighorn sheep design are, collectively and/or apart, trademarks or registered trademarks of T. Rowe Price Group, Inc.