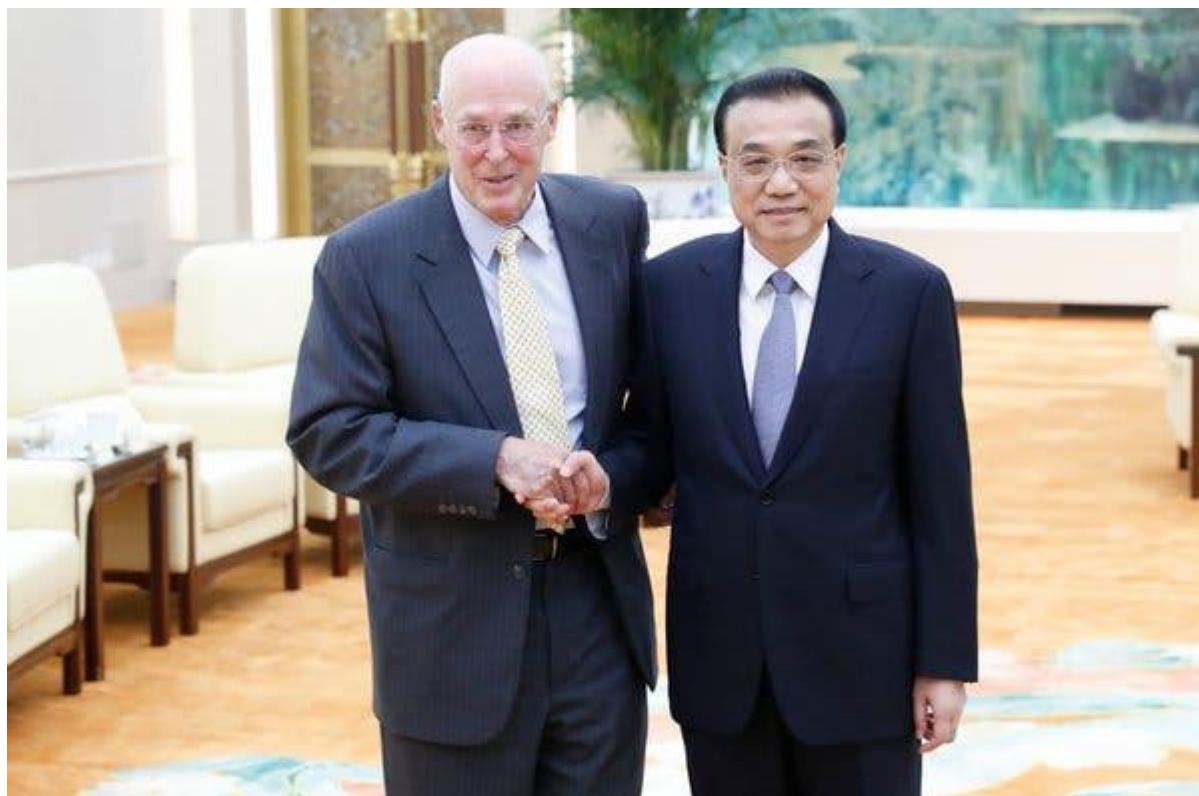


# ***Henry Paulson Sounds Alarm: U.S.-China Relations May Only Get Worse***

Whether or not a trade truce is reached, the two countries have been pushed further apart, the former Treasury secretary said.



Former Treasury Secretary Henry M. Paulson Jr. with China's premier, Li Keqiang, in Beijing last month. Credit...Pool photo by Yukie Nishizawa

The United States and China will eventually settle their differences over tariffs — maybe even reach a deal that allows both sides to say they won.

But don't be fooled. Even if the world's two biggest economies reach a truce, their relationship is likely to get worse.

That's the bold warning that Henry M. Paulson Jr., the former Treasury secretary, plans to make to many of the world's top business and political leaders on Thursday at [a Bloomberg L.P. event on the economy in Beijing](#). During an interview with me this week, he shared a copy of the speech, previewing some of what he will say.

Mr. Paulson has spent a career trying to work with China, starting as a banker at Goldman Sachs, where China represented an enormous business opportunity, and later as Treasury secretary. His think tank, the Paulson Institute, focuses on China. He has

close ties to senior officials in both countries and is often consulted by both sides — so the alarm bells he is ringing are likely to sound loudly in corner offices around the globe.

The danger, Mr. Paulson said, is that the animosity between the two countries has merged “military prisms and ideas into economic policies.”

“It should concern every one of us who cares about the state of the global economy that the *positive*-sum metaphors of healthy *economic* competition are giving way to the *zero*-sum metaphors of *military* competition,” he is planning to say.

Over the summer, President Trump declared on Twitter: “We don’t need China and, frankly, would be far better off without them.” He sent shock through industry when he added: “Our great American companies are hereby ordered to immediately start looking for an alternative to China, including bringing your companies HOME and making your products in the USA.”

Our Country has lost, stupidly, Trillions of Dollars with China over many years. They have stolen our Intellectual Property at a rate of Hundreds of Billions of Dollars a year, & they want to continue. I won’t let that happen! We don’t need China and, frankly, would be far better off without them. The vast amounts of money made and stolen by China from the United States, year after year, for decades, will and must STOP. Our great American companies are hereby ordered to immediately start looking for an alternative to China, including bringing..

Mr. Paulson never mentions Mr. Trump by name in his speech. He is hopeful that the two sides will reach the first stage of an agreement, but he suggested that inflammatory language and the use of tariffs by both sides had been deeply damaging.

“Even when this is done, it won’t be the end of the story,” he said. “The very idea of tariffs has been relegitimated after taking a wallop from the dismal failures of the 1930s.” He added, “We are now living in a world where tariffs have become normalized and even applauded.”

Most worrisome to Mr. Paulson is the prospect that the United States could close off its financial markets to Chinese investment, or even kick some Chinese companies out of American stock indexes.

“Decoupling China from U.S. markets in this way would, of course, harm China,” he said. “But it would not be in America’s interest. It would eventually threaten U.S. leadership in finance, as well as New York City’s role as the world’s financial center. And it would help other financial centers like Tokyo, London and Singapore. And, over time, Shanghai.”

Worse, he described what would happen in an imagined global financial calamity, similar to the 2008 crisis, which consumed Mr. Paulson’s tenure as Treasury secretary.

“When the next crisis comes — and a crisis will come, because financial crises are inevitable — we will regret it if we lack mechanisms for the world’s first- and second-largest economies to coordinate,” he said.

Mr. Paulson raised a worst-case scenario that is often dismissed by policymakers but that he believes deserves a lot more attention.

“Let’s not forget that China is a very large purchaser and holder of U.S. Treasuries,” he said, referring to China ownership of over \$1 trillion in United States debt. “This helps support U.S. monetary policy, enabling lower interest rates and supporting our spending and lack of saving.”

Then, he addressed what virtually no United States policymaker has been willing to acknowledge aloud: If the relationship between the countries deteriorates further, China could decide to sell — or at least not buy — as many Treasury bonds, potentially sending their value down and pushing interest rates much higher. That would undoubtedly hurt China, but it could be tremendously damaging to us, an idea [this column raised last year](#).

“That’s why the unilateral, reciprocal and retaliatory steps on both sides concern me so much,” Mr. Paulson said.

Even if the United States isn’t able to accomplish all it wants in leveling the playing field with China, Mr. Paulson said, the very idea of walking away from the country is a worse outcome.

“It is not in our interest to isolate ourselves when the rest of the world is not going to decouple from China,” he said.

Perhaps most provocatively, Mr. Paulson said the United States and China were creating divisions on technology standards in the name of national security.

“I take my nation’s national security as the highest priority of all,” he said. “But when technologies also have the potential for widespread and beneficial commercial use, sequestration risks ceding economic leadership to a rival company and country.”

He added: “A decision, after all, to protect too much of a country’s technology will ultimately undermine both economic competitiveness and national security.” He said he believed there was a middle ground that would allow for tech systems to work in both countries.

Mr. Paulson told me that he titled his speech “Delusions of Decoupling.” But he was quick to point out that the title “doesn’t mean decoupling is a delusion.”

“The delusion,” he said, “is that it will be easy or beneficial.”