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Trivium China

Markets Note

August tech and trade war roundup

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Welcome to another edition of Trivium's tech and trade war roundup. In these monthly reports, we breakdown geopolitical developments shaping the economic relationship between Beijing and Washington DC.

Here's where things stand as of late August.

The recent flurry of high-level dialogue between China and the US offers hope for a short-term stabilization of relations, even as the two sides continue to pursue measures geared toward long-term economic coercion and competition.

- On the heels of respective June and July visits to China by US Secretary of State Antony Blinken and US Treasury Secretary Janet Yellen, **US Commerce Secretary Gina Raimondo visited China in late August.**
- Raimondo's visit was notable for producing comments by both sides indicating the desire for a stable, productive economic relationship.
- That said, the trip also laid bare the disconnect when it comes to issues of national economic security – Chinese officials decry an "overstretching" of national security considerations by the US, while Raimondo insists such issues are "non-negotiable."
- Ultimately, the series of visits underscore, and hopefully marginally alleviate, concerns by both sides that overall relations have deteriorated too deeply – even as the two countries continue to talk past each other on national security and competition.

The emphasis on security was on full display in DC throughout August, most clearly exemplified by the **Biden Administration's [executive order](#) proposing restrictions on outbound investment into China's high-tech sector.**

- Further, August saw another **bump in bipartisan enthusiasm in the US Congress for tighter trade and investment restrictions.** This development could further complicate the administration's efforts to place guardrails around the Sino-US relationship.

The upshot: It's good news that Beijing and DC are talking – especially at such high levels of government – but in the background, ongoing moves geared toward economic coercion, on both sides, remain the order of the day.

Looking ahead to September, we'll be keeping a close eye on the implementation of recent export controls:

- **[Dutch export controls](#) on semiconductor equipment to China take effect on September 1**, following already-on-the-books restrictions from [Japan](#).
- Meanwhile, China's restrictions on exports of gallium and germanium – critical inputs into the production of advanced semiconductors – officially came into force in early August.

The key question is how stringently the controls will be enforced.

- Having failed to convince the Dutch and Japanese not to follow the US in implementing export restrictions, Beijing has now

shifted its calculation toward pressuring both countries to go light on implementation.

- China's controls could undermine both countries' ability to produce semiconductors and high-end electronics, and is a key stick Beijing can use to convince trade partners to tread lightly on enforcement.

Over the next month or so, all three countries will be feeling out each other's approach. Monitoring enforcement will be key to understanding whether these restrictions are mostly manageable in the short term, or whether we're set for an escalatory spiral.

- Hope you enjoyed your summer vacation, because things may be about to get real.

Now that you're up to speed, here's our wrap of notable August developments in US-China econ relations.

The mood in DC

1. On August 1, the House Select Committee on the CCP announced an **investigation into asset manager BlackRock and index provider MSCI for their China-related investments.**

- The committee is particularly interested in how the companies *"facilitate American capital flows to Chinese companies that have been blacklisted by the U.S. government."*
- Per Committee chairs Mike Gallagher and Raja Krishnamoorthi: *"It is unconscionable for any U.S. company to profit from investments that fuel the military advancement of America's foremost foreign adversary and facilitate human rights abuses."*

Actions have yet to be taken against the companies.

Our take: We expect any regulations restricting investment into Chinese companies to initially target firms already blacklisted by the US government, via inclusion on the Commerce Department's Entity List or other restricted lists.

- However, over time it's not hard to imagine restrictions being extended to target less directly problematic firms, like China's big tech companies.

2. On August 9, US President Joe Biden issued an **executive order (EO) that proposes restrictions on US investment in China's tech sector**, targeting chips, quantum information, and AI.

- The proposal won't be finalized until next year, so we don't know for sure what shape the EO will take.
- We expect it to be a mix of investment prohibitions and requirements that investors notify the Treasury in advance of certain investments.

Following the order, both Democrats and Republicans called for even stricter controls:

- CCP House Select Committee co-chair Raja Krishnamoorthi (D-IL): *"Today's announcement is an essential step forward in*

addressing the very real national security concerns from the CCP, but it cannot be the final step."

- Senator Marco Rubio (R-FL): *"The U.S. needs to do better than this, which is why I will introduce legislation in September to create an outbound investment process that actually protects American economic and national security interests."*
- Chair of the House Foreign Affairs Committee Michael McCaul (R-TX): *"The failure to include existing technology investments as well as sectors like biotechnology and energy is concerning."*

Our take: This is more of an "order to make an order" than a finished product, and there will be plenty of stakeholder discussion and intergovernmental deliberation before this document goes into effect.

- In the meantime, Congress may well pass its own outbound investment legislation.

3. On August 18, President Joe Biden **met with Japanese Prime Minister Kishida Fumio and South Korean President Yoon Suk-yeol** at Camp David.

The three nations will:

"Strengthen trilateral cooperation on export controls to prevent our technologies from being diverted for military or dual-use capabilities."

- Develop "technology protection measures," to stop advanced tech from "being illegally exported or stolen."

As for who these initiatives target, Biden admitted the obvious:

"[We] share concerns about the economic coercion [and] heightened tensions caused by China."

Our take: Despite China's carrots and sticks, the US-Japan-Korean alliance remains determined to restrict advanced technologies.

Our other take: Unlike the US and Japan, lobbying from domestic memory chip maker SK Hynix has kept South Korea from issuing strict semiconductor export controls against China.

- But the summit's language indicates that Yoon may push for tougher restrictions.

4. During the week of August 28, **US Commerce Secretary Gina Raimondo traveled to China.**

While in China, Raimondo met with:

- Premier Li Qiang
- Vice Premier He Lifeng
- Minister of Culture and Tourism Hu Heping
- Shanghai Party Secretary Chen Jining
- Minister of Commerce Wang Wentao

Raimondo and Wang agreed to establish a commercial issues working group and an export control enforcement information mechanism.

- The former, comprising government and private sector representatives, will meet twice a year starting in early 2024.
- The latter aims to “reduce misunderstanding of U.S. national security policies,” and had its first meeting on August 29.

At her meeting with Li, she called for cooperation on:

- Artificial intelligence
- The fentanyl crisis
- Climate change

But, during a press conference after the meetings, Raimondo said she shut down her interlocutors when pressed on tech restrictions:

“Their asks were to reduce export controls on technology.”

“Of course, I said no. We don’t negotiate on matters of national security.”

In final remarks on August 30, Raimondo sounded a positive note:

“The US-Chinese relationship is too consequential and we can’t drift to a place of greater conflict.”

“[The working groups are] the beginning of a new approach. There’s a strong appetite among US business to make this work.”

Our take: Agreeing to increase communication on trade issues is unquestionably a positive development – and Raimondo’s sanguine departing remarks are particularly encouraging.

Our other take: Choking off access to desperately needed semiconductors and other advanced technology is by far the most damaging action Washington has taken against Chinese economic interests.

- The US refusal to relax such measures means there is little room for bilateral relations to improve.

The mood in Beijing

1. On July 31, the Ministry of Commerce and several other agencies **widened export controls on certain civilian drones and related technologies.**

- In addition to controlling specific items, the rules also prohibit the export of other drones if their end use is for military or terrorist purposes.
- The aim is to close the loophole whereby Chinese third-party vendors continue to sell drones to Russia or Ukraine even after DJI, the leading maker, stopped direct sales to those countries.

Our take: Beijing wants to show Europe it’s committed to brokering a peace deal.

- Having Chinese drones buzzing the battlefield seriously undermines that effort.

2. In an August 10 statement **responding to the Biden executive order on outbound investment**, China's Ministry of Commerce said:

"The US...is pursuing decoupling in the investment sector... and seriously disrupting global supply chain security."

"China is deeply concerned about this and reserves the right to take measures in response."

Our take: Beijing is trying to present the US's restrictive moves to contain China's tech development as destabilizing to global trade flows.

- To date, that line has largely failed to convince other countries to reject DC's efforts.

3. On August 10, the Ministry of State Security (MSS) issued a post on its WeChat account **explaining the rationale behind Beijing's recent export controls on the critical minerals gallium and germanium**.

The message: Controls on the export of gallium and germanium were imposed for national security reasons, not in retaliation to foreign export controls.

MSS told foreign media not to read too much into the controls:

"The measures have been maliciously misinterpreted by some foreign media outlets."

"The purpose...is exactly what was stated by our official media – safeguarding national security is a necessary action!"

Our take: No matter how MSS spins it, China's mineral export controls are undoubtedly a response to foreign chip controls.

- More importantly, the rationale doesn't really matter – implementation and effectiveness does.

4. American tech giant **Intel's bid to acquire Israeli semiconductor manufacturer Tower Semiconductor collapsed on August 16 as China's antitrust regulator (SAMR) didn't approve the deal** in time.

In typical SAMR fashion, it didn't block the acquisition, per se.

- Instead, SAMR remained silent and just let the clock run out.
- That's exactly how SAMR handled the Qualcomm-NXP Semiconductors merger during the 2018 US-China trade war.

Our take: Beijing has been on a foreign business charm offensive. The collapse of the deal will undermine that effort.

- But for Beijing, showing the US that cutting China off from key technologies has consequences is a far higher priority than making foreign business happy.
- We expect Beijing to continue to weaponize antitrust deal approvals, given its limited avenues for retaliation against US efforts to contain China's tech development.

Stay tuned for next month's update – there's sure to be plenty on the boil.

Why the tech and trade roundup? And why now?

Geopolitics are increasingly at the center of China's economic story. Given the US is actively taking steps to reshape its relationship – and that of its allies – with China, it's become necessary for multinational companies and investors to keep track of the expanding list of China-focused economic restrictions and Beijing's evolving approach to dealing with them.

Thus, we've recently kicked off the Trivium China tech and trade war roundup! Each month, we'll bring you a recap of key developments in China-related cross-border trade and investment restrictions and assess where things are headed.

We hope you enjoy it – and feel free to send through comments and suggestions for improvement any time.

Need anything more?

Send us mail

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