US – China
Special Report

Preparing For A Prolonged Cold War

How Worsening US – China Relations Will Impact Companies And Investors

CAPSTONE


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Introduction

The era of China's relative openness is coming to a close.

The doors that led to the era of globalization, thrust open by the end of the Cold War, are shutting. The burgeoning number of laws and policies to reinvigorate domestic industries, "reshore" or "friend-shore" critical capabilities, prevent misappropriation of technology, and enhance supply chain security are being deployed—ostensibly to limit dependence on China or ensure America's high-tech supremacy. For business leaders and investors, this means reimagining how global trade operations can and should be restructured—and how government intervention will restructure them.

Though investors and companies are coming to terms with the change in the US-China relationship, we believe many still do not fully appreciate the accelerating pace of deterioration in the relationship and severely underappreciate the potential near- and long-term implications this dynamic has for their investments.

Consequently, the rules for high-tech industries are being rewritten in real time, including the release of the US Commerce Department Bureau of Industry and Security (BIS) Interim Final Rule regarding the semiconductor and advanced computing industries. Upon its publication, companies in the US and abroad immediately halted shipments to and paused services in China, and directed US personnel to leave the country or cease their work.

Investors today are seeing the mounting trade and national security challenges that investments in China face. Many investors say their Chinese strategies are specifically designed to avoid the US-China nexus and instead focus on Chinese companies that serve the domestic market. However, this "safer" strategy also could run afoul of US policy and investment firms' environmental, social, and governance (ESG) principles.

Policies meant to prohibit US investors from investing in or trading with companies that use forced labor are set to tighten after the State Department's January 2021 declaration that the Chinese Communist Party (CCP) was committing genocide against the Muslim ethnic minority Uyghurs in the Xinjiang Autonomous Region of China. It is almost impossible for a US company to certify that a Chinese company does not have links to using forced labor somewhere in its supply chain. Many of our conversations with corporate and investor clients underscore the growing concern that these risks will only be compounded in the future.

ENTER POLITICS

Political imperatives are accelerating the deterioration of relationships.

Fox News and other conservative media outlets in the US regularly accuse President Biden of being soft on China. Our sources in the White

2022 AT A GLANCE

US GDP Growth

2.1%

China GDP Growth

3%

Bilateral Trade US Exports to China

$153.8B

China Exports to US

$536.8B

Increase in US Trade Deficit with China

8.3%

Sources: US GDP, US Bureau of Economic Analysis; China GDP, National Bureau of Statistics of China; Trade data, US Census Bureau

House suggest the administration will meet these accusations with policies that are at least as tough as the Trump administration, if not tougher. The Biden administration's political strategy is to do whatever it takes to stop Republicans from outflanking Democrats on China. Therefore, the more Republicans accuse Democrats of being weak on China, the more aggressive Democrats will become. In future political campaigns, the two parties are likely to attempt to out-do each other in their efforts to be tough on China.

But they will have to come together at some point, as the number one policy at recent Group of Seven (G7) meetings has been to convince allies to join the US in a tougher policy toward China.

CALLING IT A COLD WAR

We may not be in a Cold War now, but that is likely where we are headed.

Although foreign policy wonks, and certainly CEOs, are loath to call the present situation a "cold war," it is getting harder to see it as anything else. In fact, most in the corporate world believe a return to the good old days of engagement and unfettered commerce between China and the West is inevitable. This stands in stark contrast to the views of policymakers on both sides of the aisle, whom we have spoken with in the past year. If the West is entering a period of cold war with China, then investors must analyze the economic implications.

There was little trade or commerce between the West and the Soviet Union during the last Cold War. In light of higher interest rates, what will happen to the sales to China for companies such as Apple Inc. (16% sales to China), Intel Corp. (21%), and Qualcomm Inc. (46%) if the West engages in a cold war with China?

HIGHER INTEREST RATES

Federal Reserve rate hikes add to an already combustible situation.

Emerging markets will be particularly vulnerable to the impact of a stronger US dollar. Countries with fixed currency exchange rates could suffer as the US continues to raise interest rates. In 1998, rising rates in the US sparked the Asian Financial Crisis. Asian countries with currencies pegged to the US dollar suffered when money suddenly flowed out of those economies and into the US as investors sought higher interest rates, leading to a series of Asian currency devaluations and deep recessions.

We believe a similar dynamic could unfold, however, this time the magnetic pull of higher interest rates will be magnified by historically high fiscal spending in the US, making investing in the US similarly attractive. The $1.2 trillion Infrastructure Investment and Jobs Act (IIJA) and the $369 billion in energy security and climate change spending from the Inflation Reduction Act (IRA) could divert investments from emerging markets to the US, given the enormity of the coming spending.

Capstone has written at length about the investment opportunities that both the IIJA and IRA create. Many of our corporate clients have engaged Capstone to help them create a heat map of where infrastructure funding will flow in order to pinpoint the most attractive projects. Infrastructure projects ranging from cybersecurity to enhancements to the electric grid will benefit from the IIJA and the IRA. The combined policies also will make the US the source for renewable power investing.

If the US is poised to benefit in an environment with rising interest rates and outsized fiscal spending, then China could be a loser. Capstone has spoken with several companies in the US, Asia, and Europe that are planning to make long-term changes to their supply chain and manufacturing strategies. Companies suddenly seem to have woken up to the risks of having all of their proverbial eggs in the "China basket." ESG-related concerns regarding forced labor, and worries about a radical shift toward Maoist Communism and the increasingly aggressive approach of US policymaking are forcing companies worldwide to reconsider China as a manufacturing base. This comes at a time when some global companies no longer believe a manufacturing base in China will help them sell their products profitably in the Chinese domestic market.

It is, of course, overly simplistic to say there is a zero-sum game between the US and China. However, in an interconnected world, the collateral damage from these shifts could impact the global economy in unforeseen ways. In addition, a weakening Chinese economy could directly result in significant political risk in Asia. A hard landing in China, for example, could prompt the ruling CCP to bolster its legitimacy by invading Taiwan or to show similar military muscle-flexing. This type of geopolitical instability is not far-fetched in the current environment, and it could easily dwarf the economic scenarios discussed so far.

RISK OF A HOT WAR

What is worse than a cold war? A hot one.

On June 15, 2022, 28 Chinese military planes, including advanced fighters and nuclear-capable bombers, entered Taiwanese airspace, the largest in a series of recent incursions. Overall, there have been more than 380 such incursions since 2020. Many experts believe they are not merely shows of force, but also a prelude to an invasion. Chinese President Xi Jinping has repeatedly stated that reunification is necessary to complete his vision for a modern China. In addition, the Chinese Foreign Minister said the use of force to achieve reunification will never be ruled out. Our contacts in US national security circles suggest that a Chinese invasion of Taiwan is rapidly moving up the list of priority threats.
The US pursues a policy of "strategic ambiguity" toward its commitment to defend Taiwan from an invasion, intentionally making the Chinese guess to what extent we will intervene. Considering the massive upgrade in Chinese military capabilities in the past decade, most military planners believe there is nothing the US could do to stop China from invading Taiwan. This fact alone increases the risk of China acting. Although the loss of life and Taiwan's sovereignty would be the real tragedy, investors also will have to consider the impact on their investments in China and Taiwan. Clients should consider hedging this risk with Taiwan index futures and options, which are among the most liquid in the world.

Tech's Challenging Path Gets Tougher

Capstone believes the divided Congress will push US-China relations and technology policy further down an already challenging path. Here, we highlight six key takeaways for investors:

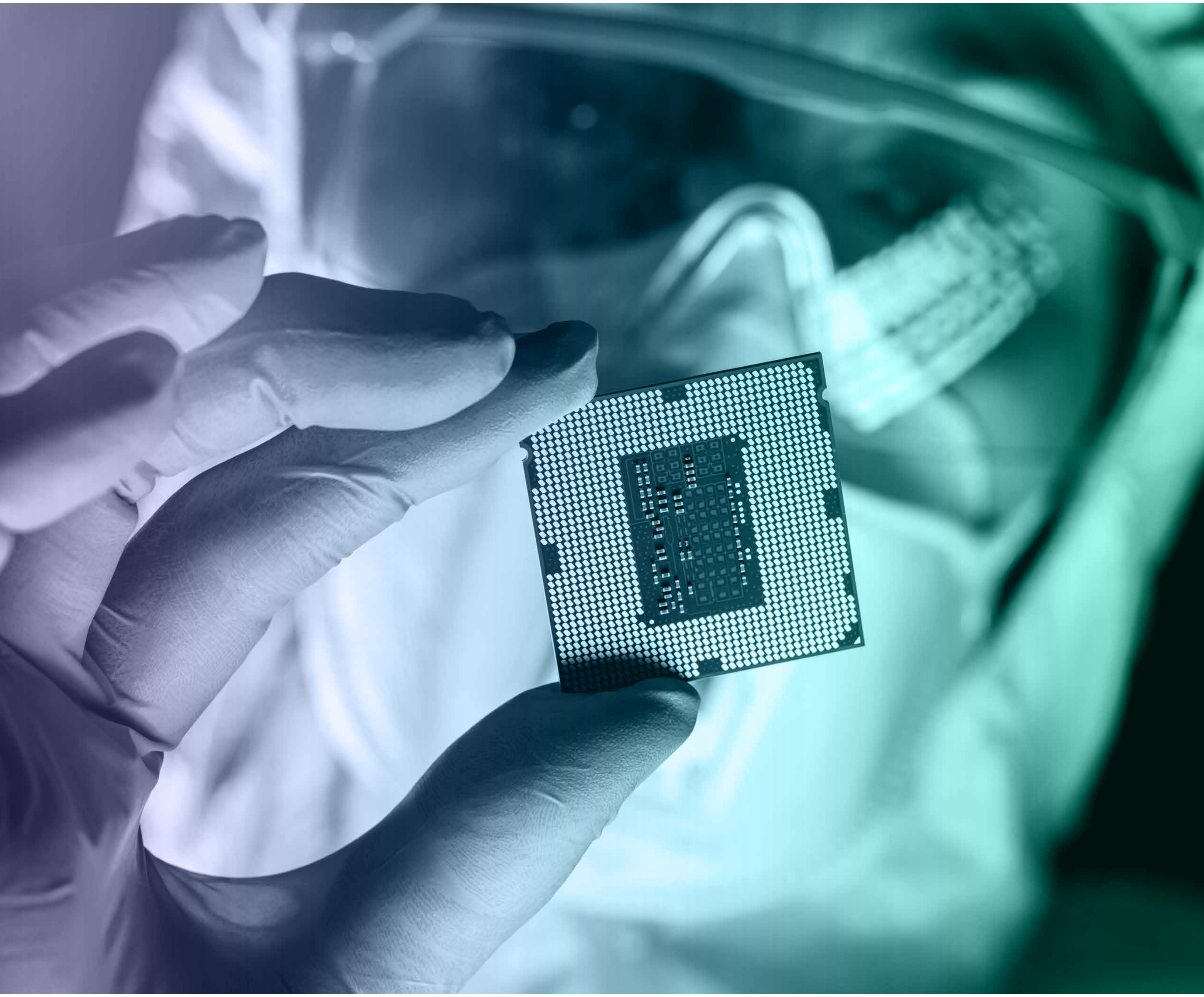
1. The Biden administration and Congress will continue the US approach toward competition with China that began in 2016, keeping the legislative focus on strategic technologies and Taiwan. The 118th Congress will likely prioritize actions that defend against China accessing the personal data of US citizens, export controls, federal incentives for domestic reshoring, and investment screenings.

2. Continued Democratic control of the Senate will bolster the Biden administration's foreign policy efforts. Although Republicans have a slim majority in the House, the lack of a "red wave" after the 2022 midterm election was a positive for President Biden's goals for rebuilding trust with key allies. This calmer environment and the perception of a continuation of foreign policy will help the executive branch in its efforts to cooperate with important partners such as Japan, the Netherlands, and South Korea. This in turn will help the Biden administration's efforts to reach a more formal multilateral agreement on semiconductors and advanced computing. Rather than implement abrupt measures aimed at specific Chinese entities, such as ByteDance's TikTok, we believe Democratic lawmakers will likely wait for federal agencies to exercise their statutory authorities.

3. The Biden administration is likely to lean heavily on top-tier talks. Some bipartisan congressional action on China is likely to be more hawkish than the administration would prefer, especially with Taiwan. However, high-level talks with Chinese President Xi will be critical in managing the US-China relationship given diplomatic engagements below top-tier talks are becoming increasingly fruitless.

4. The divided Congress will change the dynamics between the House and the Senate, including on China-related legislation. For example, despite disagreements between the chambers on how to structure the appropriations bill to fund the Creating Helpful Incentives for Producing Semiconductors (CHIPS) Act, the final product leaned toward the Senate's Endless Frontier framework. With Speaker Kevin McCarthy (R-CA) and the slim Republican majority in the House, Congress is likely to become tenser and noisier and it will become more challenging to pass legislation.

5. How Democrats address China during the next year will determine rhetoric in the 2024 presidential election. Republicans have criticized President Biden as "soft on China,"



especially compared to his predecessor. More hawkish members of the caucus, including Senator Marco Rubio (R-FL), are targeting the administration's slow pace updating the BIS Entity List and its reported tentative deal with TikTok to not change its ownership structure. These concerns will lead to additional proposals and pressure the Biden administration to act more quickly.

6. The state of the US economy presents an opportunity for Republican lawmakers to diverge from the longstanding bipartisan consensus on China. If the US enters a deep or prolonged economic slowdown, Republicans could call for an end to the Biden administration's policies that impact exports, supply chains, and trade with China. While this scenario is unlikely, it could lead to a moderation of how aggressively Democrats target China.

Republican House Will Turn Up Congress' Bark but Not Sharpen Its Bite

House Republicans have made clear that they intend to make China a priority with their newfound majority. The top Republican on the House Foreign Affairs Committee, Michael McCaul, quarterbacked a GOP China Task Force on behalf of Rep. McCarthy immediately before the 2020 election, and its report provides a blueprint of the GOP's multifaceted effort to address the "China challenge." On January 10th, the House also voted overwhelmingly in favor (365/65) of launching a China select committee, as McCarthy, now House Speaker, had promised. Recent news that Republicans are questioning President Biden's rotation of fighter jets based in Okinawa, highlights that a GOP-controlled House will push a harder line on China and seek to outflank the administration, as well as Democrats more broadly.

With Republicans in control of the House, proposals are likely to include far more aggressive language than Democrats might insert on their own, forcing House Democrats and the White House to play defense on a politically compelling issue. This is exactly what happened when Republicans controlled the House from 2011–2018. National security bills initially included restrictive provisions on Gitmo transfers, negotiations with Iran, and socially conservative issues such as access to reproductive health. In regard to China, that also could mean additional restrictions on outbound investment and technology transfer.

However, we believe this signals little and will likely be a lot of noise. Even if Republicans try to attach those measures into year-end spending bills, they will be forced by House rules to limit such provisions to the defense spending context For example, no Defense Department funds can be used to support Chinese companies. Moreover, given their slim margins, Democrats will likely succeed in knocking out controversial measures while joining Republicans on efforts to implement the stalled pieces of the bipartisan Endless Frontier Act, which passed the Senate but got minimal support from House lawmakers during the conference process. The China Select Committee, which have 11 Democrats, will generate headlines but not much practical legislation.

In short, the gridlock that we expect in other policy contexts will pervade the foreign policy space, resulting in legislative stasis on China. The tone may shift, but the White House will continue to determine how far and when to push measures such as outbound investment restrictions, and bipartisan congressional pressure will not change its calculation much.

US Manufacturing Renaissance

Our conversations with corporate clients and prospects have been dominated by companies from Europe, Australia, Japan, and Korea, all seeking to build manufacturing facilities in the US. There are many complex factors leading to this shift in strategy, but the change began well before the passage of the CHIPS Act and the Inflation Reduction Act (IRA).

We believe the interest began after 2012 with two unrelated events. The first was the ascension of President Xi to power in China, and the second was the creation of the Low Carbon Fuel Standard (LCFS) in California. These two separate developments began a process that has led many businesses to reevaluate their long-term plans.

ASCENSION OF XI JINPING

President Xi has signaled that he was uncomfortable with the growing power of China's private sector, and began asserting state control over formerly private enterprises. Companies using China as a global manufacturing base have had to confront that their local partners are increasingly controlled by the Chinese Communist Party.

For companies operating in the telecom and technology sectors, the growing rift in US-China relations is creating growing pressure to diversify from China. Consequently, Capstone believes in certain sectors, companies will have to choose between doing business with the US and China.

COVID-19 was the final straw for many companies on the fence about moving at least some of their manufacturing out of China. The pandemic's myriad disruptions shattered the wisdom of "just-in-time" manufacturing with its lean inventories and factories far from a company's end markets. Post-pandemic, the conventional wisdom now is to focus on resiliency and to manufacture goods as close to the end market as possible.

THE ATTRACTION OF CALIFORNIA'S LOW CARBON FUEL STANDARD

California's LCFS was an early catalyst for attracting foreign investment in the US energy sector. A massive subsidy for renewable gas and electricity production, the program attracted companies from Asia and Europe with technology and experience developed in their smaller home markets. And because the LCFS applies to the entire US, not just California, this new market would be huge.

The California program started a renewable energy revolution, and almost a decade later the Inflation Reduction Act will supercharge that trend. The massive subsidies included in the IRA for producing green power, electric vehicles (EVs), batteries, and critical minerals are a game-changer for global companies seeking to invest in the US.

What the IRA is to the energy industry, the CHIPs Act is to the semiconductor industry. The bill, a combination of R&D money and tax credits for manufacturers building semiconductor fabs in the US, is especially powerful when combined with policy trying to deter companies in the US and its allies from making semiconductors in China. However, it is a classic carrot-and-stick approach. The CHIPs Act creates powerful incentives to build in the US on one hand, but US export control policies are trying to make it impossible for companies in the US, EU, and Asia to produce semiconductors in China on the other.

Capstone believes these policies are deeply rooted in a bipartisan national security-based consensus and therefore are likely to toughen during the next decade than recede.

THE INDUSTRIAL IMPACT OF RUSSIA'S INVASION OF UKRAINE

The Russian invasion of Ukraine in February 2022 is also spurring the US manufacturing renaissance. The war caused natural gas prices to spike dramatically across Europe, which in turn has caused gas-intensive industries such as cement, glass, steel, aluminum, and chemicals to severely curtail production. Although the US is unlikely to be the recipient of much investment in these industries due to environmental regulations, the high cost of gas and electricity in the EU is likely to push many manufacturers to choose the US over the EU for new manufacturing investment.

> The rapid demise of globalization will spur a sea change in foreign and economic policies.

VALUE OF 2020 SEMICONDUCTOR EXPORTS

China

$35.8B

US

$5B

VALUE OF 2020 SEMICONDUCTOR IMPORTS

China

$10.8B

US

$12.5B

US MANUFACTURING JOB GAINS

2021	2022
3.1%	**3.2%**

Sources: Semiconductor imports and exports, Observatory of Economic Complexity; Manufacturing jobs, US Department of Labor

As Capstone bridges regulatory analysis with management consulting, we provide companies with market-entry strategies rooted in policy and political realities. It is unwise in the extreme to invest billions of dollars without a clear understanding of the longevity of certain subsidies. Capstone also provides advice, conducts market studies through a policy lens, and helps clients make siting decisions based on political stability and state policy trends.

For example, a manufacturing renaissance certainly sounds like a positive from a US perspective. However, in the long-term, it could have serious repercussions. The US has been a leading champion of globalization and free trade for three decades, but that era will end with economic and political costs. The Buy American provisions of the IRA are deeply offensive to US allies in Korea and the EU. The policies stick a finger in the eye of allies who are critical to the success of many US policies, not least of which are those focused on China.

But even if the Buy American provisions were changed, the IRA, coupled with the CHIPs Act and other policies, represents a modern industrial policy that will have a domino effect in the developed world. Capstone has written often about EU policies in the works to match the CHIPS Act.

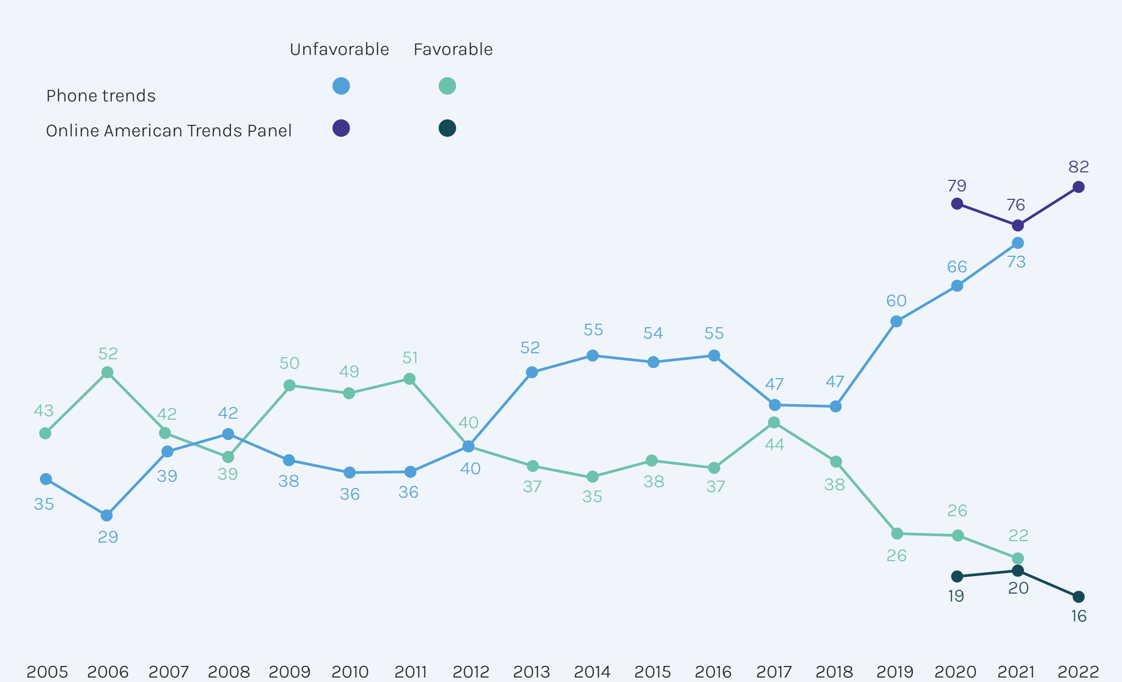
We have also become aware of rapidly convened meetings to discuss an EU version of the Inflation Reduction Act. The rapid demise of globalization will spur a sea change in foreign and economic policies. Capstone, as always, stands ready to provide clients with the analysis necessary to predict how this changing policy landscape will impact their businesses.

Bipartisan Trade Response

For much of past year, congressional Democrats and staff worked furiously on a reconciliation package incorporating a long wish list of healthcare, climate, and tax provisions. The pressure to pass something was palpable, not just because there was a desire among Democrats to have a signature legislative accomplishment to show voters, but also because of a fear of what would come after the November 2022 election. With Republicans retaking control of the House of Representatives, Democrats rightly feared their ability to use budget reconciliation to overcome the customary 60-vote threshold in the Senate would disappear. Now that has happened, leaving many to wonder what comes next.

Much has been made about the decline of bipartisanship in Washington, and the 118th Congress will likely be less productive than the previous one. As we look at current Congress, the issue that could be primed for both legislative and executive action is trade policy.

EIGHT IN TEN AMERICANS EXPRESS AN UNFAVORABLE OPINION OF CHINA



% who say they have a(n) opinion of China

Note: Those who did not answer not shown.

Source: Pew Research Center, Survey of US adults conducted March 21-27, 2022

WHY TRADE POLICY:

Capstone can see trade policy in general, and trade policy targeting China in particular, undergoing significant shifts with a divided Congress for two reasons: 1) both parties see potential political gain; and 2) it can be easily accomplished by executive action. Recent polling from the Pew Research Center shows that since the Trump administration, both Democrats and Republican's views regarding China have become more hostile, with a strong majority in both parties describing "cold" feelings toward China.

Republicans have telegraphed their intention to capitalize on China's unpopularity with voters. In a recent interview with CNN, House Speaker McCarthy said the GOP will launch a "frontal attack" on China to stop the flow of fentanyl into the US. Republican actions on China likely will not stop there. In the lead-up to the 2024 election, we expect Republicans to paint President Biden and Democrats as weak on China based on current US trade policy.

For its part, the Biden administration has similarly sought to stake out a tough-on-China position, something we expect to continue as the 2024 election draws nearer. Senior Biden administration officials maintain their intent to address the harm caused by Chinese industrial policies. However, unlike House Republicans, President Biden can act unilaterally and materially change the US-China trade relationship. During the past 100 years, Congress has delegated significant authority to the executive branch to oversee US trade policy. President Biden and US Trade Representative Katherine Tai have the ability to maneuver when it comes to a range of restrictions on imports, exports, and foreign investment.

WHAT ACTION WILL LOOK LIKE:

For investors, perhaps the most intriguing action comes from the prospect of the Biden administration reopening President Trump's Section 301 tariffs on products imported from China. President Biden has long signaled his desire to put his stamp on President Trump's signature trade policy, and we believe it is likely that he is serious about doing this before the 2024 election. Before former House Speaker Nancy Pelosi's visit to Taiwan in August 2022 and the deterioration in US-China relations that followed, many of our contacts speculated that a new Section 301 investigation was likely.

While it is difficult to know exactly how the Biden administration will shape China tariffs, two themes seem likely to factor in prominently.

First, President Biden will likely reduce tariffs on more consumer goods in an effort to provide buyers some relief from rising inflation.

Second, the Biden administration will look to increase tariffs on products that benefit from Chinese industrial subsidies, including those in the Made in China 2025 Plan. This could result in significantly higher tariffs on everything from lithium-ion batteries to medical devices. Though less likely to grab headlines, a trade bill also could have significant implications for investors and represents one of the early favorites for major legislation that could be passed in a divided Congress.

The foundation for any trade bill in Congress will likely be drawn from a chapter that was dropped from the CHIPS Act. While the CHIPS Act trade chapter includes many relatively mundane provisions, such as tariff relief for highly specialized products ordinarily found in Miscellaneous Tariff Bills, it also could include fundamental changes to US trade law.

Legislation introduced in the previous Congress by Senators Rob Portman (R-OH) and Sherrod Brown (D-OH) that would supercharge sections of US trade law governing antidumping and countervailing duties has generated significant discussion and is likely to be reintroduced in the current Congress. If implemented, it could be a boon to the domestic industries such as steel, which made use of antidumping and countervailing duties cases most frequently.

Biden Administration to Build Momentum for Export Controls Multilateral Agreement

Capstone believes 2023 will mark a pivotal year for the White House in its push to implement its domestic manufacturing strategies to compete against China, with the US increasingly likely to reach a multilateral agreement with key allies on semiconductor-related export controls. However, questions remain on what that framework will look like, how it will be updated over time, and how consistent restrictions will be.

The passage of the funding for the Creating Helpful Incentive for Producing Semiconductors (CHIPS) Act, signed by President Biden on August 9, 2022, presented a tailwind for domestic semiconductor producers, as chipmakers with domestic production capabilities and associated equipment makers stand to benefit from government incentives of up to $3 billion per project, administered and distributed through the Department of Commerce. However, the CHIPS Act is not the end of the story for chipmakers, who will face an uphill battle in 2023.

On October 7, 2022, the US Department of Commerce's Bureau of Industry and Security announced two actions as part of the Biden administration's broader effort to curtail access to advanced semiconductors by the People's Republic of China. The new rules are the result of concerns that have been growing since the beginning of the Trump administration on the Chinese Communist Party's "military-civil fusion development strategy," specifically for artificial intelligence (AI) applications.

Winners and Losers from Adoption of Multilateral Export Controls

Winners	N/A
Losers	ASML Holding NV (ASML), Intel Corp. (INTC), Nvidia Corp. (NVDA), Samsung Electronics Co. Ltd. (005930 on the Korean exchange), Seagate Technology Holdings PLC (STX), SK Hynix, Taiwan Semiconductor Manufacturing Co. Ltd. (TSMC), Tokyo Electron (8035 on the Tokyo exchange)

One of the measures contained sweeping prohibitions and licensing requirements on exports to China of certain semiconductors and related equipment, specifically for advanced computing integrated circuits and supercomputers end-uses (see “US–China Quick Take: Commerce Dept’s Additional Export Controls on Chips Shifts Regime Away from Narrow, Entity-Based Framework,” October 7, 2022).

The October 2022 rules implicated not only the chips as part of an update to the Commerce Control List, but also exports of manufacturing equipment and software necessary for their production. Commerce is implementing a new end-use control based on the Control List, specifically targeting the development of supercomputers. The Commerce Department signaled that companies would face a relatively rigorous process to obtain license approvals, as it would review with a presumption of denial for licenses for exports destined for any of the 28 companies added to the Entity List.

Currently, the US licensing rules directly impact domestic companies by imposing new restrictions on equipment or semiconductor manufacturing items and, in part, can capture only foreign entities. The Foreign-Produced Direct Product Rule (FDPR) subjects goods with a certain degree of US-made parts to the same restrictions when bound for companies that were placed on the Entity List.

Multilateral export controls established through the 1996 Wassenaar Arrangement or a new regime will extend US restrictions to foreign-based companies. BIS viewed the utility of the FDPR as a potential

carrot-and-stick approach, where its unilaterally imposed rules would be relaxed in exchange for adopting similar controls.

At the time, Commerce Department Undersecretary Alan Estevez characterized the unilateral action from the US government as a “downpayment” on its efforts to persuade allies, including the Netherlands and Japan, to adopt similar restrictions and committed to working with these partners for uniform export controls. However, based on public reporting, the Dutch rejected US proposals on two occasions in 2022 before BIS opted tightened export controls unilaterally.

Still, we believe the sentiment for how feasible this type of arrangement generally has shifted positively and favorably for the US government. Because of the developments regarding the receptiveness of US allies to place similar controls on companies in their jurisdictions, we believe it is becoming increasingly probable that the US will create a multilateral agreement on export controls by the end of 2023, though that deal might not go as far as the US would want.

While the Dutch and Japanese governments in December signaled their openness to a multilateral framework and may even have potentially reached an agreement in principle, it remains unlikely that they will adopt rules that are as stringent as the Commerce Department’s October rule. That rule targets equipment capable of producing semiconductors at the 14 nanometer or below level with additional constraints on US persons involved in some of the related work. In contrast, we believe the Dutch government will restrict ASML Holding NV (ASML)’s exports of specific lithography products capable of producing advanced chips, but will stop short of a full export ban.

In the best-case scenario, the US appears to be trying to recreate the Coordinating Committee for Multilateral Export Controls, a defunct group comprised of Western European nations and US allies launched after World War II. This committee maintained three lists of controlled items with a much stronger compliance policy than what is required of Wassenaar Arrangement members. While the US is moving in this direction, as well as continuing to focus on end-use/end-users (rather than lists), plurilateral arrangements that are initiated by the US and specific countries, more limited in reach and relevant solely to the semiconductor space, is more likely before an eventual multilateral venue is created. Reaching these one-off agreements will still take considerable time and effort by the Biden administration.

In November 2022, Commerce Secretary Gina Raimondo suggested that such a process could take six to nine months to finalize. If public reporting about allies’ support as of mid-December is accurate, then we anticipate further details to become available and materialize in H1 2023. We continue to note that the so-called Chip 4 alliance, an initiative announced in March 2022, and includes Japan, South Korea, Taiwan, and the US. Has faced headwinds in moving forward. The alliance has yet to meet or provide additional information on its objective of coordinating policy related to semiconductors. The overall state of the demand cycle and China’s response to US rules with its own industry incentives also could challenge the resolve of US allies to sign on.

The Biden administration’s effort to reach a multilateral agreement on semiconductors and advanced computing will be aided by the Democrat-controlled Senate. Democrats maintaining control means a calmer, more consistent policy environment than would exist if the red wave had materialized in November. The US will be perceived as likely to continue existing policies. Continuity in foreign policy will aid Biden’s attempts to forge agreements with key allies.

After receiving significant benefits from the CHIPS Act, chipmakers in the US must be aware of the challenges that lie ahead. For US firms, the anticipated start of the CHIPS for America Act program and the Commerce Department’s application process by around February 2023 will likely see additional guardrails introduced that they must consider before accepting the potential government funding.

Seagate Serves as a Bellwether for US Export Control Enforcement

We view the fate of Seagate Technology Holdings Plc (STX) and potential fines from an investigation related to accusations of selling hard drives to China's Huawei Technologies as a bellwether for the US enforcement posture of existing export controls. We expect Seagate to face limited fines of around $10 million, given the BIS's long-standing guidance on penalty assessment. However, a higher fine, up to $176 million in a worst-case scenario, would suggest a harsher tone to future enforcement.

Despite the aggressive expansion of export controls, BIS enforcement has been slow. However, in an October 26th regulatory filing, Seagate Technology disclosed a proposed charging letter (PLC) issued by BIS against the company on August 29, 2022, pertaining to hard disk drives (HDDs). Public reporting and an analysis of prior comments made by the company's top executives suggest that Huawei Technologies Co. Ltd. is likely the entity in question. The BIS action is likely a result of public criticism and acknowledgement by the company throughout 2021 regarding Seagate's continued shipments to Huawei, even as other competitors such as Toshiba Corp. (6502 on the Tokyo exchange) and Western Digital Corp. (WDC) ceased theirs.

Most prominently, the Senate Committee on Commerce, Science & Transportation published in October 2021 a detailed report titled "Huawei's Access to Hard Disk Drives in America: An Investigation into Seagate Technology." Senate Republicans, the minority staff at the time, alleged that the company continued to ship prohibited products without a valid license after the placement of Huawei onto the Entity List in May 2019, violating of the foreign direct product rule. Seagate's headquarters are in California, but the company is incorporated in Ireland. Still, many of its products are either directly subject to the US Export Administration Regulations (EAR) or are covered under the Entity List's expansive Foreign Direct Product Rule. That provision extends US jurisdiction over items that are made with a certain amount of US-made inputs. The company is the largest manufacturer of HDDs.

Prior to Seagate, violations of China-related export controls and subsequent enforcement action involving monetary penalties were relatively limited. As a general matter, BIS discloses these proceedings once resolved, but has moved to publish charging letters once issued in the future. In November 2021, BIS disclosed an administrative settlement with SP Industries Inc. that included an $80,000 civil penalty. In that case, the bureau accused the company of exporting items to Huawei and its affiliates, such as HiSilicon Technologies Co. Ltd. through four unauthorized shipments valued at just over $180,000. That case marked the first such action for the new Entity List restrictions placed on Huawei.

According to BIS, EAR violations are subject to both civil and criminal penalties. The former can be as high as the greater of $330,947 per violation, or twice the value of the transaction. While its official

guidance allows for adjustments in either direction based on both aggravating and mitigating factors, the bureau published a memo in June 2022 warning that its Office of Export Enforcement will seek to impose “significantly higher penalties.” However, these fines have been limited in practice. Experts Capstone spoke with were skeptical that BIS will levy a material fine against a US firm.

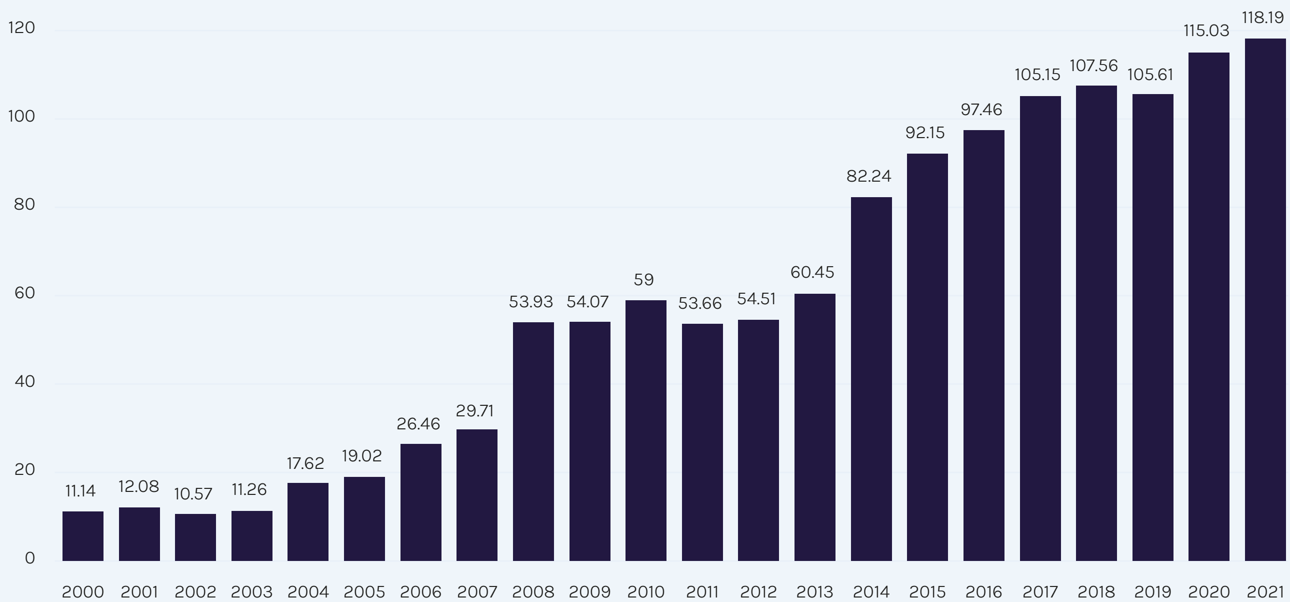
New Bipartisan Scrutiny of Overseas Investment

Capstone believes one of the next regulatory "shoes" to drop will be an outbound investment screening mechanism, which will subject more foreign investments by US companies to a multi-agency review and scrutiny. We expect Congress to debate establishing the mechanism through legislation this session. The Biden administration also could issue an executive order (EO) establishing an investment screening mechanism, but that directive will likely serve as a precursor to legislation that provides firmer statutory authority.

The idea of an outbound investment screening mechanism (sometimes imprecisely referred to as "outbound CFIUS") has bipartisan support in Congress—with the obvious focus being China. In many ways, the policy disagreements at present are not about whether to establish an outbound

DIRECT INVESTMENT FROM THE US IN CHINA, 2000-2021

Direct investment position of the United States in China from 2000 to 2021 (in billion U.S. dollars, on a historical-cost basis)



Source: US Bureau of Economic Analysis via Statista investment screening mechanism but how to do it and what to restrict or review. The return of Republican control over the House only increases the probability of this becoming reality.

DEVIL IN THE DETAILS

There are significant questions right now about exactly what will be included in an EO or final legislation. In recent expert testimony at a US Senate Banking Committee hearing, Capstone Senior Adviser Tom Feddo and others encouraged Congress to deliberate and be cautious in its approach, given the significant business and investment impacts and potential for unintended consequences.

Capstone believes one foundational element that will almost surely be included is a reporting requirement for all private sector entities engaging in certain outbound transactions in "countries of concern." Ultimately, this means reporting on outbound transactions involving China.

The key question will be how reporting requirements will be scoped, both in terms of the sectors and industries included in the definition of a "national critical capability," and the reach of these authorities. For example, will it include only direct investments or third-party investments with relationships in China? Will there be a clear definition of relationships, joint ventures, certain types of contracts, etc.?

In terms of sectors, high-tech areas of the economy such as semiconductors, artificial intelligence, biotech, critical minerals, and clean energy tech are almost certainly being contemplated in either/both an EO and legislation.

Notably, each of these categories, as defined by the White House's Critical and Emerging Technologies List, is broad. An EO, as well as a final bill with greater Democratic influence, also could be scoped to include a broader swath of Chinese manufacturing, with the aim of benefiting US industry and workers.

There will likely be flexibility for the screening mechanism to expand its scope. In terms of the types of "covered activities" that would be subject to US, approval, previous legislative language has included both physical production (for example, "builds, develops, produces, manufactures, manages, operates, sells…" a national critical capability), as well as financial transactions and investments and knowledge transfer/intellectual property broadly defined. Joint ventures and subsidiaries also will likely be considered.

The key question will be how reporting requirements will be scoped.

SWEEPING BUSINESS IMPLICATIONS

Capstone recommends that all our clients track developments in this space. Indeed, Ohio Sen. Brown recently testified on this topic, underscoring the degree to that institutional investors would be scrutinized. "US investments—whether from a venture capitalist or pension fund—could wittingly or unwittingly support foreign technological investments that, in the words of our Secretary of State, could 'increase other countries' technological dependence, and then use that dependence to impose its foreign policy preference," he said.

The national and economic security concerns being addressed here are broad and the business implications are sweeping. They will require many to make change investment and business strategies with an "over-the-horizon" approach to cross-border transactions. Capstone will be tracking this closely in the weeks and months ahead.

TikTok Divestiture from ByteDance Still Most Likely Option

The Republican majority in the House will put additional pressure on the Biden administration to address US vulnerabilities and national security concerns related to China's "military-civil fusion" development involving semiconductors and Chinese social media applications such as TikTok.

Despite growing pressure from Congress and state leaders in the second half of 2022, the Biden administration did not take direct steps to address US concerns regarding TikTok's ownership. Throughout the last year, officials at the US Department of the Treasury said they were conducting an "ongoing security review" and the Committee on Foreign Investment (CFIUS) and the US Department of Justice (DOJ) were locked in negotiations with the company.

Following additional reporting that revived uneasiness within Congress about TikTok's ownership structure, we continue to believe the 2020 presidential order requiring divestiture based on an earlier referral by CFIUS is the most suitable pathway, especially as its ownership remains a key political question.

Over half of US states have banned, fully or in part, the download and/or use of TikTok onto government-owned devices or networks as of February 15, 2023. A large majority of these restrictions came about by executive action by Republican governors. Despite the limited impact this has had on the app itself, pressure snowballed into effectively forcing the federal government to take similar action. On December 14, 2022, the Senate unanimously passed No TikTok on Government Devices Act (S. 1143), originally introduced in August 2020. Its adoption quickly prompted the former House Speaker to seek its inclusion in the omnibus government funding bill. This stands in stark contrast to the stalled efforts for the House's inclusion of a similar mandate in the FY 2021 National Defense Authorization Act more than two years ago.

Winners and Losers from TikTok Divestiture

Winners	Meta Platforms Inc. (META), Snap Inc. (SNAP)
Losers	Privately owned ByteDance/ TikTok Tencent Holdings Ltd. (TCEHY)

The swell in support for “banning” TikTok also led to the introduction of the Averting the National Threat of Internet Surveillance, Oppressive Censorship and Influence, and Algorithmic Learning by the Chinese Communist Party Act (ANTI-SOCIAL CCP Act) by Senator Marco Rubio (R-FL) and Representative Mike Gallagher (R-WI) at the end of the last legislative session. Based on our understanding of the measure, we believe it will compel the president to use powers granted under the International Emergency Economic Powers Act (IEEPA) to “block and prohibit all transactions” involving a social media company domiciled in a country of concern.

That bill, now reintroduced, and a similar one by Sen. Josh Hawley (R-MO) will face significant headwinds, especially in the Democratic-controlled Senate. Furthermore, while both ByteDance and Tencent/WeChat were successful in their efforts to overturn two August 2020 executive orders that President Trump issued under IEEPA, we believe there is a more legally sound option. The president has broad authority to require divestiture as a mitigating measure following CFIUS review to restrict foreign investment in a US business. We believe a separate presidential order using that power under Section 721 of the Defense Production Act for unwinding ByteDance’s acquisition of Musical.ly remains valid. The CFIUS process started following the transaction, which ByteDance did not voluntarily notify the committee about beforehand for review.

The Biden administration’s appetite for enforcing the presidential order and addressing lawmakers’ security concerns is likely to become more evident in 2023. Even as elected officials raise consumer protection questions, the most pressing concern is still about the access and involvement of employees based in mainland China. President Biden is vulnerable to Republican attacks that he is weak on China, especially compared to his predecessor, if his administration either takes no action or produces an agreement that appears weak and we believe divestiture remains his best option.

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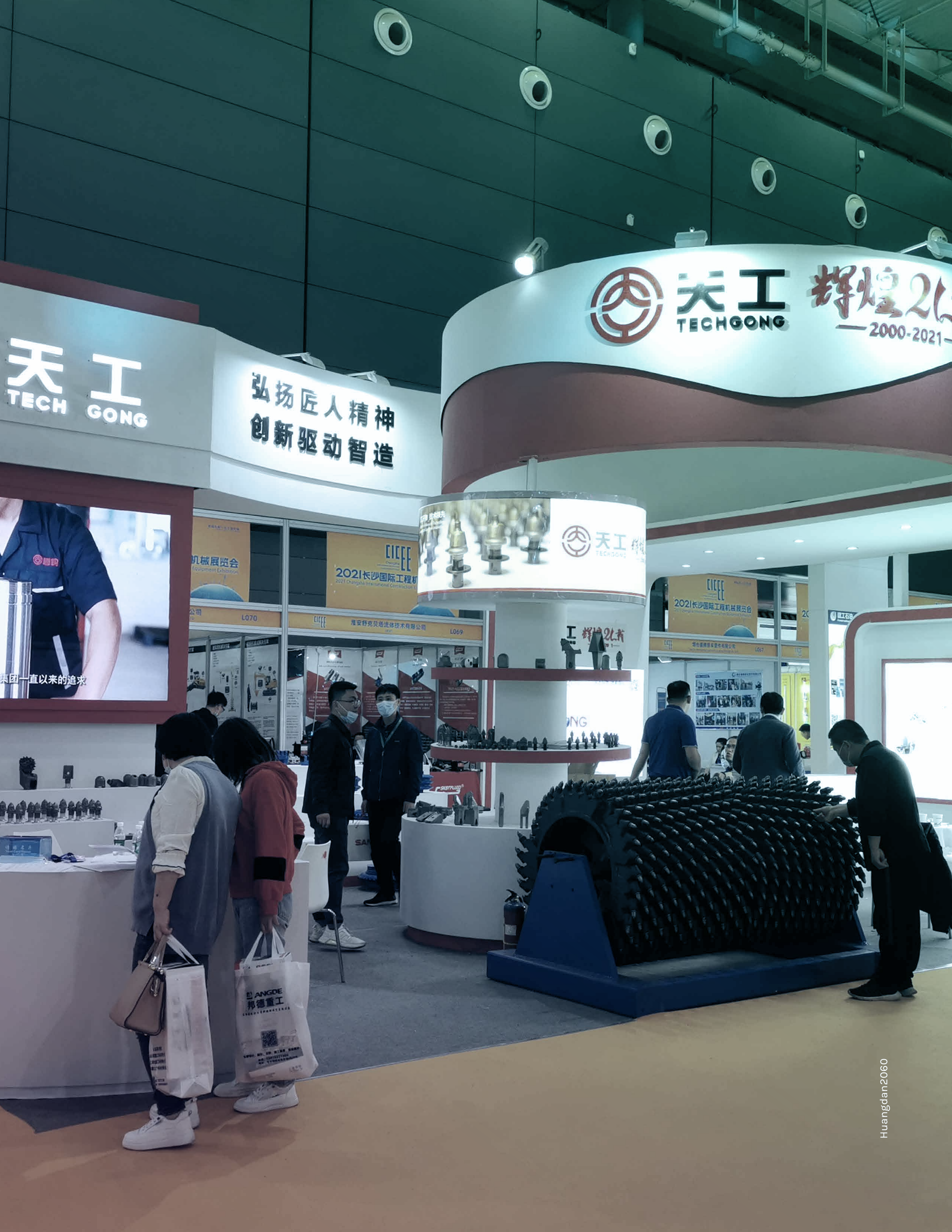

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Expect a Continued Heavy Hand from China in Tech

Capstone believes heavy-handed state regulation of China's tech industry is here to stay, despite broader market expectations that the government's crackdown is near its end. In 2023, China will set and enforce policies that require technological development and innovation to occur hand-in-hand with the state.

Winners and Losers: China's Tech Industry and Regulation	
Winners	Electronics, hardware, parts and components, digital infrastructure, some digital platforms that adapt to CCP regulations and integration, vehicle (EV and driverless), advanced computing manufacturers.
Losers	Some digital platforms, social media, entertainment, gaming companies.

Private companies will have to abide by a higher "new normal" level of state integration in corporate governance and avoid conduct that runs afoul of the regulators or the CCP. They also will be encouraged to innovate as long as they stay in line with CCP objectives. For some companies, this will prove burdensome while for others it will bolster their success.

China will likely limit its highly public IPO-scrapping politics of the past three years due to economic pressures. Instead, the CCP will more quietly move to integrate itself with the private tech sector.

Platform companies will broadly be negatively impacted by greater state involvement. However, some tech giants like Alibaba Group Holding Ltd. (9988 on the Hong Kong exchange) and Tencent Holdings Ltd. (0700 on the Hong Kong exchange) are adapting to the heavy state supervision and integration. That entails cooperating with the state by focusing on products less likely to be subject to domestic political issues (such as computing), and, in some instances, integrating its corporate and operational governance and shedding platform economy investments.

Industrial tech products are the major winners, with China staking much of its future growth on developing products like high-end semiconductors and photonic silicon chips, cloud/quantum/satellite-integrated terrestrial computing, and driverless and EVs. These products will benefit from state investment and industrial policy in 2023. Economic and social pressures are also pushing the CCP to liberalize its Zero COVID regime, bolstering tech manufacturing.

WHAT CHINA WANTS: TECHNOLOGICAL INNOVATION WITH CHINESE CHARACTERISTICS

While many observers claim that China's crackdown on technology companies is nearly over, Capstone believes this is far from true. Following two decades of explosive growth and little regulation of the Chinese "platform economy," an era of heavy state influence and strict regulation in its domestic tech industry has begun. Under the leadership of President Xi, who has made centralizing power and bolstering CCP control of Chinese society the cornerstone of his rule, this trend has little hope of abatement, no matter the economic pressures.

Just as the West looked on with surprise when China's economic liberalization in the 1980s-1990s failed to result in democratization, Capstone believes the CCP also will try to conduct technological development based on the party's political ideology—"Socialism with Chinese characteristics"—at its core. Unlike the West, China does not see state regulation as anathema to technological innovation. Tech companies will be forced to operate within a staunchly Marxist-Leninist socialist market economy, with CCP integration a necessity for any powerful company or product. While the CCP may not be a master at picking winners or fostering innovation, it can make losers of tech giants at a moment's notice

China will set policies that force technological development and innovation to occur hand-in-hand with the state and companies will, as a matter of survival, have to abide by stricter state regulations and incorporate CCP ideology in their products.

How We Got Here: Jack Ma's Hubris and the Rise of Big Tech in China

In 2021 and 2022, the CCP finally began to flex its regulatory muscle following the meteoric rise of Chinese Big Tech companies in global markets. Three or four Chinese tech firms have consistently ranked in the top 10 global technology companies by market cap since 2018, and using the output of the private tech industry has become a near-necessity for day-to-day living in China.

The Chinese tech boom led to the emergence of a powerful tech entrepreneurial class and the permeation of private industry influence and control across nearly all aspects of Chinese society and economy. That influence was manifest in areas that included information flows and communications, detailed data collection at gargantuan scales, and economic necessities including digital payments and travel passes.

Some among the class of powerful tech entrepreneurs did overstep the CCP line, breaching acceptable degrees of outspokenness or power and influence over Chinese society (such as Jack Ma's criticisms of the CCP in 2020). This, coupled with President Xi's fear that a privately owned tech infrastructure that underpinned much of China's society posed a risk of undercutting CCP objectives and state institutions, prompted a crackdown.

The October 2020 suspension of Ant Group's planned initial public offering (IPO) in New York and Hong Kong showed how the CCP, with a wave of its hand, could halt a deal that was expected to raise $34.5 billion (it would have been at the time the world's largest-ever IPO). Similarly, in 2021, the CCP showed tech platforms that it ruled the roost when it suspended ridesharing giant Didi Chuxing (owned by Tencent) from Chinese app stores. Chinese regulators also eliminated the for-profit ed-tech industry in China, imposed onerous licensing requirements for video games—virtually banning violent content—and limited gaming for people younger than 18 to three hours per week. Chinese companies have rushed to file for local IPOs in Hong Kong and Shanghai.


WORLD ECONOMIC FORUM
THE FORUM OF
YOUNG GLOBAL LEADERS
SHAPING THE FUTURE

Today, amid sluggish economic growth and some social and health dilemmas stemming from its Zero COVID policy, China faces ample internal pressure to open up its economy and stimulate private enterprise in 2023. Chinese regulators also have concluded some investigations into technology platforms, including Jack Ma's Ant Group and Tencent's Didi Chuxing, which is a win for Didi Chuxing's shares and the prospects for Ant Group's eventual IPO. However, official Chinese statements, policy planning documents, and draft legislation suggest that these developments should not be taken to mean the CCP will take a hands-off approach when it comes to state control and regulation of the domestic tech industry. China's leaders remain in full control over the mechanisms through which its companies raise money from investors.

Due to economic pressures, Capstone believes China will likely limit its highly public IPO-scrapping politics of the past three years. China likely expects that the domestic signaling and power-play tactics it has employed during the past two years have hampered the ability or willingness of private enterprises to make major moves that could undermine the CCP in the near-term. Instead, the CCP will more quietly move to integrate itself with the private tech sector

CHINA'S DOMESTIC TECH POLICIES: WHAT TO EXPECT

Chinese regulators are considering broad new regulatory regimes to address various tech platform transgressions and limitations, in addition to those introduced this year. (Those include onerous licensing requirements for video games, favoring non-violent, pro-CCP themes.) This is highly likely to include new or updated regulations on:

- Mandated structural changes to corporate governance and ownership from Chinese regulators, including changes in the structure of certain tech companies on an ad hoc basis and state ownership of shares and/or operations of certain companies. For instance, Alipay accepted partial state-ownership, and Tencent has divested from several partially owned platform companies, seemingly to escape the glare of China's regulators. We are likely to see more of this in 2023. Amid US-China technology decoupling, this trend will harm Chinese corporations that want to attract foreign investment or operate internationally, given that links to the CCP increase the likelihood the US will brand them a risk to its national security. In particular, digital financial payments systems such as WeChat Pay and Alipay are likely to experience structural changes as Beijing is worried about their ability to undercut state-owned banks and the Renminbi.

- Mandated full or partial state control related to securitized industrial products (that is, matters of national security) is inevitable. Chipmakers, EV and driverless vehicle manufacturers, quantum computing centers, biotech manufacturers, and digital payments systems all fall under this category. Subsidies for core industrial "winners" such as photonic silicon chips and industrial policy more broadly under Made in China 2025 will supplement China's drive to boost these products.

- Additional regulations (and their implementation) relating to recommendation algorithm design and use. For large Chinese technology firms, the recent revelation that the Cyberspace Administration of China (CAC) has been investigating the algorithms of Alibaba Group, Tencent, and privately held ByteDance (owner of TikTok) served as a cause for concern, among other regulatory themes. The 2022 Provisions on the Administration of Recommendation of Internet Information Service Algorithms are far-reaching and comprehensive, including a mandate that algorithm recommendation service providers "actively disseminate positive energy, and promote the application of algorithms upward and good," to a prohibition of algorithms that "violate public order and good customs, such as inducing users to over-indulge or over-consume" or the use of algorithms to engage in anti-competitive behavior or activities that threaten national security.

- Protections for individuals: Gig-worker protections, privacy protections, international data transfer restrictions, and anti-trust regulations are all being strengthened and will be rolled out in the next one to two years.

- Other emerging tech in the private sector: Deepfake, generative AI, and "metaverse" companies in China will face regulatory scrutiny from the get-go as companies attempt to roll out these products more widely. Web3 is a non-starter for the Chinese government given its decentralized, user-controlled infrastructure. It will inevitably run into regulatory hurdles, though no timing has been indicated by regulators.

Implementation

Chinese technology law tends to be vague and sweeping, allowing the government to prosecute cases as it wishes. The precise terms of the regulations are not what matters most. Instead, regulations serve as a deterrent against transgressions and as a broadly permissive tool for regulators to crack down on the most powerful players if deemed necessary.

Companies that cannot easily adapt their business models to meet CCP requirements will struggle in this new environment and risk losing sizable profits. For some, stricter standards mean limiting customer- and sales-focused innovation of their products, while greater state involvement in operational activities tends to create difficulties in day-to-day product functionality.

CHINA'S ECONOMIC PRIORITIES FOR 2023: WHERE DOES TECH FIT IN?

China held its annual Central Economic Work Conference (CEWC) in December 2022, during which the economic priorities of the year were laid out in broad terms (to be followed by a tangible work program in early 2023).

It is clear from official state documents that there is anxiety within the CCP about the economic and social pressures that China currently faces amid the spread of COVID-19 and the economy's declining growth rate. There also is immense pressure on the state to quickly find a remedy for the situation. Capstone believes China will try to use industrial technology policy as a core driver of economic growth in 2023 but will not significantly ease up on the platform economy, despite an emphasis on private sector innovation.

The CEWC identified industrial technology policy as a core economic priority for 2023 and in the longer term. It stated that China aims "to accelerate the construction of a modern industrial system." A key focus will be development of the "weak links in parts and components," giving "full play to the organizational role of the government in key core technological breakthrough" while also "highlighting the dominant position of enterprises in scientific and technological innovation."

The CEWC also stated the need to support platform technologies' leadership in development, job creation, and global competition. While some observers have taken this to mean the end of Big Tech regulation has arrived, we believe this is unlikely, but may mean a slowdown in the highly public IPO-scrapping politics of 2021-2022. There will likely be fewer publicized crackdowns on tech giants, with companies now better attuned to the ramifications of shunning local regulations or overstepping the party line, having learned from Alibaba co-founder Jack Ma's example. This is a positive for several of the largest technology platforms, including Ant Group, Alibaba, Tencent, Meituan, among others, that have come under substantial pressure during the past two years.

With China's authorities having inculcated that adhering to the state's interests is a key goal for corporate enterprises, they are seeking ways to grow the economy within that framework. This has led the leadership's recent decision to publish new draft rules reforming the market for domestic initial public offerings. We expect the rules to be implemented in the first half of 2023 and to be most beneficial for smaller Chinese firms in strategic industries, which are generally unimpeded by state intervention. The new rules will make it easier for these companies to raise money and also play an important role in stimulating China's economy as it tries to rebound from COVID's impact.

While the rules are likely to stimulate IPO activity, China's efforts to revive its finance sector will be hampered by US crackdowns on technology companies—many firms are likely to be dissuaded from filing for IPOs while under foreign scrutiny

The CCP has a clear bent toward attracting more foreign investment and stimulating private enterprise and consumer spending in the coming year—all of which will benefit Big Tech. A return to more normal levels of economic activity also is expected as Zero COVID restrictions ease. However, these tech giants still will have to manage a prolonged internal struggle to maintain pace with CCP regulations and greater state involvement in corporate decision-making.

INDUSTRIAL GOODS TO FAREWELL UNDER DOMESTIC INDUSTRIAL POLICY

Capstone believes that industrial "bread-and-butter" technologies of the 21st century, including Chinese electronics, hardware, components, computing, and vehicle (EVs and driverless) manufacturers, will fare well from a domestic regulatory standpoint. China is heavily invested in the success of products that will drive its geopolitical ambitions. These companies, however, will continue to bear the burden of coercive economic and national security policies from the US The CCP's policy direction for 2023 states that "industrial policy should be developed simultaneously with security," suggesting a high level of state involvement.

Beijing has focused much of its tech crackdown on Big Tech, digital platforms, and entertainment companies that were becoming too powerful in their influencing power over Chinese citizens, working against CCP control rather than for it. On the contrary, China sees hardware manufacturing and computing as the metaphorical oil of the 21st century: the industrial bread and butter of China's future economic growth and geopolitical power. These industries have also stayed away from products that go against CCP preferences. In addition, e-games are seen as corrupting youth, social media as feeding citizens influential information and potentially fueling anti-government sentiment, and digital payments as undercutting core state functions.

Beijing therefore will try to ensure that entrepreneurship and innovation are fostered in this domain and will invest heavily in Chinese alternatives to foreign advanced computing and semiconductor products. Beijing plans to bolster investment in Shenzhen and Guangzhou "innovation corridors," considered to be China's Silicon Valley, to support its Made in China 2025 goals.

We are likely to see more digital platform companies move into this space, too. Superapps such as Tencent and Alibaba are moving into product categories that were formerly considered to be industrial goods; for instance, working on producing photonic silicon chips, satellite-terrestrial integrated computing, or vehicles (electric and driverless).

THE CONFOUNDERS: WHAT COULD CHANGE PREDICTED OUTCOMES FOR CHINESE TECH

Zero COVID

Regardless of what COVID-19 policy China follows, it will have a tough year ahead economically and socially.

Capstone believes China will ease some but overall maintain significant COVID-19 lockdown measures to limit the impact on the Chinese health system. Another mass vaccination effort is likely to ensue, even as vaccination hesitancy among the Chinese populace is high. It is possible that President Xi also

will strike a deal with European partners to import mRNA vaccines to help boost immunity among the Chinese population. The current scientific literature suggests that the top Chinese vaccines (CoronaVac and Sinopharm) have been roughly as effective as mRNA vaccines at protecting against severe COVID-19, but not as effective at preventing infection.

Industrial manufacturers will continue to be hit hard if lockdowns persist. There may be fewer rewards to be reaped from favorable industrial policies toward manufacturers if factories and R&D facilities are closed, or if workers revolt amid poor working conditions (think Foxconn factories). Much of the platform economy that depends on day-to-day economic activity also will depend on the extent of lockdowns. If China relaxes restrictions, it could experience a health crisis that similarly heavily impacts the economy writ large.

US Economic Coercion

China's domestic technology policy for 2023 may be a boon for some companies and industries, but these industries could lose business from foreign investors and consumers in 2023 if they are targeted by US tech decoupling policies (see "US-China Tech 2023 Preview: Biden Administration to Build Momentum for Export Controls Multilateral Agreement, Face Pressure to Act on TikTok," December 22, 2022). In fact, those industries most likely to be favored by China's domestic policies usually manufacture highly strategic products that are most likely to be targeted by the US (hardware, semiconductors, etc.). Investors will have to balance the net gain of those industries from domestic subsidies and other favorable policies from Chinese regulators, with the negative impacts of US tech decoupling and coercive economic policies.

About Capstone

Capstone is a global, policy-driven strategy firm helping corporations and investors navigate the local, national, and international policy and regulatory landscape.

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Authors:

David Barrosse
CEO
Capstone

JB Ferguson
Managing Director
Tech, Media & Telecom

Daniel Silverberg
Managing Director
Corporate & National Security

Sebastiaan Bierens
Director
Financial Services

Andrew Gier, CFA
Director
Energy & Industrials

Elena McGovern
Director
Private Markets

Ian Tang
Vice President
Tech, Media & Telecom

Thomas Feddo
Senior Adviser
Capstone

Gabe Armstrong-Scott
Fellow
Tech & National Security

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capstonedc.com
(202) 449-9862