

ISSUE BRIEF

China and the New Globalization

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The unitary globalized economy no longer exists. Driven in significant part by security considerations, a new and more diverse globalization is both required and being built. The transition is ongoing, and its final form is yet to be determined. Many of the causal factors for this very significant change revolve around China and the consequent responses to its actions by the United States, other democracies of the transatlantic alliance, and the advanced democratic economies of the Indo-Pacific. There are other important factors generating this new globalization including the impact of the Russia-Ukraine war both on energy markets and on trade and investment with Russia generally, as well as the global requirements for mitigating and adapting to climate change. However, China has been a critical element in what might be described as the "maximum trade-centered globalization," which has dominated trade and investment policy in the three decades since the end of the Cold War.

This issue brief describes the still-developing new globalization focusing on the issues surrounding China. A fundamental challenge that China presents arises because its actions have generated significant security and economic challenges, yet it nonetheless is a massive trade and investment partner for the “advanced democratic economies” (ADEs),¹ which for purposes of this analysis include the Group of Seven (G7) countries,² plus Australia, Norway, the Republic of Korea, and the European Union. Adapting to a new globalization requires establishing a strategic approach that resolves the inherent contradictions between those conflicting considerations.

The brief begins by setting forth the ongoing changes in China that have significantly affected global geopolitical and geoeconomic environments including the increased emphasis by the Chinese Communist Party (CCP) on the role of the state and on economic self-reliance. China is an ever more ideological environment generating a higher degree of economic and security risks including over Taiwan.

The brief then discusses the advanced democratic economies, first focusing on the United States including the US emphasis on national security concerns, and then reviewing the policies of other advanced democratic economies, especially issues regarding economic dependencies. The United States has put in place significant limitations on trade and investment with China and, at the same time, expanded its security and economic cooperation with Taiwan. The other ADEs have established frameworks or taken other economic and security measures affecting their relations with China, though, for the most part, not with the degree of restrictions undertaken by the United States.

The brief concludes with recommendations for the United States and the other ADEs for responding to China in transi-

tioning to the new globalization with an objective of establishing “free but secure trade,” as identified by US Treasury Secretary Janet Yellen.³ Critical to the success of this new globalization approach will be:

- ◆ Undertaking selective decoupling from China as particularly relevant to each ADE’s national security requirements; advanced and emerging technologies; and critical infrastructure resilience.
- ◆ Establishing resilient supply chains outside China including in and among the United States and other advanced democratic economies and through “friendshoring,”⁴ i.e., with reliable partners in the Global South; utilizing incentives including tax credits, subsidies, and concessional financing in order to reduce dependencies on China; and developing a critical minerals financing initiative focused on enhancing the transition to clean energy and providing alternatives for other sectors such as defense.
- ◆ Expanding the G7 to a “G10-plus” of the advanced democratic nations, which would coordinate intelligence and economic and security interactions with China among the ADEs including through the establishment of a multinational staff.

Successfully undertaking selective decoupling and establishing resilient supply chains as the substantive cornerstones of the new globalization will require a multiyear effort that should be undertaken in prompt coordinated fashion through the G10-plus so as to accomplish the requisite security and economic objectives of the ADEs.

1 The ADEs are liberal democracies with advanced economies.

2 The members are Canada, France, Germany, Italy, Japan, the United Kingdom, and the United States.

3 “Remarks by Secretary of the Treasury Janet L. Yellen on Way Forward for the Global Economy,” Department of the Treasury, Press Release, April 13, 2022, <https://home.treasury.gov/news/press-releases/jy0714>.

4 “Remarks by Secretary of the Treasury Janet L. Yellen at Microsoft in New Delhi, India,” Department of the Treasury, Secretary Statement and Remarks, November 11, 2022, <https://home.treasury.gov/news/press-releases/jy1096>.

I. CHINA'S ONGOING TRANSITION: THE STATE AND SELF-RELIANCE

The ongoing changes in China's approach to economics and security under Xi Jinping are having the consequence of making the country less central to and posing greater risks for the global economy than has been the case for many years. China's changed policies, as underscored by the recent Chinese Communist Party congress and the revised CCP constitution, now include a substantially increased role of the state, a focus on self-reliance, and a willingness to put economic development behind other interests. Those factors have coupled with concerns of the United States—shared at least in part by the transatlantic allies and others with advanced democratic economies (ADEs)—arising from issues of security, unfair competition, strategic dependencies, and human rights. Security considerations, in particular, are much heightened and the prospect of conflict over Taiwan now looms larger. In combination, this multiplicity of concerns has affected economic interactions with China. To be sure, China is still—and will remain—an important participant in the global economy. For the ADEs, however, five overlapping factors have combined to require that economic interactions with China receive more thoughtful analysis and an appropriate degree of circumspection.

First, China's economic policy has now been well described as “politics in command”;⁵ the state and particularly the CCP are in control, and China consequently is less oriented to being a market-driven economy. As Dexter Tiff Roberts has written:

Beijing is intent on strengthening control over private companies and foreign investment, reserving set shares of its market for indigenously produced technologies like semiconductor chips and electric vehicle

batteries, and boosting the role of state-owned firms. It is all part of what can be considered a new form of state capitalism, defined by a top-down approach to the economy featuring government-directed and supported industrial policies with the goal of creating a far more self-sufficient country . . .⁶

In principle, this is not an entirely new idea for China as the Chinese Communist Party has always been in ultimate control, but in practice it is a substantial deviation from the Deng Xiaoping approach of “reform and opening up” and instead reflects a Mao-era requirement: “all enterprises must persevere in putting proletarian politics in command and ideological and political work first.”⁷

Findings from the recent China Pathfinder Annual Scorecard underscore these points:

At the Sixth Plenum in November 2021, the Chinese Communist Party (CCP) said the country had entered a “new era” under Xi Jinping, emphasizing the CCP's leading role in steering long-term strategy. For domestic and foreign observers, this sent a clear signal that market-oriented policy reform is taking a back seat to ideological imperatives⁸

As a result, China's state-owned enterprises can be expected to maintain their very significant role:

For China, 43.6 percent of its top ten companies were [state-owned enterprises]. This is, unsurprisingly, considerably above the open-economy average of 2 percent. SOEs' role in China's economy is one of the key

5 Dexter Tiff Roberts, “Xi Jinping's Politics in Command Economy,” Issue Brief, Atlantic Council, July 2021, 1, <https://www.atlanticcouncil.org/wp-content/uploads/2021/07/Xi-Jinpings-politics-in-command-economy.pdf>.

6 Roberts, “Xi Jinping's Politics,” 1.

7 Document of the Politburo of the Chinese Communist Party, September 2, 1975, quoted by Kenneth Lieberthal, James Tong, and Sai-cheung Yeung in *Central Documents and Politburo Politics in China* (Ann Arbor: University of Michigan Press, 1978), doi:10.3998/mpub.2002; and cited in Roberts, “Xi Jinping's Politics,” 1. Xi's decision to emphasize concerns regarding market liberalism was underscored early in his tenure in the April 2013 presentation of “Document 9,” which included among seven “false ideological trends, positions, and activities” that “Western countries, led by the United States . . . aim to change our country's basic economic infrastructure and weaken the government's control of the national economy.” See “Document 9: A ChinaFile Translation,” ChinaFile (online magazine), Center on US-China Relations at Asia Society, November 8, 2013, <https://www.chinafile.com/document-9-chinafile-translation>.

8 Atlantic Council and Rhodium Group, *China Pathfinder: Annual Scorecard*, October 2022, 8, <https://www.atlanticcouncil.org/in-depth-research-reports/report/china-pathfinder-2022-annual-scorecard/>.

differences between the Chinese system and market economies.⁹

This emphasis on state-owned enterprises exists despite the “average profit margins and return on assets show[ing] that Chinese SOEs are still extremely inefficient and not very profitable.”¹⁰ By contrast, private-sector firms have received intense scrutiny including multiple acquisitions by SOEs,¹¹ crackdowns on leading companies such as Alibaba,¹² and effective termination of the private tutoring industry.¹³

Similarly, the strict implementation of the zero-COVID policy, then followed by the abrupt order to drop many of its elements, are reflective of the significant political control over the economy that the Chinese leadership exerts,¹⁴ as does the acquisition of “golden shares” in key companies, discussed further below.

It is accurate to say that in recent weeks there has been a change in tone by the government with language of a more business-friendly approach. But that does not alter the systemic control that the state maintains. As reported by the *New York Times*:

Xiang Songzuo, a Chinese economist and a former official at the People’s Bank of China, said he did not think

that fundamentally there had been a major change in the Chinese leaders’ approach to business, but that their language had softened because of the sluggish economy.

In the current economy, China needs private firms to invest more, hire more and pay more in taxes. As a result, the tone has changed to “reassure and pacify them,” Mr. Xiang said. But tension remains because China wants to maintain control over private companies and will not entrust oversight purely to the markets or existing laws.¹⁵

Second, China is seeking a much greater degree of “self-reliance”¹⁶ through its “dual circulation” strategy. Initially described by Xi in May 2020, the dual circulation strategy was “incorporated into China’s central economic blueprint, the 14th Five Year Plan in March 2021, cementing its high-level status.”¹⁷ The strategy seeks to put significantly heavier reliance on China’s domestic market as compared to its long-standing export-driven approach.¹⁸ Key elements include reducing “external demand as a driver of economic growth by boosting domestic consumption,” attaining “higher levels of self-sufficiency in key areas by enhancing innovation,” ensuring “access to critical inputs by diversify-

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- 9 Atlantic Council and Rhodium Group, *China Pathfinder*, 21. The state’s control over financial institutions offers one important example: “Our indicator measures the degree of state ownership in the country’s top ten financial institutions by market capitalization. For each country, we look at the proportion of each institution’s public stock owned by the government. . . . We see a high degree of polarization within the results for this indicator, with a weighted average government ownership proportion of 39.01 percent for China in 2021 compared to the open-economy average of 3.36 percent. . . . This degree of state involvement in finance has been, and remains, one of the core systemic differences between China’s system and that of open economies.” See *China Pathfinder*, 12.
- 10 Maya Mei, “Fortune Favors the State-Owned: Three Years of Chinese Dominance on the Global 500 List,” *Trustee China Hand* (blog), Center for Strategic and International Studies (CSIS), October 7, 2022, <https://www.csis.org/blogs/trustee-china-hand/fortune-favors-state-owned-three-years-chinese-dominance-global-500-list>.
- 11 According to a *New York Times* article, “from 2019 to 2021, state-owned enterprises acquired more than 110 publicly traded Chinese companies, valued at more than \$83 billion. . . . Such acquisitions were rare before Mr. Xi took over in 2012.” See Daisuke Wakabayashi, Chang Che, and Claire Fu, “In Xi’s China, the Business of Business Is State-Controlled,” *New York Times*, October 17, 2022, <https://www.nytimes.com/2022/10/17/business/china-xi-jinping-business-economy.html>.
- 12 Canghai Chen, “The Real Cause of China’s Alibaba Crackdown,” *Diplomat*, September 9, 2021, <https://thediplomat.com/2021/09/the-real-cause-of-chinas-alibaba-crackdown/>.
- 13 Alexander Chipman Koty, “More Regulatory Clarity After China Bans For-Profit Tutoring in Core Education,” *China Briefing Magazine*, Dezan Shira & Associates, September 27, 2021, <https://www.china-briefing.com/news/china-bans-for-profit-tutoring-in-core-education-releases-guidelines-online-businesses/>.
- 14 Chang Che, Amy Chang Chien, and Alexandra Stevenson, “What Has Changed About China’s ‘Zero Covid’ Policy,” *New York Times*, December 7, 2022, <https://www.nytimes.com/2022/12/07/world/asia/china-zero-covid-changes.html>.
- 15 Daisuke Wakabayashi and Claire Fu “From Disciplinarian to Cheerleader: Why China Is Changing Its Tone on Business,” *New York Times*, January 12, 2023, https://www.nytimes.com/2023/01/12/business/china-economy.html?smid=tw-share&utm_source=substack&utm_medium=email
- 16 Adam Segal, “China’s Move to Greater Self Reliance,” *China Leadership Monitor*, December 1, 2021, <https://www.prcleader.org/segal>.
- 17 ChinaPower Project, “Will the Dual Circulation Strategy Enable China to Compete in a Post-Pandemic World?,” CSIS, December 15, 2021, <https://chinapower.csis.org/china-covid-dual-circulation-economic-strategy/>.
- 18 As the ChinaPower analysis describes: “The DCS comprises two main components: the internal (domestic) circulation and external (international) circulation. The overarching goal of the DCS is to enable the internal and external markets to reinforce and sustain the other, with a focus on establishing the domestic market as the primary driver of economic development.” See ChinaProject, “Will the Dual Circulation Strategy Enable China?”

ing supply chains,” and positioning China as a “global manufacturing powerhouse in high value-added products.”¹⁹

Two critical elements of this approach are the focus on advanced and emerging technologies as exemplified by the Made in China 2025 plan and the very substantial subsidies that China provides to its companies:

- ◆ Made in China is focused on “leapfrogging into emerging technologies . . . reducing reliance on foreign firms . . . [with] breakthroughs in 10 sectors [and for] China . . . to lead at each point in the value chain,” according to a Congressional Research Service report.²⁰
- ◆ China’s state-provided subsidies are far in excess of any such actions by the advanced democratic economies, according to Gerard DiPippo et al.:

Even using a conservative methodology, China’s industrial policy spending is enormous, totaling at least 1.73 percent of [gross domestic product] in 2019. This is equivalent to more than \$248 billion at nominal exchange rates and \$407 billion at purchasing power parity exchange rates. This is higher than China’s defense spending for 2019, which the Stockholm International Peace Research Institute (SIPRI) estimated at \$240 billion at nominal exchange rates. Alternative data and assumptions, including for China’s below-market credit, subsidies to non-listed private firms, government guidance funds, and state-owned enterprise net payables, would result in larger aggregate estimates.

Even with such a low-end estimate, China is an outlier; it spends far more on supporting its industries

than any other economy in this study. As a share of GDP, China spends over twice as much as South Korea, which is the second-largest relative spender in the sample. In dollar terms, China spends more than twice as much as the United States.²¹

A third feature of China’s “new development pattern”²² is an emphasis on the establishment of party organizations in both state-owned and private enterprises. Such activities are specifically provided for in the CCP constitution, which states:

A primary-level Party organization shall be formed in any enterprise . . . where there are three or more full Party members. . . . Primary-level Party organizations [in state-owned enterprises] shall guarantee and oversee the implementation of the principles and policies of the Party and the state within their own enterprises and shall support the board of shareholders, board of directors, board of supervisors, and manager (or factory director) in exercising their functions . . . and shall participate in making decisions on major issues in the enterprise. . . . Primary-level Party organizations in non-public sector enterprises shall implement the Party’s principles and policies . . .²³

As a matter of fact, these party activities appear to be prevalent in larger enterprises but may not be so substantial in smaller ones.²⁴ However, since as a general proposition, it is larger firms from the ADEs that undertake the most significant activities in China, there should be an expectation of CCP involvement. That, however, is hardly conducive to the normal business approach taken by the private sector

19 ChinaProject, “Will the Dual Circulation Strategy Enable China.”

20 Karen M. Sutter, “‘Made in China 2025’ Industrial Policies: Issues for Congress,” Congressional Research Service, InFocus Brief IF10964, updated August 11, 2020, 1, <https://crsreports.congress.gov/product/pdf/IF/IF10964/6>.

21 Gerard DiPippo, Ilaria Mazzocco, and Scott Kennedy, Red Ink: Estimating Chinese Industrial Policy Spending in Comparative Perspective, eds. Scott Kennedy and Matthew P. Goodman, CSIS, May 2022, 2, https://csis-website-prod.s3.amazonaws.com/s3fs-public/publication/220523_DiPippo_Red_Ink.pdf?LH8ILLKWz4o.bjrwNS7csuX_C04FyEre.

22 “Opinion: How China’s New Development Pattern Helps Empower Global Recovery,” Xinhuanet, December 18, 2020, http://www.xinhuanet.com/english/2020-12/18/c_139600803.htm.

23 Articles 30 and 33, Full Text of Constitution of Communist Party of China, Xinhuanet, October 22, 2022, http://eng.chinamil.com.cn/view/2022-10/27/content_10195159.htm.

24 An analysis by Neil Thomas in 2020 stated: “Party organizations are more pervasive in big companies, present in 92.4% of China’s top 500 private enterprises, according to ACFIC’s 2019 ‘Top 500’ annual report . . . This coverage has held steady at 92-93%, but could increase further now that Beijing has made these committees mandatory for *listed companies*.” By contrast, a 2022 analysis by Colin S. C. Hawes states that “if we calculate the percentage of CPC branches within Chinese private firms as a whole (rather than merely in large firms), it is currently only around 7%.” See Thomas, “Party Committees in the Private Sector: Rising Presence, Moderate Prevalence,” Commentary, MacroPolo (Paulson Institute think tank), December 16, 2020, <https://macropolo.org/party-committees-private-sector-china/?rp=e>; and Hawes, “Has the Communist Party of China (CPC) Increased Its Control Over Private Corporations?”, fifteen eightyfour (blog), Cambridge University Press, August 23, 2022, <https://www.cambridgeblog.org/2022/08/has-the-communist-party-of-china-cpc-increased-its-control-over-private-corporations/>.

in the ADEs. As an analysis from an investment advisory firm stated:

The notion that a political party, especially one dedicated to communism, should seek to embed itself in companies and exert control from within is antithetical to American notions of capitalism. American companies operating within China and American investors in Chinese companies are faced with the unsettling prospect of a CCP organization inside their company with an unclear agenda and overlapping lines of authority with the company's managers. There is limited transparency over how party organizations make decisions, what aspects of a company they seek to control, what accountability—if any—they have to a company's shareholders, and what information they may be sharing with outside parties.²⁵

A related development to enhance state control is the acquisition of “golden shares” in Chinese private companies by the government or SOEs that provide “board seats and/or veto rights for key business decisions.”²⁶ Chinese regulators including the Cyberspace Administration and state-owned firms are seeking golden shares in data-rich Internet and technology firms, especially those organizing, structuring, and labeling content; these shares “give special powers to the shareholder like veto power over changes to the company's charter, and even the ability to block other shareholders from holding more than a particular ratio of the company's ordinary shares.”²⁷ As of this writing, the state is taking golden shares in Alibaba and Tencent, two of China's largest technology companies, and has previously acquired such shares in ByteDance (TikTok's parent company) and Weibo (social media), “usually involving a 1 per cent share of internet groups' key [subsidiary] entities.”²⁸

As one person knowledgeable about the Tencent transaction stated, “The state is not going away, this is the trend for the future.”²⁹

Fourth, China's military-civil fusion doctrine raises issues for economic engagement in China by companies from the ADEs. Military-civil fusion is what it sounds like: a whole-of-nation attempt “to create and leverage synergies between defense and commercial developments, particularly in emerging technologies such as artificial intelligence and biotechnology.”³⁰ The important issue that the military-civil fusion doctrine raises is that economic involvement by private-sector companies from the ADEs in China might support—even if inadvertently—important development by the People's Liberation Army, particularly through trade and investment in dual-use technologies. That concern is not speculative. As a recent analysis by the Washington Post found:

Military research groups at the leading edge of China's hypersonics and missile programs—many on a U.S. export blacklist—are purchasing a range of specialized American technology, including products developed by firms that have received millions of dollars in grants and contracts from the Pentagon . . .

The advanced software products are acquired by these military organizations through private Chinese firms that sell them on despite U.S. export controls designed to prevent sales or resales to foreign entities deemed a threat to U.S. national security, the investigation shows.³¹

Fifth, the recent changes to the CCP constitution underscore a more aggressive approach to Taiwan, adding to

25 “Party Committees in Chinese Companies,” *Prevailing Winds* (blog), Seafarer Funds, June 2021, <https://www.seafarerfunds.com/prevailing-winds/party-committees-in-chinese-companies/>.

26 “China Takes Stakes in Private Data Companies,” *Asia Financial* (website), Fintech (vertical), December 16, 2021, <https://www.asiafinancial.com/china-takes-stakes-in-private-data-companies>.

27 ANI Asia, “China: Govt Buying Stakes in Tech Firms to Increase Its Influence,” *Business Standard*, March 26, 2022, https://www.business-standard.com/article/international/china-govt-buying-stakes-in-tech-firms-to-increase-its-influence-122032600263_1.html#:~:text=Golden%20shares%20are%20types%20of,%20the%20company's%20ordinary%20shares.

28 Ryan McMorro, Qianer Liu and Cheng Leng, “China moves to take ‘golden shares’ in Alibaba and Tencent units,” *Financial Times*, January 12 2023, <https://www.ft.com/content/65e60815-c5a0-4c4a-bcec-4af0f76462de>

29 *Id.*

30 Elsa P. Kania, “In Military-Civil Fusion, China Is Learning Lessons from the United States and Starting to Innovate,” *Strategy Bridge* (nonprofit organization), August 27, 2019, <https://thestrategybridge.org/the-bridge/2019/8/27/in-military-civil-fusion-china-is-learning-lessons-from-the-united-states-and-starting-to-innovate>. It is perhaps worth noting that such an approach is hardly surprising. The United States and its allies and close partners all rely on the private sector; the “defense industrial base” is a critical element of national defense strategy.

31 *Cate Cadell and Ellen Nakashima*, “American Technology Boosts China's Hypersonic Missile Program,” *Washington Post*, October 17, 2022, <https://www.washingtonpost.com/national-security/2022/10/17/china-hypersonic-missiles-american-technology/>.

both military and economic risks. The newly amended constitution now sets forth the CCP commitment to “resolutely oppose and deter . . . ‘Taiwan independence’” to “achieve reunification of the motherland,”³² including through strengthening the Chinese military. As an analysis by Mariah Thornton states:

The amendment against Taiwanese independence . . . demonstrates a significant escalation in cross-strait relations in two ways. First, the Chinese leadership is establishing a stronger legal basis from

which it will likely pursue harsher, more punitive action toward any perceived expressions of Taiwanese independence or external support for Taiwanese independence. . . . Second, the amendment signals Xi’s intention to cement fierce opposition to Taiwanese independence as part of the fundamental position of any successive regimes.³³

In sum, China has taken a number of consequential actions that have changed the nature of its relationships with the advanced democratic economies.

32 Full text of Constitution of Communist Party of China, Xinhuanet.

33 Mariah Thornton, “China’s 20th Party Congress Escalates Cross-Strait Tensions,” *Diplomat*, October 27, 2022, <https://thediplomat.com/2022/10/chinas-20th-party-congress-escalates-cross-strait-tensions/>.

II. THE CHANGING ADEs

In the past several years, the advanced democratic economies have significantly changed their approaches to globalization in important part because of the changes by China described above.

A. United States

The global engagement of the United States has been importantly affected by a combination of factors. National security considerations have taken on increased importance, the relationship between economics and security has received heightened attention, concern over dependencies has received added scrutiny, and significant efforts are being taken to support the US domestic economy. The results for this new globalization have been substantial.

First, the US approach to globalization now includes a very substantial domestic element as a key part of the policy. The Biden administration has been clear that “to succeed abroad, we must invest in our innovation and industrial strength, and build our resilience, at home.”³⁴ The implementation of this domestic aspect of the 2022 US *National Security Strategy* is reflected in the hundreds of billion dollars enacted by the combination of the Infrastructure Investment and Jobs Act,³⁵ the Chips and Science Act,³⁶ and the Inflation Reduction Act,³⁷ each of which contains significant funding for investment designed to “onshore” and support the development of key technologies and industries. There is a focus on “strategic sectors and supply chains, especially critical and emerging technologies, such as microelectronics, advanced computing, biotech-

nologies, clean energy technologies, and advanced telecommunications,”³⁸ as exemplified by the multibillion dollar funding for semiconductor fabrication and the development of hydrogen hubs.³⁹

Second, China has been identified as presenting a very significant challenge as the “PRC is the only competitor with both the intent to reshape the international order and, increasingly, the economic, diplomatic, military, and technological power to do it.”⁴⁰ The *National Security Strategy* makes clear the scope of China’s ambition and the breadth of its activities:

Beijing has ambitions to create an enhanced sphere of influence in the Indo-Pacific and to become the world’s leading power. It is using its technological capacity and increasing influence over international institutions to create more permissive conditions for its own authoritarian model, and to mold global technology use and norms to privilege its interests and values. Beijing frequently uses its economic power to coerce countries. It benefits from the openness of the international economy while limiting access to its domestic market, and it seeks to make the world more dependent on the PRC while reducing its own dependence on the world.⁴¹

It is worth underscoring the military aspects of the challenge. The US Department of Defense describes China as the “pacing challenge” inasmuch as the “PRC is also investing in a military that is rapidly modernizing, increasingly capable in the Indo-Pacific, and growing in strength and

34 White House, National Security Strategy, October 2022, 11, <https://www.whitehouse.gov/wp-content/uploads/2022/10/Biden-Harris-Administrations-National-Security-Strategy-10.2022.pdf>.

35 Infrastructure Investment and Jobs Act, Pub. L. No. 117–58, 135 Stat. 429 (2022), <https://www.congress.gov/117/plaws/publ58/PLAW-117publ58.pdf>.

36 CHIPS Act of 2022 and the Research and Development, Competition, and Innovation Act, Divisions A and B, Pub. L. No. 117–167, 136 Stat. 1372 (2022), <https://www.congress.gov/117/plaws/publ167/PLAW-117publ167.pdf>.

37 Inflation Reduction Act of 2022, Pub. L. No 117–169, 136 Stat. 1818 (2022), <https://www.congress.gov/117/plaws/publ169/PLAW-117publ169.pdf>.

38 White House, National Security Strategy, 11.

39 These efforts are a very decided change from the approaches of prior administrations (both Democratic and Republican) that were substantially laissez-faire and led to the relocation (i.e., offshoring) of important industries and supply chains such as for information technology. Among the many analyses of this trend, a 2022 Big Data China piece by Scott Kennedy and Ileana Mazzocco found that “in the decade leading up to 2010 . . . increased imports from China hurt employment and wages in regional labor markets that were more exposed to import competition with China. In other words, areas with a high concentration of manufacturing-based industries that were in direct competition with Chinese companies experienced a fall in employment and wages.” Further, the “regions affected by the import competition with China have struggled to recover a decade later”; that regional employment issue has been a significant policy driver for both the current and prior administration. See Kennedy and Mazzocco, “The China Shock: Reevaluating the Debate,” Analysis, Big Data China, collaboration of CSIS Trustee Chair in Chinese Business and Economics and the Stanford Center on China’s Economy and Institutions, October 14, 2022, <https://bigdatachina.csis.org/the-china-shock-reevaluating-the-debate/>.

40 White House, National Security Strategy, 8.

41 White House, National Security Strategy, 23.

reach globally—all while seeking to erode U.S. alliances in the region and around the world.⁴² Moreover, the United States has reached the clear conclusion that the risks of military confrontation over Taiwan are growing. Secretary of State Antony Blinken has stated that China has made “a fundamental decision that the status quo was no longer acceptable and that Beijing was determined to pursue reunification on a much faster timeline.”⁴³

There is a significant overlap among these factors. It is, as Treasury Secretary Yellen has said, “increasingly difficult to separate economic issues from broader considerations of national interest, including national security.”⁴⁴ That combination has generated revised trade and investment policies for the United States with respect to China.

Most notable perhaps of the changed policies are the tariffs—initially imposed by the Trump administration and generally kept in place by the Biden administration—which have substantially affected certain trade flows. A recent Peterson Institute for International Economics blog observes:

As expected, the trade war has had the largest impact on imports from China of products hit with the highest US tariffs. US imports from China of goods currently facing a 25 percent duty . . . remain 22 percent below pre-trade war levels . . . US imports of those same products from the rest of the world are now 34 percent *higher*. US imports from China of products currently subject to 7.5 percent tariffs . . . remain 3 percent below levels in August 2019 (right before imposition of tariffs on those products), whereas comparable imports from the rest of the world are now 45 percent *higher*.⁴⁵

The impact of the tariffs has been across multiple sectors:

US imports of certain products from China—including semiconductors, some IT hardware, and con-

sumer electronics—have fallen dramatically. Even clothing, footwear, and furniture imports are down.⁴⁶

Tariffs are, however, hardly the only the instrument of change. Beginning in the Trump administration and significantly increasing in the Biden administration are regulatory limitations on trade and investment, as noted in a *Foreign Policy* article. Thus:

Leveraging new laws passed in 2018, [the Trump administration] expanded the use of export controls in defense technology, imposed stricter vetting of foreign investments in strategic U.S. industries, and restricted the procurement of equipment and services from five Chinese information technology companies, the most prominent of which was Huawei. . . . Using presidential emergency powers, the Trump administration also created regimes to remove untrusted contractors from U.S. IT infrastructure projects and block Americans from investing in companies that work with the Chinese military.⁴⁷

Congress has been fully supportive of this approach and has enacted relevant restrictive legislation during both the Trump and Biden administrations including adding human rights as an additional rationale for limitations:

Congress has passed a slew of China-related bills. Among other actions, legislators have reformed inbound investment screening, forced the delisting of Chinese stocks that do not comply with U.S. accounting practices, expanded requirements for the U.S. Defense Department to list Chinese companies assisting the People’s Liberation Army, strengthened sanctions authorities in response to atrocities in Xinjiang and repression in Hong Kong, presumed that all goods produced in Xinjiang are made with forced labor (and thus banned as imports), and prohibited the federal purchase of Chinese telecommunications equipment.⁴⁸

42 White House, National Security Strategy, 23-24.

43 Ellen Francis, “China Plans to Seize Taiwan on ‘Much Faster Timeline,’ Blinken Says,” Washington Post, October 18, 2022, <https://www.washingtonpost.com/world/2022/10/18/china-seize-taiwan-plan-blinken/>.

44 “Remarks by Secretary of the Treasury Janet L. Yellen on Way Forward for the Global Economy.”

45 Chad P. Bown, “Four Years into the Trade War, Are the US and China Decoupling?,” Realtime Economics (blog), Peterson Institute for International Economics, October 20, 2022, <https://www.piie.com/blogs/realtime-economics/four-years-trade-war-are-us-and-china-decoupling/>.

46 Bown, “Four Years into the Trade War.”

47 Eric Sayers and Ivan Kanapathy, “America Is Showering China With New Restrictions,” Foreign Policy, February 15, 2022, <https://foreignpolicy.com/2022/02/15/us-china-economic-financial-decoupling-controls-restrictions-sanctions/>.

48 Sayers and Kanapathy, “America Is Showering China.”

The Biden administration not only has largely maintained the restrictions imposed by the Trump administration but has added significant restrictions of its own. Most notably it recently has established export controls barring the transfer to China of “advanced computing and semiconductor manufacturing . . . items and capabilities.”⁴⁹ These new controls cover not only items manufactured in the United States but also those produced outside the United States through the application of the “Foreign-Direct Product Rules.”⁵⁰ The national security rationale for the controls is clear, as underscored in a Department of Commerce statement:

The export controls announced in the two rules today restrict the PRC’s ability to obtain advanced computing chips, develop and maintain supercomputers, and manufacture advanced semiconductors. These items and capabilities are used by the PRC to produce advanced military systems including weapons of mass destruction; improve the speed and accuracy of its military decision making, planning, and logistics, as well as of its autonomous military systems; and commit human rights abuses.⁵¹

Experts noted the strong posture of the US government, with one referring to it as an aggressive approach intended to undercut China’s capacity to develop its own technolo-

gies in critical areas.⁵² The new controls were not the first restrictive actions on exports to China taken by the Biden administration. Previously, it had imposed limitations on biotechnology/life sciences⁵³ and quantum computing capabilities⁵⁴ by adding multiple companies to the Department of Commerce’s Entity List, thereby essentially preventing exports to them,⁵⁵ as well as expanding the prohibition of investments to Chinese companies providing “Chinese surveillance technology outside the PRC . . . to facilitate repression or serious human rights abuses.”⁵⁶

The results of these multiple restrictions have been consequential in the arenas where they have been applied. However, it is also important to note that there are other areas in which US-China trade remains quite substantial and, in fact, overall US-China bilateral trade has actually increased. As one recent analysis summarized:

Yet, US imports from China of certain products have surged. Imports of products never hit with trade war tariffs are now 50 percent higher than immediately prior to the trade war. . . . Products not facing tariffs made up roughly 33 percent of total US imports from China before the trade war and have grown to 47 percent today. . . . Imports from China of laptops and

49 Bureau of Industry and Security, “Commerce Implements New Export Controls on Advanced Computing and Semiconductor Manufacturing Items to the People’s Republic of China (PRC),” Department of Commerce, October 7, 2022, 2, <https://www.bis.doc.gov/index.php/documents/about-bis/newsroom/press-releases/3158-2022-10-07-bis-press-release-advanced-computing-and-semiconductor-manufacturing-controls-final/file>.

50 According to US rules relating to commerce and foreign trade, “foreign-produced items located outside the United States are subject to the EAR [Export Administration Regulations] when they are a ‘direct product’ of specified ‘technology’ or ‘software,’ or are produced by a plant or ‘major component’ of a plant that itself is a ‘direct product’ of specified ‘technology’ or ‘software.’ ” See 15 C.F.R. § 734.9 (as amended December 8, 2022), <https://www.ecfr.gov/current/title-15/subtitle-B/chapter-VII/subchapter-C/part-734/section-734.9>.

51 Bureau of Industry and Security, “Commerce Implements New Export Controls,” 1.

52 Ana Swanson, “Biden Administration Clamps Down on China’s Access to Chip Technology,” New York Times, October 7, 2022, https://www.nytimes.com/2022/10/07/business/economy/biden-chip-technology.html?campaign_id=60&emc=edit_na_20221007&instance_id=0&nl=breaking-news&ref=cta®_id=169223421&segment_id=109292&user_id=d2bcc4d73398823c64e17b75c053c05e. According to the article, Emily Kilcrease, a senior fellow at the Center for a New American Security, said: “It is an aggressive approach by the U.S. government to start to really impair the capability of China to indigenously develop certain of these critical technologies.”

53 The biotechnology restrictions focused “principally on the Chinese Academy of Military Medical Sciences and its research institutes in response to their use of ‘biotechnology processes to support Chinese military end uses and end users’ . . . [Control of] certain life sciences technology . . . include[d] certain software (and related technology) designed for nucleic acid assemblers and synthesizers . . . capable of designing and building functional genetic elements from digital sequence data given . . . possible use in biological weapons programs.” Jeffrey L. Kessler et al., “United States Adopts Wide-ranging China Restrictions,” WilmerHale, December 29, 2021, <https://www.wilmerhale.com/en/insights/client-alerts/20211229-united-states-adopts-wide-ranging-china-restrictions>.

54 The earlier quantum computing restrictions added “27 Chinese and third-country entities to the Entity List for their role in support of Chinese ‘quantum computing efforts that support military applications, such as counterstealth and countersubmarine applications, and the ability to break encryption or develop unbreakable encryption,’ among other activities.” Kessler et al., “United States Adopts.”

55 The Entity List contains the names of “foreign persons—including businesses, research institutions, government and private organizations, individuals, and other types of legal persons—that are subject to specific license requirements for the export, reexport and/or transfer (in-country) of specified items.” See Bureau of Industry and Security, “Entity List,” Department of Commerce (website), accessed November 10, 2022, 1, <https://www.bis.doc.gov/index.php/policy-guidance/lists-of-parties-of-concern/entity-list>. Though requests for export licenses are reviewed on a case-by-case basis, there often is a presumption of denial associated with a listing. See, for example, Bureau of Industry and Security, “Commerce Implements New Export Controls on Advanced Computing and Semiconductor Manufacturing Items to the People’s Republic of China (PRC),” Department of Commerce, October 7, 2022, , <https://www.bis.doc.gov/index.php/documents/about-bis/newsroom/press-releases/3158-2022-10-07-bis-press-release-advanced-computing-and-semiconductor-manufacturing-controls-final/file>.

56 Exec. Order No. 14032, 86 Fed. Reg. 30145 (2021), <https://home.treasury.gov/system/files/126/14032.pdf>.

computer monitors, phones, video game consoles, and toys are higher than ever.⁵⁷

Accordingly, for overall trade between the United States and China, US trade statistics show higher levels of exports and imports: US exports to China totaled \$151.1 billion, a rise of 21.4% (\$26.6 billion) compared to 2020, while US imports from China totaled \$506.4 billion, an increase of 16.5% (\$71.6 billion).⁵⁸

As the trade numbers above imply, there is an important differential in the analysis of risks undertaken by private-sector enterprises and by the government. Governments will review societal risks including external diseconomies and security while enterprises generally will take a narrower view focused on the firm and sector. This is not to suggest that enterprises are unaware of societal risks, as may be relevant to the enterprise. By way of example, an annual economic analysis published in 2022 found:

Even before the pandemic, concerns had been growing about supply chain resiliency and the asymmetric dependencies that had built up in the deeply intertwined supply chains linking the United States, Europe, and China. Before the pandemic hit, many companies were already shifting production out of China or diversifying their production. Some didn't want to become inordinately dependent on any one particular link in their supply chain. Several feared data security and privacy risks. Others wanted to avoid being caught in a U.S.-China trade war. And many decided that rising labor costs in China made other locales more attractive. Footwear, accessories, toy and furniture manufacturers began moving out of China more than a decade ago. More than 83% of North American businesses and about 90% of European firms have announced plans to relocate at least part of their supply chains away from China.⁵⁹

In general, however, it is the government's role to take account of the wider risk environment.

B. The ADEs

The ADEs have adopted security and economic strategies that, at least rhetorically, highlight certain issues in a fashion comparable to the strategic approach of the United States. On the security side, while none of the ADEs has a statutory mandate comparable to the Taiwan Relations Act, there have been changes in policy and posture—some significant and some early days—including working more closely with the United States in key geographic and technological arenas. Economically, there has been substantial focus on the issue of dependencies, though the scope of any actual changes is yet to be determined.

In the security arena, three significant changes include the Australia-United Kingdom-United States (AUKUS) agreement; Japan's focus on the need for peace and stability in the Taiwan Strait; and NATO's inclusion of China as a challenge in its new Strategic Concept.

The AUKUS agreement involves very substantial technological interactions among the three countries. The agreement has two main components:

- ◆ Providing Australia “with a conventionally armed, nuclear powered submarine capability” with decisions on the way forward planned to be made by March 2023.
- ◆ Developing and providing “joint advanced military capabilities” with efforts in eight areas including autonomous underwater vehicles; generation-after-next quantum capabilities; artificial intelligence; advanced cyber; hypersonic and counterhypersonic capabilities; electronic warfare; innovation including ways to integrate commercial technologies more rapidly; and information sharing.⁶⁰

While the substantive results of AUKUS are yet to be achieved, the agreement is already notable geopolitically for its substantial engagement of the United Kingdom in

57 Bown, “Four Years into the Trade War.”

58 Bureau of Industry and Security, Office of Technological Evaluation, “U.S. Trade with China,” Department of Commerce, 2021, 1, [https://www.bis.doc.gov/index.php/country-papers/2971-2021-statistical-analysis-of-u-s-trade-with-china/file#:~:text=Goods%20with%20China-,ln%202021%2C%20U.S.%20exports%20to%20China%20were%20%24151.1%20billion%2C%20a,%25%20\(%2445.0%20billion\)%20increase.](https://www.bis.doc.gov/index.php/country-papers/2971-2021-statistical-analysis-of-u-s-trade-with-china/file#:~:text=Goods%20with%20China-,ln%202021%2C%20U.S.%20exports%20to%20China%20were%20%24151.1%20billion%2C%20a,%25%20(%2445.0%20billion)%20increase.)

59 Daniel S. Hamilton and Joseph Quinlan, “Shifting Dependencies: Rethinking Russia, China, and Global Supply Chains,” in *The Transatlantic Economy 2022: Annual Survey of Jobs, Trade and Investment between the United States and Europe* (Washington, DC: Foreign Policy Institute, Johns Hopkins University SAIS/Transatlantic Leadership Network, 2022), 35-42, https://transatlanticrelations.org/wp-content/uploads/2022/03/TE2022_CHAP3.pdf.

60 White House, “Fact Sheet: Implementation of the Australia–United Kingdom–United States Partnership, (AUKUS),” White House Briefing Room, April 5, 2022, <https://www.whitehouse.gov/briefing-room/statements-releases/2022/04/05/fact-sheet-implementation-of-the-australia-united-kingdom-united-states-partnership-aukus/>.

the security of the Indo-Pacific,⁶¹ and for underscoring Australia's decision to confront China in the security field.

The Japanese determination to include the Taiwan Strait as a matter of security importance to Japan is likewise consequential for both security and geopolitical reasons. Japan has explicitly “confirmed a continued close cooperation to maintain peace and stability in the Taiwan Strait,” including having done so in the context of US Speaker of the House of Representatives Nancy Pelosi's visit to Taiwan, which was much condemned by China.⁶² In addition, Japan has continued increasing its defense budget,⁶³ has undertaken enhanced defense exercises with the United States,⁶⁴ is upgrading its military capabilities such as through the purchase of long-range cruise missiles,⁶⁵ and is in the process of enhancing its defense cooperation with European nations including potentially developing a highly advanced fighter aircraft with the United Kingdom and Italy.⁶⁶

NATO's new Strategic Concept states quite clearly that the People's Republic of China's “stated ambitions and coercive policies challenge our interests, security and values.”⁶⁷ Accordingly, NATO will:

... address the systemic challenges posed by the PRC to Euro-Atlantic security and ensure NATO's

enduring ability to guarantee the defence and security of Allies. We will boost our shared awareness, enhance our resilience and preparedness, and protect against the PRC's coercive tactics and efforts to divide the Alliance. We will stand up for our shared values and the rules-based international order, including freedom of navigation.⁶⁸

The geopolitical value of the Strategic Concept is substantial, though substantively NATO has not yet taken any significant implementing steps—which is not entirely surprising given the current focus on Ukraine and the relatively recent issuance of the Strategic Concept. NATO has, however, begun discussing “concrete ways to meet the challenge,” according to Secretary of State Blinken following a NATO foreign ministers meeting.⁶⁹ Moreover, while not under a NATO flag, a number of NATO nations including Canada,⁷⁰ France,⁷¹ Germany,⁷² the Netherlands,⁷³ and the United Kingdom⁷⁴ have undertaken freedom of navigation activities in the Indo-Pacific including through the Taiwan Strait. Additionally, Canada recently has required China to divest its ownership in three mining companies on national security grounds, as the following news report describes:

Canada has ordered China to immediately sell its holdings in three Canadian mining companies, as

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- 61 The United Kingdom and Japan are in process of finalizing a reciprocal access agreement, which the Financial Times reported “will make joint exercises and logistics co-operation between the nations easier.” See Kana Inagaki and Demetri Sevastopulo, “Japan to Sign Military Pact with UK as Allies Eye China Threat,” Financial Times, November 5, 2022, <https://www.ft.com/content/6ea15304-551b-4161-af6c-38cccf56d40d>.
- 62 “Japan, US to Cooperate on Maintaining Peace, Stability in Taiwan Strait,” CNA, Mediacorp, August 5, 2022, <https://www.channelnewsasia.com/asia/japan-us-cooperate-maintaining-peace-stability-taiwan-strait-2860501>.
- 63 Kana Inagaki, “Japan Plans Big Defence Spending Boost to Counter Rising China Threat,” Financial Times, August 31, 2022, <https://www.ft.com/content/d5f91273-61c9-4116-9620-a5e771563e9d>.
- 64 “Japan and U.S. Begin Large-scale Joint Exercise with China in Mind,” Japan Times, November 10, 2022, <https://www.japantimes.co.jp/news/2022/11/10/national/japan-us-joint-drill-china/>.
- 65 Michelle Ye Hee Lee and Ellen Nakashima, “Japan to Buy Tomahawk Missiles in Defense Buildup amid Fears of War,” Washington Post, December 12, 2022, <https://www.washingtonpost.com/world/2022/12/12/japan-tomahawk-missiles-ukraine-war/>.
- 66 Kana Inagaki, Leo Lewis, and Sylvia Pfeifer, “The Fighter Jet That Could Create a New Alliance between the UK and Japan,” Financial Times, November 27, 2022, <https://www.ft.com/content/a013530d-82f9-4a89-b5cf-5d76032d8c47>; also see Inagaki and Sevastopulo, “Japan to Sign Military Pact.”
- 67 NATO 2022 Strategic Concept, 2022, 5, https://www.nato.int/nato_static_fl2014/assets/pdf/2022/6/pdf/290622-strategic-concept.pdf; the Strategic Concept was adopted by heads of state and government at the NATO Summit in Madrid, June 29, 2022.
- 68 NATO 2022 Strategic Concept, 5.
- 69 Henry Foy and Demetri Sevastopulo, “Nato Debates Measures to Confront ‘Challenge’ from China,” Financial Times, November 30, 2022, <https://www.ft.com/content/6df14a27-4d0e-49ba-98eb-d9e7b3997486>.
- 70 “US, Canada Warships Sail through Strait,” Taipei Times, September 22, 2022, <https://www.taipetimes.com/News/front/archives/2022/09/22/2003785727>.
- 71 Joseph Pedrajas, “France Calls for Rule of Law Preservation, Freedom of Navigation in Indo-Pacific,” Manila Bulletin, September 16, 2022, <https://mb.com.ph/2022/09/16/france-calls-for-rule-of-law-preservation-freedom-of-navigation-in-indo-pacific/>.
- 72 Associated Press, “German Navy Chief Vows Long-term Commitment to Indo-Pacific,” Asahi Shinbun, November 10, 2021, <https://www.asahi.com/ajw/articles/14478795>.
- 73 Maaik Okano-Heijmans, “Netherlands and Indo-Pacific: Inclusive but Not Value-Neutral,” Clingendael Magazine, Netherlands Institute of International Relations, August 31, 2021, <https://www.clingendael.org/publication/netherlands-and-indo-pacific-inclusive-not-value-neutral>.
- 74 Agence France-Presse, “UK Sends Warship through Taiwan Strait for First Time in More Than a Decade,” Guardian, September 28, 2021, <https://www.theguardian.com/uk-news/2021/sep/28/uk-sends-warship-through-taiwan-straight-for-first-time-in-more-than-a-decade>.

the need for investments in the extraction of critical minerals clashes with growing concerns over national security. . . .

[Canada's industry minister, François-Philippe Champagne, said:] "While Canada continues to welcome foreign direct investment, we will act decisively when investments threaten our national security and our critical minerals supply chains, both at home and abroad. . . ."75

Similarly, the British government has recently decided to take a 50 percent stake in a new nuclear plant, which "squeezes out a Chinese state-owned company, China General Nuclear, which had owned 20 percent of the project."76

Economically, the ADEs have highlighted the issue of dependencies (as further described below), but economic interactions with China have not significantly changed, with trade flows continuing at high levels in:

- ◆ **Europe:** EU exports and imports to and from China have increasingly reached higher levels as a recent EU ten-year review demonstrates. "Both exports to and imports from China increased between 2011 and 2021. EU exports to China were highest in 2021 (€223 billion) . . . EU imports from China were highest in 2021 (€472 billion)," according to Eurostat.77
- ◆ **Japan:** While the impact of the pandemic (including China's zero-COVID policy) affected trade, nonetheless "China consumed more than 20 percent of Japanese exports for the first time [in 2020] . . . leapfrogging the [United States] to become Japan's leading destination for exports for the first time in two years. . . . China and

the U.S. have repeatedly alternated as Japan's leading trading partner since the late 2000s. Last year [2020], China accounted for 22% of all exports, while the U.S. trailed at 18.4%," *Nikkei* reported.78 The high level of Japan's trade with China continued in 2021, with exports to China increasing from \$146 billion to \$206 billion.79

- ◆ **South Korea:** China is South Korea's largest trading partner, with trade totaling \$240 billion between the two countries in the 2016-2021 period, compared with \$131 billion in US-South Korea trade in the same period.80
- ◆ **Australia:** Overall, Australia-China trade during the period of 2016-2021 was approximately \$160 billion—more than twice the combined total of its second-largest partners in imports (Japan) and exports (United States).81 At an Asia Society panel discussion in Melbourne, a senior Australian official described China as "such an enormous economy," and was quoted by Bloomberg as saying that "it will be almost unimaginable to think that that importance will decrease significantly." The official, Elizabeth Bowes from the Department of Foreign Affairs and Trade, highlighted that Australia's exports to China are higher than a year earlier, following record two-way trade totaling A\$282 billion (\$178 billion) in 2021.82

As noted above, the data underscore the importance for ADE enterprises to engage in the China market. However, while trade flows have not been affected, the issue of dependencies has received increased attention by the governments of the ADEs.

75 Leyland Cecco, "Canada Orders China to Divest from Country's Mining Companies," *Guardian*, November 3, 2022, <https://www.theguardian.com/world/2022/nov/03/canada-china-mining-companies-divest>.

76 Stanley Reed, "U.K. Backs Giant Nuclear Plant, Squeezing Out China," *New York Times*, November 29, 2022, <https://www.nytimes.com/2022/11/29/business/uk-nuclear-plant-china.html>.

77 Eurostat Statistics Explained, "China-EU: International Trade in Goods Statistics," Eurostat, February 2022, [https://ec.europa.eu/eurostat/statistics-explained/index.php?title=China-EU_-_international_trade_in_goods_statistics#:~:text=billion%20in%202021.-,Both%20exports%20to%20and%20imports%20from%20China%20increased%20between%202011,2013%20\(%E2%82%AC%20239%20billion\)](https://ec.europa.eu/eurostat/statistics-explained/index.php?title=China-EU_-_international_trade_in_goods_statistics#:~:text=billion%20in%202021.-,Both%20exports%20to%20and%20imports%20from%20China%20increased%20between%202011,2013%20(%E2%82%AC%20239%20billion)).

78 *Nikkei* staff writers, "China Passes US as Top Japanese Export Buyer, Topping 20%," *Nikkei Asia*, January 22, 2021, <https://asia.nikkei.com/Economy/Trade/China-passes-US-as-top-Japanese-export-buyer-topping-20>.

79 "Japan-China Relations (Basic Data)," Ministry of Foreign Affairs (website), February 24, 2022, <https://www.mofa.go.jp/region/asia-paci/china/data.html>.

80 World Integrated Trade Solution (WITS), Republic of Korea data, World Bank (website), accessed November 10, 2022, <https://wits.worldbank.org/CountrySnapshot/en/KO>.

81 WITS, Australia data, World Bank (website), accessed November 10, 2022, <https://wits.worldbank.org/CountrySnapshot/en/AUS>.

82 Swati Pandey, "China to Remain a Key Trade Partner for Australia, Official Says," *Bloomberg*, October 19, 2022, <https://www.bloomberg.com/news/articles/2022-10-19/china-to-remain-a-key-trade-partner-for-australia-official-says>.

Japan has been a leader in generating a degree of movement of Japanese companies from China. As the pandemic began to disrupt supply chains in 2020, the Japanese government saw an opportunity to diversify supply chains and in April established a multibillion yen fund to support company transfers to Japan or Southeast Asia.⁸³ In the first year of the fund's existence, more than two hundred companies received funding to subsidize their moves,⁸⁴ and Japanese companies began to increasingly focus their new investments elsewhere.⁸⁵

Europe has not undertaken concrete steps similar to those of Japan, but the issue of dependencies has received high-level attention. European Commission President Ursula von der Leyen's recent State of the Union Address reflects that concern, mentioning that China controls the global processing industry for strategic minerals, and referencing its dominance in rare earth materials (nearing 90 percent of the market) and in lithium processing (at 60 percent).⁸⁶ Similarly, just prior to his recent trip to China, German Chancellor Olaf Scholz wrote that Germany seeks to "dismantle one-sided dependencies in the interest of smart diversification"; and is putting "supply chains on a broader footing . . . for example with new raw material partnerships." He added that where China bars reciprocity, "it cannot be without consequences."⁸⁷

There have been some European steps toward taking a broader approach beyond the issue of dependencies. The European External Action Service recently recommended in an internal paper that the EU should "identify and address the challenges deriving from China's foreign policy," including changing the emphasis in the tripartite division among systemic rivalry, competition, and cooperation to-

ward greater focus on rivalry and competition.⁸⁸ While hardly a model of clarity, the language is a useful step toward recognizing the challenges presented by China. Likewise, according to a *Brussels Morning* report:

European Commissioner for Internal Market Thierry Breton warned European governments and businesses that they must realise China is the Union's rival, and urged them not to be naive when approving Chinese investments.⁸⁹

The report further quotes Breton as stating that "the European market is open, (but) with conditions."⁹⁰ According to the report, Breton also warned European businesses that they are expanding their investments in China at their own risk, as the country is becoming more "autocratic."⁹¹

Similarly, the Associated Press reported that French President Emmanuel Macron said "Europe made a 'historical' mistake during the global financial crisis of 2007-2008 by pushing some member states to sell their infrastructure. . . . Macron said Europeans were 'naïve' to treat the bloc like an 'open supermarket' because of public finance issues."⁹²

It would be inaccurate to say that European efforts have only been rhetorical. There have been at least three significant sets of actions involving human rights, cybersecurity, and cooperation to promote investment:

- ◆ **Human rights:** After China placed sanctions on four EU parliamentary members in response to EU sanctions imposed as a result of human rights violations by China against the Uighur population, the European Parliament passed a resolution barring "any consideration by the

83 In dollar terms, that's at least \$5 billion. See Pascal Delloué, "Why Is Japan Incentivizing Companies to Leave China," Kusu (company website), July 21, 2022, <https://www.kusucorp.com/blog/why-is-japan-incentivizing-its-companies-to-leave-china-and-why-it-matters>.

84 Francesca Regalado, "Japan Chip Suppliers Reap Benefits of 'China Exit' Subsidy," Nikkei Asia, January 25, 2021, <https://asia.nikkei.com/Economy/Trade/Japan-chip-suppliers-reap-benefits-of-China-exit-subsidy>; and Delloué, "Why Is Japan Incentivizing Companies."

85 "Japanese Companies Try to Reduce Their Reliance on Chinese Manufacturing," Economist, September 18, 2021, <https://www.economist.com/business/2021/09/18/japanese-companies-try-to-reduce-their-reliance-on-chinese-manufacturing>.

86 "2022 State of the Union Address by President von der Leyen," European Commission (website), September 14, 2022, https://ec.europa.eu/commission/presscorner/detail/en/speech_22_5493.

87 Olaf Scholz, "We Don't Want to Decouple from China, but Can't Be Overreliant," Politico, November 3, 2022, <https://www.politico.eu/article/olaf-scholz-we-dont-want-to-decouple-from-china-but-cant-be-overreliant/>.

88 Stuart Lau, "Brussels Playbook: EU-China Rethink—MEPs and Their Receipts—Josep's Garden," Politico, October 17, 2022, <https://www.politico.eu/newsletter/brussels-playbook/eu-china-rethink-meps-and-their-receipts-joseps-garden/>.

89 Ivan Fischer, "Market Commissioner Breton Warns Governments and Businesses China Is a Rival," Brussels Morning, October 31, 2022, <https://brusselsmorning.com/market-commissioner-breton-warns-governments-and-businesses-china-is-a-rival/27578/>.

90 Fischer, "Market Commissioner Breton Warns Governments."

91 Fischer, "Market Commissioner Breton Warns Governments."

92 Lorne Cook and Geir Moulson, "EU Leaders Weigh Future of China Ties as Rivalry Mounts," Associated Press, October 21, 2022, <https://apnews.com/article/european-union-council-xi-jinping-beijing-china-42316d57714db211345dfd1d1bb10d11e>.

European Parliament of the EU-China Comprehensive Agreement on Investment, agreed in principle between the EU and China in December 2020.”⁹³

- ◆ **Cybersecurity:** A key set of issues related to whether the Chinese telecommunications company Huawei Technologies Co. Ltd. would be allowed to provide 5G networks for European countries. The EU adopted a “cyber toolbox” for dealing with the risks raised,⁹⁴ and the United Kingdom undertook its own review.⁹⁵ Partly as a consequence—and in combination with limits on Huawei and vigorous diplomacy by the United States—a number of EU member states and the United Kingdom decided not to utilize Huawei.⁹⁶
- ◆ **Cooperation on investment:** The Baltic countries have all exited the “17+1” format that was intended to enhance investment and trade cooperation between China and Eastern European countries.⁹⁷

The European Union has also adopted (or is in process of adopting) a set of regulatory frameworks that are designed

to offset inimical Chinese behavior (though notably, none mention China by name). These include a countersubsidy mechanism,⁹⁸ foreign direct investment screening and export controls,⁹⁹ several actions focused on cybersecurity including a proposed Cyber Resilience Act¹⁰⁰ (as well as the above-noted cyber toolkit), a proposed anti-coercion instrument,¹⁰¹ and a proposed European Critical Raw Materials Act.¹⁰² The application of these measures has, however, been quite limited thus far in scope and impact:

- ◆ In December 2021, the European Union announced that it will place extra tariffs on aluminum foil coming from China after the European Commission found that producers in China benefited from excessive and unfair subsidies.¹⁰³
- ◆ In March 2022, the EU imposed anti-subsidy duties on imports of stainless-steel cold-rolled flat products originating in Indonesia and India to counter subsidies on raw materials and transnational subsidies from China.¹⁰⁴

93 “MEPs Refuse Any Agreement with China whilst Sanctions Are in Place,” European Parliament, Press Release, May 17, 2021, <https://www.europarl.europa.eu/news/en/press-room/20210517IPRO4123/meps-refuse-any-agreement-with-china-while-sanctions-are-in-place>.

94 Network and Information Systems (NIS) Cooperation Group, “Cybersecurity of 5G networks: EU Toolbox of Risk Mitigating Measures,” European Commission, January 2020, <https://digital-strategy.ec.europa.eu/en/library/cybersecurity-5g-networks-eu-toolbox-risk-mitigating-measures>.

95 UK Department for Digital, Culture, Media and Sport, National Cyber Security Centre, and the Right Honourable Oliver Dowden CBE MP, “Huawei to Be Removed from UK 5G Networks by 2027,” Government of the United Kingdom, Press Release, July 14, 2020, <https://www.gov.uk/government/news/huawei-to-be-removed-from-uk-5g-networks-by-2027>.

96 According to *The Economist*, “Australia, Canada, New Zealand and Sweden have followed America in banning Huawei gear outright. New rules in Britain force carriers to remove all Huawei technology from public 5G systems by 2027. France has asked operators to rip out Huawei gear from many parts of their networks. Other countries, such as Japan, have not barred Huawei but signaled that it is unwelcome. The constant risk of fresh restrictions has led many customers in places without bans to steer clear of Huawei. This has already happened in Italy and Portugal.” See “Can Huawei Thrive despite American Sanctions?,” *Economist*, October 25, 2022, <https://www.economist.com/business/2022/10/25/ren-zhengfei-has-big-plans-for-huawei-in-spite-of-american-sanctions>.

97 Pepijn Bergsen and Valdonė Šniukaitė, “Central and Eastern Europe Become Hawkish on China,” Commentary, Chatham House, September 16, 2022, <https://www.chathamhouse.org/2022/09/central-and-eastern-europe-become-hawkish-china>.

98 “Anti-subsidy Measures,” European Commission, Trade webpages, accessed November 18, 2022, https://policy.trade.ec.europa.eu/enforcement-and-protection/trade-defence/anti-subsidy-measures_en.

99 “EU Investment Screening and Export Control Rules Effectively Safeguard EU Security,” European Commission Press Corner, September 2, 2022, https://ec.europa.eu/commission/presscorner/detail/en/ip_22_5286.

100 “Policy and Legislation: Cyber Resilience Act,” European Commission (website), September 15, 2022, <https://digital-strategy.ec.europa.eu/en/library/cyber-resilience-act>.

101 Camille Gijjs, “EU Countries Seek to Claw Back Power from Brussels on Upcoming Trade Bazoooka,” *Politico*, October 20, 2022, <https://www.politico.eu/article/eu-countries-seek-to-claw-back-power-from-brussels-on-upcoming-trade-bazoooka/>.

102 “Critical Raw Materials Act: Securing the New Gas & Oil at the Heart of Our Economy,” Blog of Commissioner Thierry Breton, European Commission Press Corner, September 14, 2022, https://ec.europa.eu/commission/presscorner/detail/en/statement_22_5523.

103 “EU to Impose Extra Tariffs on China Aluminium Foil over Subsidies,” *Reuters*, December 22, 2021, <https://www.reuters.com/markets/commodities/eu-impose-extra-tariffs-china-aluminium-foil-over-subsidies-2021-12-22/>.

104 “EU Counters Steel Subsidies Resulting from Export Restrictions on Raw Materials and Transnational Subsidies from China,” European Commission Press Corner, March 16, 2022, https://ec.europa.eu/commission/presscorner/detail/en/ip_22_1774; and Max Hall, “EU Adds Anti-subsidy Duty to Existing Trade Measures on Indian and Indonesian Steel,” *pv magazine*, March 21, 2022, <https://www.pv-magazine.com/2022/03/21/eu-adds-anti-subsidy-duty-to-existing-trade-measures-on-indian-and-indonesian-steel/>.

- ◆ In 2022 and 2020, the EU imposed duties on glass fiber fabrics and products from Chinese companies or joint venture on products arriving via Morocco and Egypt.¹⁰⁵
- ◆ In support of Lithuania, the European Parliament has passed resolutions calling “on the PRC to revoke its unjustified sanctions against Lithuanian officials” and condemning “the PRC’s trade restriction,” which came in response to Lithuania allowing “Taiwan” to be utilized as part of the name of the Taiwan economic office that was opened in Lithuania.

To sum up, there is a good deal of uncertainty as to future European-China trade relations. While overall trade will likely continue at a high level (as the data noted above imply), greater restrictions are being contemplated. The debate in Germany exemplifies the issues, as outlined in *The New York Times*: On the one hand, “Scholz overruled the recommendation of six of his ministries and both domestic and foreign intelligence chiefs to allow Cosco, a Chinese state-owned shipping company, to buy a stake of up to 25 percent in a container-handling terminal in Hamburg, Germany’s most important port.” (True, amid public outcry, COSCO did not get the 35 percent stake it had originally sought.) On the other hand, Berlin has blocked two deals: the sale of a semiconductor company to a Chinese-owned firm and, according to Germany’s economy minister, another proposed investment in a “German company pro-

ducing critical infrastructure,” which the official declined to identify due to “secrecy agreements.”¹⁰⁶

The level of European uncertainty regarding the actual direction of economic relations with China is visible in high-level statements after a recent meeting of heads of government. EU Council President Charles Michel, for instance, said: “This discussion showed a very clear will to avoid being naive, but neither did we want to embark into a logic of systematic confrontation.”¹⁰⁷

But the concern regarding dependencies remained central as European Commission President von der Leyen stated after the same meeting: “Obviously, we have to be very vigilant when it comes to dependencies. And we’ve learned our lesson.”¹⁰⁸

While these statements of European policy do reflect a degree of toughening of views toward China, there is, however, a clear inclination among at least some European leaders to have a policy that is different than that of the United States. Dutch Prime Minister Mark Rutte, for instance, underscored how the EU should develop its own course in response to China’s increasing assertiveness. “It’s important that Europe operates as self-confident as possible, but also independently,” Rutte said, adding that the EU should seek “equality and reciprocity, so that we are not a kind of extension of America but that we have our own politics vis-à-vis China.”¹⁰⁹

105 “EU Acts to Stop Chinese Glass Fibre Fabrics Circumventing EU Tariffs via Morocco,” Directorate-General for Trade, European Commission (website), February 25, 2022, https://policy.trade.ec.europa.eu/news/eu-acts-stop-chinese-glass-fibre-fabrics-circumventing-eu-tariffs-morocco-2022-02-25_en.

106 Melissa Eddy, “Germany Blocks 2 Foreign Investment Deals, Taking a Firmer Line on China,” *New York Times*, November 9, 2022, <https://www.nytimes.com/2022/11/09/world/europe/germany-china-investment.html>.

107 Le Monde staff and AFP, “EU Not Looking for ‘Systematic Confrontation’ with China, Says Council President Michel,” *Le Monde*, updated October 21, 2022, https://www.lemonde.fr/en/international/article/2022/10/21/eu-not-looking-for-systematic-confrontation-with-china_6001242_4.html.

108 Alexandra Brzozowski, “EU Leaders Wary of Dependencies Created with China, but Far from United,” *Euractiv*, updated October 23, 2022, <https://www.euractiv.com/section/eu-china/news/eu-leaders-wary-of-dependencies-created-with-china-but-far-from-united/>.

109 Brzozowski, “EU Leaders Wary of Dependencies.”

III. RECOMMENDATIONS

As described at the beginning of this brief, the fundamental challenge in establishing an effective strategy for China is to reconcile the fact that it is a massive trading partner for the ADEs while also being a significant security threat and an economic actor that acts in ways substantially inconsistent with market-based economies. Rather than maximum trade-centered globalization, which has been a long-standing approach by the major trading entities, a critical goal for the United States and its allies and close partners should now be giving agreed content to the concept of “free but secure trade,” as identified by US Treasury Secretary Yellen.¹¹⁰ Doing so will require a combination of selective decoupling to offset security and economic challenges and the development of strategic supply chains outside China to resolve the problems of dependencies.

The recommendations below are intended to provide specifics for such a coordinated strategic security and economic framework for the United States and the ADEs in dealing with the challenges presented by China.

A. Enhance Economic and Security Coordination by Expanding the G7 to a G10-plus to Formally Include Australia, Norway, the Republic of Korea, and the European Union and by Establishing a Multinational Staff Focused on China

As the substantive recommendations below are generally multinational—or at least have multinational consequences—an important element of implementation will be to undertake appropriate diplomatic efforts to achieve as broad a consensus as possible as to their substance. This will involve both sustained bilateral discussions and the use of a variety of fora such as the US-EU Trade and Technology Council, the “Chip 4” alliance (Japan, Republic of Korea, Taiwan, United States), and the Quadrilateral Security Dialogue (Australia, India, Japan, United States), known as the Quad. From the US perspective, it will be important to recognize the often-substantial differences between the American economy and the economies of allies and close partners, and to incorporate that understanding into a realistic strategy that will mitigate security and economic risks without causing unwarranted economic harm.

Critical, however, to effectuating an effective coordinated security and economic approach will be the need for an appropriate forum that encompasses the ADEs. The meetings of the G7 group (Canada, France, Germany, Italy, Japan, United Kingdom, United States) have in recent years included not only the European Union but Australia and the Republic of Korea as observers as well. Norway is a democracy with an advanced free-market economy, a critical energy provider, and very closely associated with the EU through the European Economic Area (EEA) Agreement, and has “very close and active cooperation on foreign and security policy issues” with the EU,¹¹¹ as well as with the United States, both through NATO and bilaterally. Expanding the G7 to a G10-plus to formally include Australia, Norway, the Republic of Korea, and the European Union would recognize the reality and necessity of a coordinated China policy among the ADEs.

The newly established G10-plus should create a multinational staff to help coordinate and implement China policy. Indeed, this change is even more important than the formal expansion, and the staff should have three foci: intelligence, economics, and security.

First, a shared intelligence picture will illuminate economic and security decisions. Each of the G10-plus countries (and the EU) will likely have information that others may not, and a common picture on economic and security matters would be invaluable for policymakers.

Second, economic coordination should include actions (as discussed below) with respect to limits on China in the domestic markets of the ADEs; actions taken regarding China’s domestic market; and actions of importance taken with respect to other countries including those focused on the Global South. A common approach to the export of high-end capabilities, for example, will be very important as will be protections to enhance resilience for critical infrastructures. Similarly, a number of Indo-Pacific strategies have been promulgated by different members of the prospective G10-plus, and it will be highly valuable for G10-plus members to have a common understanding of how those multiple economic strategies are being implemented.

¹¹⁰ “Remarks by Secretary of the Treasury Janet L. Yellen on Way Forward for the Global Economy.”

¹¹¹ “The European Union and Norway,” Delegation of the European Union to Norway, European External Action Service (website), European Union, July 28, 2021, https://www.eeas.europa.eu/norway/european-union-and-norway_en?s=174.

Third, security issues include limitations on trade and investment with China—the specifics for a number of which are discussed below. Security also involves gray area/hybrid concerns such as cybersecurity and influence operations, matters involving the global commons including freedom of navigation and space, security support to nations in the Indo-Pacific, and deterrence and defense issues including those concerning Taiwan, the East China Sea, and the South China Sea.

Regularizing information sharing and, as appropriate, coordination on each of the above three areas would allow for a more effective set of policies toward China (though the lead for military and intelligence issues such as military planning and operations would remain elsewhere).

B. Establish National Security Limits on Transactions with China

1. Limit or prohibit the transfer of advanced capabilities that have significant national security implications.

The US Department of Defense has identified fourteen “critical technology areas” vital to maintaining national security.¹¹² As discussed above, the United States has also undertaken a number of regulatory measures to limit the transfer of certain advanced technology capabilities to China including with respect to advanced chips, artificial intelligence, quantum computing, and biotechnology (each of which is on the Defense Department list).¹¹³ In a discussion of the most recent limitations on advanced chips and artificial intelligence (AI), Under Secretary of Commerce Alan Estevez indicated that further restrictions were likely with

respect to other key technologies.¹¹⁴ The intent, of course, is to enhance deterrence by reducing the likelihood of a successful military operation by China, particularly with respect to Taiwan. All of the members of the proposed G10-plus would be significantly affected by an armed attack by China against Taiwan; as noted, the importance of maintaining peace and stability in the Taiwan Strait has been highlighted by many, including the G7.¹¹⁵ Limiting China’s military capabilities is accordingly of high consequence, and a common approach to limitations on transactions involving advanced technologies will be in the interests of all.

2. Limit or prohibit trade and investment with companies that have substantial involvement in China’s military-civil fusion effort.

Militaries do not run only on advanced technologies. More mundane capabilities including materials, components, and software are important contributors to military effectiveness. By way of example, logistics is critical to all military operations, but most logistic requirements are relatively lower end. For the same reason that advanced technology exports with national security implications should be limited to China, so should exports to companies that significantly support China’s military-civil fusion efforts. The United States has already prohibited investments in a number of Chinese companies substantially involved in China’s military-civil enterprise.¹¹⁶ However, the United States and the other G10-plus countries should undertake a more comprehensive review, and then apply additional restrictions to companies significantly engaged in China’s military-civil fusion effort to limit the growth in effectiveness of the Chinese military.

112 Office of the Under Secretary of Defense for Research and Engineering, Memorandum on USD(R&E) Technology Vision for an Era of Competition, Department of Defense, February 1, 2022, 1, https://www.cto.mil/wp-content/uploads/2022/02/usdre_strategic_vision_critical_tech_areas.pdf.

113 The technologies are (in the order presented in the memo): biotechnology, quantum science, future generation wireless technology, advanced materials, trusted AI and autonomy, integrated network systems-of-systems, microelectronics, space technology, renewable energy generation and storage, advanced computing and software, human-machine interfaces, directed energy, hypersonics, and integrated sensing and cyber. See Office of the Under Secretary of Defense for Research and Engineering, Memorandum, 3-6; also see “Critical And Emerging Technologies List Update,” Report, Fast Track Action Subcommittee on Critical and Emerging Technologies of the National Science and Technology Council, Executive Office of the President, February 2022, <https://www.whitehouse.gov/wp-content/uploads/2022/02/02-2022-Critical-and-Emerging-Technologies-List-Update.pdf>.

114 In a conversation at the Center for a New American Security (CNAS), Under Secretary of Commerce Alan Estevez said: “We’re not done. I mean, there’s other things to be done. There’s other technologies and there’s other things as technology moves, we’re going to stay with it.” See Martijn Rasser, “A Conversation with Under Secretary of Commerce Alan F. Estevez,” Transcript, CNAS, October 27, 2022, <https://www.cnas.org/publications/transcript/a-conversation-with-under-secretary-of-commerce-alan-f-estevez>.

115 “G7 Foreign Ministers’ Statement on Preserving Peace and Stability Across the Taiwan Strait,” Media Note, Office of the Spokesperson, Department of State, August 3, 2022, <https://www.state.gov/g7-foreign-ministers-statement-on-preserving-peace-and-stability-across-the-taiwan-strait/#:~:text=We%20reiterate%20our%20shared%20and,of%20communication%20to%20prevent%20misunderstanding>.

116 White House, “Fact Sheet: Executive Order Addressing the Threat from Securities Investments That Finance Certain Companies of the People’s Republic of China,” White House Briefing Room, June 3, 2021, <https://www.whitehouse.gov/briefing-room/statements-releases/2021/06/03/fact-sheet-executive-order-addressing-the-threat-from-securities-investments-that-finance-certain-companies-of-the-peoples-republic-of-china/>.

3. Limit or prohibit outbound financial investments that support China's development of advanced or emerging technologies that have national security implications.

In earlier versions of the CHIPS and Science Act, the draft statute provided for review of transactions that transferred to China (or any “country of concern”) capabilities or ownership that “could result in an unacceptable risk to a national security capability.”¹¹⁷ While the provision was dropped from the final enacted statute, outside financial investments can support development by China of advanced or emerging technological capabilities with defense or other national security implications. The law does prohibit “material expansion of semiconductor manufacturing capacity in the People’s Republic of China” of state-of-the-art technology for a ten-year period after receiving any award under the statute.¹¹⁸

However, a broader approach beyond semiconductors is warranted. A recent analysis of the issues surrounding these concerns recommended restrictions on “flows of capital and associated expertise that can support the indigenous [Chinese] development of technology that would be controlled if it originated in the United States, or emerging technology that is likely to have national security implications.”¹¹⁹ Such restrictions would be very important additions to the types of controls that should be instituted to enhance deterrence and defense.

4. Prohibit the use of Chinese products by the United States and other ADEs in their defense and intelligence sectors.

As discussed above, China is not only the “pacing challenge” for the US Department of Defense, but also a recognized security challenge for the ADEs, as underscored by the AUKUS agreement, and Japan’s (and others’) concerns over “peace and stability in the Taiwan Strait.” Put

plainly, China is a potential military adversary and therefore Chinese products should not be utilized to provide any defense or intelligence capabilities to the United States or other ADEs. That limitation should extend to components and to dual-use items to mitigate risks that could affect the functionality of defense or intelligence capabilities.

By way of example, a Department of Defense report concluded that “procuring measurably secure microelectronics sources [e.g., semiconductors, transistors, diodes] is challenged by the potential for China, or countries under the influence of China, to tamper with or insert malicious functionality into microelectronics products.”¹²⁰ Similarly, the United States recently “temporarily halted deliveries of F-35 fighters following the discovery that the raw materials used for a magnet in the plane were produced in China,”¹²¹ although ultimately performance appears not to be affected. Most recently, the Federal Communications Commission effectively banned the use of Chinese telecommunications capabilities in the United States.¹²²

5. Prohibit the use of Chinese software for key critical infrastructures in the United States and other ADEs including the electric grid, pipelines, air, rail, ports, finance, health, and water.

The Director of National Intelligence has described China’s very substantial cyber capabilities:

China almost certainly is capable of launching cyber attacks that would disrupt critical infrastructure services within the United States, including against oil and gas pipelines and rail systems. . . . China’s cyber-espionage operations have included compromising telecommunications firms, providers of managed services and broadly used software, and other targets potentially rich in follow-on opportu-

117 Venable LLP, “A CFIUS-Type Review for Overseas Investment? Beware the Outbound Investment Review Framework Proposed in the COMPETES Act,” JD Supra (website), February 18, 2022, <https://www.jdsupra.com/legalnews/a-cfius-type-review-for-overseas-9974345/>.

118 Definition of a legacy semiconductor within Pub. L. 117–167, div. A, § 104, 136 Stat. 1390 (2022), as reprinted in 15 U.S.C. § 4652(a)(6), https://www.law.cornell.edu/definitions/uscode.php?width=840&height=800&iframe=true&def_id=15-USC-102889058-1966900778&term_occur=999&term_src=title:15:chapter:72A:section:4652.

119 Sarah Bauerle Danzman and Emily Kilcrease, “Sand in the Silicon: Designing an Outbound Investment Controls Mechanism,” Issue Brief, Atlantic Council, 2, https://www.atlanticcouncil.org/wp-content/uploads/2022/09/Sand_in_the_Silicon-Designing_an_Outbound_Investment_Controls_Mechanism.pdf.

120 Department of Defense, Securing Defense-Critical Supply Chains: An Action Plan Developed in Response to President Biden’s Executive Order 14017, 2022, 35, <https://media.defense.gov/2022/Feb/24/2002944158/-1/-1/1/DOD-EO-14017-REPORT-SECURING-DEFENSE-CRITICAL-SUPPLY-CHAINS.PDF>.

121 Stephen Losey, “Pentagon Suspends F-35 Deliveries Over Chinese Alloy in Magnet,” Defense News, September 7, 2022, <https://www.defensenews.com/air/2022/09/07/pentagon-suspends-f-35-deliveries-over-chinese-alloy-in-magnet/>.

122 “FCC Bans Authorizations for Devices That Pose National Security Threat,” Federal Communications Commission, News Release, November 25, 2022, <https://www.fcc.gov/document/fcc-bans-authorizations-devices-pose-national-security-threat>.

nities for intelligence collection, attack, or influence operations.¹²³

Those capabilities can be combined with Chinese-provided software that enables cyberattack vectors. Examples of such attacks include the SolarWinds and Hafnium attacks,¹²⁴ and demonstrate that the use of Chinese software, such as 5G software provided by Huawei, presents very substantial risks. Accordingly, the use of Chinese software for key critical infrastructures should be prohibited by the United States and the other ADEs. Such a prohibition should, at a minimum, cover the electric grid, pipelines, air, rail, ports, finance, health, and water.

6. Expand the scope of review of Chinese investments in the United States and the ADEs that present national security risks.

The Committee on Foreign Investment in the United States has statutory authority to review and, if required, prohibit, foreign investments that would undercut national security. Comparable authorities exist in the ADEs; the EU, as noted, has a regulation focused on screening such investments. The key challenge is to ensure that national security considerations are looked at broadly enough. The Biden administration promulgated an executive order that directs the Committee on Foreign Investment in the United States (CFIUS) to include in its reviews, among other matters, the impact on resilience of critical supply chains, leadership for advanced technologies, and cybersecurity.¹²⁵ The United States should work with the other members of the G10-plus to establish a comparable common approach.

C. Undertake Economic Actions to Offset Unfair Chinese Competition and Reduce Dependencies

1. Utilize tariffs and other limitations including a border-adjustment mechanism to offset the impact of Chinese sub-

sidies and other types of unfair competition that China's state-driven economy supports and that Chinese enterprises undertake.

The discussion above described both the breadth of Chinese subsidies to industries and the impact that tariffs nonetheless can have in affecting trade flows. So long as China continues its heavy subsidization of its industries, market-driven companies in the ADEs will often face an unfair competitive situation. The United States and other ADEs should determine how to respond to this issue.¹²⁶ The European Union countervailing mechanism is a start, but it does not take into account the systemic nature of the subsidies provided to Chinese industry. Due to the importance ADEs attach to having their companies move advanced and emerging technologies from the research and development stage and into competitive markets, there will be a need to evaluate whether Chinese companies in those new markets are obtaining unwarranted advantages through China's subsidization activities. Establishing a border-adjustment mechanism for key sectors likely would prove much more valuable than a one-by-one approach to review. The United States and other ADEs should discuss such a mechanism in the proposed G10-plus format and enact comparable legislation and the required regulatory regimes.

2. Establish resilient supply chains outside of China to reduce overreliance on the Chinese market through expanded use of tax credits, subsidies, and concessional financing, among other things, and specifically enhance energy-sector and other technology supply chains by developing a critical minerals financing initiative.

Resilient supply chains are needed for both economic and security reasons by the United States and the other ADEs. As the discussion on trade flows demonstrates, the ADEs rely heavily on trade in and from the China market. The impact of the Russia-Ukraine war has, however, underscored the dangers of dependencies in circumstances where se-

123 Office of the Director of National Intelligence, Annual Threat Assessment of the U.S. Intelligence Community, February 7, 2022, 8, <https://www.dni.gov/files/ODNI/documents/assessments/ATA-2022-Unclassified-Report.pdf>.

124 Charlie Osborne, "Everything You Need to Know About the Microsoft Exchange Server Hack," ZDNet, April 19, 2021, <https://www.zdnet.com/article/everything-you-need-to-know-about-microsoft-exchange-server-hack/>.

125 White House, "Fact Sheet: President Biden Signs Executive Order to Ensure Robust Reviews of Evolving National Security Risks by the Committee on Foreign Investment in the United States," White House Briefing Room, September 15, 2022, <https://www.whitehouse.gov/briefing-room/statements-releases/2022/09/15/fact-sheet-president-biden-signs-executive-order-to-ensure-robust-reviews-of-evolving-national-security-risks-by-the-committee-on-foreign-investment-in-the-united-states/>.

126 The United States and the European Union are themselves in dialogue as to how to reconcile subsidies available under the Inflation Reduction Act for products manufactured in the United States, with a desire not to undercut the economies of close allies. See Doug Palmer, "Biden 'Confident' U.S. Can Address EU Concerns about IRA Subsidies," Politico, December 1, 2022, <https://www.politico.com/news/2022/12/01/biden-eu-ira-subsidies-00071645>.

curity considerations, such as those surrounding Taiwan, could significantly affect trade flows. There are considerable benefits for the ADEs, including the United States, to maintain trade with China (though with the limitations noted above), but inasmuch as the Taiwan risks are real, an effective strategic approach should include diversification in order to reduce risk. Companies are already responding to these concerns and a well-known exemplar is Apple, which is moving a number of its facilities to India.¹²⁷

Coincident with the need for responding to the risks is the desirability for the ADEs generally to enhance trade and investment with the countries of the Global South. A variety of mechanisms can be utilized. For example, the Quad has six working groups undertaking economic and security cooperation.¹²⁸ Meanwhile, Australia and India are in the process of negotiating a free trade agreement.¹²⁹ Multilaterally, the G7 countries have agreed on the Partnership for Global Infrastructure Investment, which is intended to provide \$600 billion for infrastructure projects;¹³⁰ if accomplished, that will be an enormously valuable achievement.

The countries of the Global South also need capable industries as part of their economies. While the ADE governments do have multiple development financing programs, another worthwhile approach would be to build on the Japanese government's subsidy programs that incentivize companies to move out of China and into more reliable partnering nations. Such an effort could be supported by the use of tax credits, subsidies, and concessional financing. The United States and the other ADEs should utilize

the G10-plus format to develop a coordinated approach to expand such incentives with a focus on the Global South.

One specific critical area that demands high focus by the ADEs—both among themselves and with the countries of the Global South—involves the supply chains for energy, especially the critical materials necessary for a clean energy transition, and for other key sectors such as defense.

The key critical materials for the energy sector include cobalt, lithium, nickel, and rare earths. The demand for each is expected to increase by orders of magnitude. The Biden administration has projected:

As the world transitions to a clean energy economy, global demand for these critical minerals is set to skyrocket by 400-600 percent over the next several decades, and, for minerals such as lithium and graphite used in electric vehicle (EV) batteries, demand will increase by even more—as much as 4,000 percent.¹³¹

The United States as well as most ADEs rely on imports for these materials, including significant reliance on China. The White House has noted that the United States “is increasingly dependent on foreign sources for many of the processed versions of these minerals. Globally, China controls most of the market for processing and refining for cobalt, lithium, rare earths and other critical minerals.”¹³²

127 “The End of Apple’s Affair with China,” *Economist*, October 24, 2022, <https://www.economist.com/business/2022/10/24/the-end-of-apples-affair-with-china>.

128 The working groups are COVID-19 Response and Global Health Security, Climate, Critical and Emerging Technologies, Cyber, Space, and Infrastructure. See White House, “Fact Sheet: Quad Leaders’ Tokyo Summit 2022,” White House Briefing Room, May 23, 2022, <https://www.whitehouse.gov/briefing-room/statements-releases/2022/05/23/fact-sheet-quad-leaders-tokyo-summit-2022/>.

129 The agreement has been ratified by Australia, but not by India (as of this writing). Rod McGuirk, “Australia Ratifies Free Trade Deals with India and Britain,” *Associated Press*, November 21, 2022, <https://apnews.com/article/british-politics-india-australia-global-trade-business-d538020d808747d28b588a9c784ac207>.

130 White House, “Fact Sheet: President Biden and G7 Leaders Formally Launch the Partnership for Global Infrastructure and Investment,” White House Briefing Room, June 26, 2022, <https://www.whitehouse.gov/briefing-room/statements-releases/2022/06/26/fact-sheet-president-biden-and-g7-leaders-formally-launch-the-partnership-for-global-infrastructure-and-investment/>.

131 White House, “Fact Sheet: Securing a Made in America Supply Chain for Critical Minerals,” February 22, 2022, <https://www.whitehouse.gov/?s=Securing+a+Made+in+America+supply+chain>. The International Energy Agency (IEA) similarly has stated that the “shift to a clean energy system is set to drive a huge increase in the requirements for these minerals, meaning that the energy sector is emerging as a major force in mineral markets.” See IEA, *The Role of Critical Minerals in Clean Energy Transitions*, Executive Summary, 2021, <https://www.iea.org/reports/the-role-of-critical-minerals-in-clean-energy-transitions/executive-summary>. The IEA document describes demand: “Solar photovoltaic (PV) plants, wind farms and electric vehicles (EVs) generally require more minerals to build than their fossil fuel-based counterparts. A typical electric car requires six times the mineral inputs of a conventional car and an onshore wind plant requires nine times more mineral resources than a gas-fired plant. Since 2010 the average amount of minerals needed for a new unit of power generation capacity has increased by 50 percent as the share of renewables in new investment has risen.”

132 White House, “Fact Sheet: Securing a Made in America Supply Chain”; and IEA, *The Role of Critical Minerals in Clean Energy Transitions*.

Giving some specifics, a Biden administration report on building resilient supply chains found that China refines 60 percent of global lithium and 80 percent of cobalt.¹³³

Another analysis similarly described China's significant involvement in refining and processing critical minerals:

There are many weaknesses in the critical mineral supply chain, but U.S. import reliance on China presents one of the most immense risks. Currently, the [United States] imports over half of its minerals, with China supplying 80% of those imports. China controls approximately 55% of the global rare earth mining capability and 85% of rare earth findings as of 2020. Additionally, China's processing capability is five times greater than the combined global capacity for producing rare earth minerals, giving China a competitive advantage regarding low costs and infrastructure.¹³⁴

That degree of concentration presents security as well as economic issues. As the Secretary of Defense has stated, "Strategic and critical materials are vital to our national defense . . . enabling the United States to develop and sustain emerging technologies. . . . [and to] improve our warfighting capability." The DOD has made clear that the "concentration of global supply chains for strategic and critical materials in China creates risk of disruption."¹³⁵

The administration has made some useful efforts to deal with the problem including convening supply chain ministerial fora,¹³⁶ expanding activities with Canada and Australia,¹³⁷ and establishing contracts for rare earths

through the Defense Department.¹³⁸ However, a key requirement remains sufficient financing for the very large future requirements.

In the context of the recent G20 meeting, the United States and several other ADEs have pledged to provide Indonesia with \$20 billion in financing to support that country's clean energy transition from coal.¹³⁹ A comparable model should be developed for financing the necessary mining and processing of critical materials. As previously proposed by the author, a critical minerals financing initiative should be established:

The United States should develop a multilateral initiative that would undertake to finance the resourcing of critical minerals requirements for defense and national security needs and for the economy as a whole. Membership should include the United States, the EU, Australia, Canada, Japan, the Republic of Korea, and the United Kingdom. A combined effort would provide a mechanism to coordinate interactions with key producing countries as well as funding support for private-sector entities that would undertake the actual mining and processing. Such an effort should be combined with actions to support environmentally sound mining and processing efforts including the multilateral Energy Resource Governance Initiative. Finally, a coordinated effort would also allow for support to riskier but potentially highly important efforts such as deep-sea mining for critical materials.¹⁴⁰

Establishing such a critical minerals financing initiative would be an important project for the proposed G10-plus.

133 White House, Building Resilient Supply Chains, Revitalizing American Manufacturing, and Fostering Broad-Based Growth: 100-Day Reviews under Executive Order 14017, June 2021, 7, <https://www.whitehouse.gov/wp-content/uploads/2021/06/100-day-supply-chain-review-report.pdf>.

134 Jeremy Dasilva, "Securing the Critical Mineral Supply Chain Is Vital to the Future of the U.S. Military," American Security Project (website), October 20, 2021, <https://www.americansecurityproject.org/securing-the-critical-mineral-supply-chain-is-vital-to-the-future-of-the-us-military/>.

135 "The Defense Department's Strategic and Critical Materials Review," News Release, Department of Defense, June 8, 2021, <https://www.defense.gov/News/Releases/Release/Article/2649649/the-defense-departments-strategic-and-critical-materials-review/>.

136 "Joint Statement on Cooperation on Global Supply Chains," Media Note, Office of the Spokesperson, Department of State, July 20, 2022, <https://www.state.gov/supply-chain-ministerial-joint-statement/>.

137 "United States and Canada Forge Ahead on Critical Minerals Cooperation," Media Note, Office of the Spokesperson, Department of State, July 31, 2021, <https://www.state.gov/united-states-and-canada-forge-ahead-on-critical-minerals-cooperation/>; and "Next Steps on U.S.-Australia Critical Minerals Collaboration," Office of Public Affairs, Department of Commerce, November 17, 2021, <https://www.commerce.gov/news/press-releases/2021/11/next-steps-us-australia-critical-minerals-collaboration>.

138 "DOD Announces Rare Earth Element Award to Strengthen Domestic Industrial Base," Department of Defense Press Release, February 1, 2021, <https://www.defense.gov/News/Releases/Release/Article/2488672/dod-announces-rare-earth-element-award-to-strengthen-domestic-industrial-base/>; and "DOD Awards \$35 Million to MP Materials to Build U.S. Heavy Rare Earth Separation Capacity," DOD Press Release, February 22, 2022, <https://www.defense.gov/News/Releases/Release/Article/2488672/dod-announces-rare-earth-element-award-to-strengthen-domestic-industrial-base/>.

139 Brad Plumer, "Wealthy Nations Offer Indonesia \$20 Billion to Curb Coal," New York Times, November 15, 2022, <https://www.nytimes.com/2022/11/15/climate/indonesia-coal-agreement.html>.

140 Franklin D. Kramer, Free but Secure Trade: Priorities in Support of National Security, Atlantic Council, June 2022, 6, <https://www.atlanticcouncil.org/wp-content/uploads/2022/06/Free-but-Secure-Trade-Priorities-in-Support-of-National-Security.pdf>.

IV. CONCLUSION

China will remain an important part of the new globalization. But its relationships with the United States and the other advanced democratic economies have changed and will need to further change in important ways. A combination of selective decoupling focused on national security, advanced technologies, and critical infrastructures and the development of strategic supply chains outside China to

reduce dependencies will be the key elements of a new strategic approach. Establishing the G10-plus along with a multinational staff to help coordinate such actions will be invaluable. Successfully undertaking each of those efforts will be of critical importance to establishing strategic stability and economic prosperity for the United States and the advanced democratic nations.

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