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# PAMIR Executive Brief

## China Update

16 February 2023

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*“China’s National People’s Congress will review and approve China’s 2023 defense budget in March. The increase of China’s defense budget would indicate whether hardliners or moderates are dominating the central government’s decision-making.”*



# Executive Summary

- China has become increasingly confrontational toward the US as President Xi Jinping attempts to project an image of strength in the lead-up to the 5 March National People's Congress.
- Xi's "new pattern of development" calls for China to deal urgently with economic decoupling and focus on technological self-reliance and strengthening the manufacturing industry rather than the financial economy.
- USTR data indicates that China-origin goods, including those transshipped through Hong Kong, accounted for 75% of the value of counterfeit and pirated goods seized by US Customs and Border Protection in 2021.
- The US and the Philippines expanded the scope of their Enhanced Defense Cooperation Agreement (EDCA) to add four military bases that would play a critical role in a possible Chinese military incursion of Taiwan. US Defense Secretary Austin called the accord "a big deal; it is really a big deal."



# US-China Relations

China has taken an increasingly confrontational stand against the US in the wake of the spy balloon incident, accusing the US of engaging in “information and public opinion warfare.” On 12 February China countered with claims of shooting down a “foreign balloon” in the Bohai Sea where the PLA Navy was conducting exercises and the following day accused the US of more than 10 balloon intrusions into Chinese airspace. Pamir questions the veracity of these claims.

With the National People’s Congress opening on 5 March, President Xi Jinping cannot afford to be seen as weak towards the US. China is publicly demanding return of the balloon wreckage and threatening to take further action, but internally, Beijing is trying to move beyond the incident.

Three signposts could indicate the direction of US-China relations in the coming months:

- Proposed ban of select US investments in China;
- US Speaker McCarthy’s likely visit to Taiwan in April;
- Congressional bills that would revoke China’s Most Favored Nation status.

On 13 February China’s Foreign Ministry announced that Politburo member WANG Yi in charge of international relations will attend the 59th Munich Security Conference on 17-19 February in Germany. The US State Department has not confirmed if Secretary Blinken will meet with his Chinese counterpart in Munich.

*“The number of global non-immigration visas issued in 2022 almost returned to 2019 pre-Covid levels, but the US Embassy in Beijing and its consulates ...issued only 10% of the number issued in 2019.”*

Recently released US State Department data confirmed that China’s Zero-Covid policy severely reduced travel compared to other countries. The number of global non-immigration visas issued in 2022 almost returned to 2019 pre-Covid levels, but the US Embassy in Beijing and its consulates in Shanghai, Shenyang, and Guangzhou issued only 10% of the number issued in 2019. Chinese social media are trying to refocus blame on the US and are full of comments about the increased difficulty of getting a visa due to US restrictions, particularly for STEM students.

## Military Use of Balloons

High-altitude balloons (HABs) are an integral part of what the Chinese military views as the newest battlefield sitting between 12 and 60 miles above the earth's surface, above flightpaths and below satellites, in a layer called "near space."

This is the same space used by ballistic and hypersonic missiles. China's technical leader in HAB development and employment is the China Academy of Science (CAS), which in 2019 established its Aerospace Information Research Institute (AIR) by consolidating the Institute of Electronics (IECAS), Institute of Remote Sensing and Digital Earth (RADI), and Academy of Opto-Electronics (AOE).

Since April 2014, when President Xi instructed the PLA Air Force to "speed up air and space integration and sharpen offensive and defensive capabilities," China has worked to improve its HAB capabilities and to use light-than-air vehicles as launch pads from near space for hypersonic and ballistic missiles and unmanned vehicles.

China has developed HABs for military reconnaissance, surveillance, communications relay, and electronic countermeasures. China first revealed an export version of its military HAB, the JY-400 In-Air Reconnaissance and Surveillance System, in 2014 and displayed the latest version at the November 2022 Zhuhai Air Show.

*“China has developed HABs for military reconnaissance, surveillance, communications relay, and electronic countermeasures.”*



# China's Economy

President Xi chaired a Politburo session on 31 January to promulgate his “new pattern of development,” which calls for China to deal urgently with decoupling with the US and sets new guidelines for China’s efforts in the coming years.

Xi’s new policy will focus on increasing domestic consumption while opening to the outside world. Its aim is to allow China to survive, compete, develop, and sustain itself in unpredictable circumstances.

Xi called for building a modern industrial system that is “independent, controllable, safe, reliable, and highly competitive.” He said China’s new pattern of development will focus on the manufacturing industry rather than the financial economy. He is requiring improvements to China’s supply chains and promoting greater global dependence on China.

Xi emphasized the importance of science and technology and the need for China to become a global leader in important fields, a pioneer in cutting-edge interdisciplinary areas, and a major scientific center and innovation hub for the world." He stressed quickening the pace of tech self-reliance and called for creating a new eco-system to integrate innovation, production, talent training, and recruitment.

China dominates 96% of the global large photovoltaic wafer market. It is the only country in the world that has the technology to produce 182-210mm photovoltaic wafers. China has made significant progress in laser radar technology, which is essential for auto driving. The Chinese government predicts that China will have 400,000 to 500,000 cars equipped with laser radar automation systems in 2023.

## Xi’s New Pattern of Development

- Continue supply-side reform
- Improve the market environment
- Expand people’s income
- Launch new infrastructure projects and expand investments in high-tech and strategic newly emerging industries
- Rejuvenate private investment enthusiasm
- Resolve debt problems
- Advance balanced development of urban and rural areas and regional development
- Encourage qualitative development of the Belt and Road Initiative
- Participate actively in world trade negotiations with increased China voices and promote an “open, multipolar and stable world economic order”



According to 2022 foreign trade data from the US Commerce Department released on 7 February, US-China trade in goods climbed to a record \$690.6 billion in 2022, exceeding the record set in 2018.

- ✓ US imports from China reached \$536.8 billion, while US exports climbed to an all-time high of \$153.8 billion. Exports of agriculture products to China were \$40.85 billion, one-fifth of total US agriculture exports.
- ✓ The deficit with China widened 8% to \$382.9 billion and was the second highest after the \$419.4 billion record in 2018. China remains the third largest US trading partner (13% of total trade) after Canada (14.9%) and Mexico (14.7%).

## Trade Disputes

China is imposing restrictive export controls of Chinese sensitive technologies – Beijing’s reaction to the tech war with the US and its allies and partners.

- China’s Ministry of Commerce and Ministry of Science and Technology are finalizing the 2023 Catalogue of Technologies Prohibited or Restricted from Export, which will ban 24 technology categories for export and designate 115 for restrictive exporting. A new category added to the export ban list is technology related to human cell cloning, genetic editing, and CRISPR. Photovoltaic wafer manufacturing and laser radar technologies are also included on the restrictive list.

Counterfeit and pirated goods from China topped the US Trade Representative Office’s newly published 2022 Review of Notorious Markets for Counterfeiting and Piracy – also known as the Notorious Market List. The List identified 39 online markets and 33 physical markets.

*“China dominates 96% of the global large photovoltaic wafer market. It is the only country in the world that has the technology to produce 182-210mm photovoltaic wafers. China has made significant progress in laser radar technology, which is essential for auto driving.”*

USTR said that China-origin goods, together with goods transshipped from China to Hong Kong, accounted for 75% of the value of counterfeit and pirated goods seized by US Customs and Border Protection in 2021.





**IN 2021  
HUAWEI  
SPENT 22.4%  
OF ITS REVENUE ON  
R&D**

- Tencent and Alibaba e-commerce platforms were added to the list. On 9 February China's Ministry of Commerce called the US allegations "unprofessional and irresponsible." Tencent and Alibaba also denied any wrongdoing.

On 31 January Western media reported that the Biden administration stopped approving licenses for US companies, and companies with US components like Samsung and TSMC, to export nearly all items to Huawei, "including those for 4G, Wi-Fi 6 & 7, artificial intelligence, and high-performance computing and cloud."

The Chinese government and state media predictably have criticized the US move. This latest US ban could substantially debilitate Huawei's cellphone and laptop computer business.

- In 2015 Huawei produced 40 million cellphones and had 16.7% of the global market, but under US pressure only produced about 4 million cellphones and had less than 2% of the market in 2022. Huawei's 5G station business also has been greatly affected. Huawei's 2022 revenue was RMB 636.9 billion, nearly unchanged from 2021.

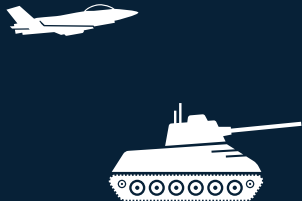
*China dominates 96% of the global large photovoltaic wafer market. It is the only country in the world that has the technology to produce 182-210mm photovoltaic wafers. China has made significant progress in laser radar technology, which is essential for auto driving.*

One of Huawei's lifelines could be its patent revenues, which from 2019 to 2021 produced licensing income of \$1.2 billion. In 2022 Huawei filed a record of more than 11,000 patent applications with the US, according to IFI Claims Patent Services, ranking it #4 in patent filings after Samsung, IBM, and TSMC.

Huawei's own R&D could potentially rescue the company. In 2021 Huawei spent 22.4% of its revenue on R&D, bringing its total R&D expenditure to \$120 billion over the past decade. The proportion of US components used in Huawei's 5G Small Cell has dropped from 27% in 2020 to less than 1% in 2022, but it is not clear if R&D was the sole driver.

# Military Tensions

The US and the Philippines signed an accord on 1 February under the Enhanced Defense Cooperation Agreement (EDCA) for the US to add four military bases in the Philippines, bringing the total available to pre-position military equipment and rotate US forces to nine. In addition to accelerating implementation of the EDCA, which focuses on combined training, exercises, and force interoperability, the Biden administration has increased efforts to boost US military presence and cooperation with other allies in the Western Pacific:



- In November 2022 the US diverted a dozen F-22 fighters from Germany to the US military base in Kadena, Okinawa.
- In December 2022 Japan added an infantry regiment to its 15th Brigade responsible for defense of Japan's southern and western-most Okinawan Prefecture. One of the Brigade's bases will be only 186 miles from Taiwan.
- On 12 January the US redesignated the 12th Marine Regiment on Okinawa as the 12th Marine Littoral Regiment, equipped with advanced intelligence and surveillance capabilities, and the ability to fire antiship missiles.
- On 26 January the US Marine Corps reactivated Camp Blaz in Guam after 70 years.
- The 2023 National Defense Authorization Act authorizes funds for military construction projects throughout the Pacific, including the US territory of Tinian in the Northern Mariana Islands.
- Advanced military assets will be deployed to South Korea, Japan, and Australia.



*“From China’s viewpoint, the EDCA expansion poses a serious threat to China’s security interests, particularly in the event of a Chinese invasion of Taiwan. US Defense Secretary Austin said in Manila, “It is a big deal; it is really a big deal.”*”

Chinese military experts perceive that the new US-Philippines agreement completes the US military encirclement of China along the first island chain in the Western Pacific. One of the new bases with US access is in Cagayan, which is just 118 miles from Taiwan and represents a choke point to the strategic Basi Channel in the South China Sea.

From China’s viewpoint, the EDCA expansion poses a serious threat to China’s security interests, particularly in the event of a Chinese invasion of Taiwan. US Defense Secretary Austin said in Manila, “It is a big deal; it is really a big deal.” Some Chinese commentators cite these recent developments to advocate for more defense build-up including increasing the number of China’s nuclear warheads and hypersonic missiles.

Some Chinese commentators downplayed these developments, arguing that the US owns or has access to more than 100 military bases around China. Given today’s technology, another four bases in the Philippines make no major difference. They suggest that China should focus on its own agenda of national development and point out that several Asian countries, like the Philippines, are just expedient in their policies, trying to benefit economically from China and militarily from the US.

- For example, the US is promising \$82 million to the Philippines to improve facilities at the four bases. These Chinese commentators opine that China should win these countries over, rather than push them to the US side and that increased military presence in Western Pacific will add significant financial stress to the US economy.

Beijing has criticized the US-Philippine deal. China’s Foreign Ministry said, “The US side, out of selfish interests, holds on to a zero-sum mentality and keeps strengthening military deployment in the Asia-Pacific.” China’s embassy in Manila also issued a similar statement, saying China hoped that the Philippines “resists being taken advantage of and dragged into troubled waters.”

China’s National People’s Congress will review and approve China’s 2023 defense budget in March. The increase of China’s defense budget would indicate whether hardliners or moderates are dominating the central government’s decision-making.





# China-Russia Cooperation

China-Russia cooperation is accelerating as measured by annual trade, diplomatic engagements, and joint military exercises. President Xi plans to visit Russia in late spring, and in preparation Politburo member Wang Yi is expected to travel to Moscow on 20 February.



- China imported a record 3.8 million tons of Russian oil in January, according to Russian media, and the purchase price was the highest in the world – \$72.51 to \$83.67 per barrel – exceeding caps imposed by the West.
- Bilateral trade in 2022 grew 29.3% over 2021, according to China Customs.
- On 4 February Russian Customs data showed China had provided navigation equipment, parts for fighter jets and helicopters, and other military technology equipment in 2022, according to western media reports. Two-thirds of Russia's chip imports came from China. China's Foreign Ministry only said the two countries engage in normal trade.

# Strategic outcomes

## Absence of top-level communications

Pamir assesses that the absence of top-level communication channels between the US and China is hindering Washington and Beijing from mitigating risk and miscalculations. The spy balloon incident revealed the ineffectiveness of China's central control system. Beijing's two-day delayed and muddled initial response followed by subsequent aggressive statements against the US demonstrated China's mercurial crisis management approach.

### LEVEL OF CONCERN



## Risks of further US-China friction

Pamir expects that forthcoming US actions – possible ban on select technology-related US investments in China and the high probability of US House Speaker McCarthy's visit to Taiwan – will further exacerbate bilateral friction with potential repercussions for US companies operating in greater China.

### LEVEL OF CONCERN



### Level of Concern indicators - what they mean

- 1 - indicates no change to the status quo
- 2 - indicates escalating tensions
- 3 - indicates aggressive escalation
- 4 - indicates high probability of impending crisis event
- 5 - indicates a full-scale crisis or conflict situation.

### How we calculate them

- Frequency of references to subject in Chinese-language official government statements, credible press reporting, and social media
- Frequency of references to subject in English-language official government statements, credible press reporting, and social media from the US, EU, UK, Australia, Japan, etc.
- Consistency of historical, current, and emerging trendlines related to the subject
- Aberrations in official Chinese-language policy formulations
- Strategic shifts in official Chinese government and military signaling through diplomatic, information, military, and economic actions and behavior

**Analytic Methodology:** internal monitoring with quantitative and qualitative analysis of Chinese media and propaganda; comparative trend analysis, intelligence tradecraft; other proprietary methods.

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