Report number: PAMIR2023020101

# PAMIR Executive Brief

## China Update

1 February 2023

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## PAMIR Executive Brief - 1 February 2023

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# Executive Summary

- A senior US military commander raised the prospect of a conflict with China in 2025. Despite distancing of the US Department of Defense from the assertion, Beijing will likely view the commander's statement as probable US intent to not abandon Taiwan.
- Boeing is losing its share of a rapidly expanding China market to Airbus and, potentially, Chinese domestic manufacturers.
- China has delisted all its state-owned enterprises from the US stock market, probably to avoid mandated audits and protect these assets in the event of future military conflict.
- Chinese firms have been providing satellite imagery support to the Ukraine war efforts of Russia's Wagner Group and have been hit with US sanctions.
- South Korea indicted a group of five for passing advanced semiconductor manufacturing technology to China. In a related development, the US, Holland, and Japan expanded restrictions on equipment sales to China.
- Beijing is exerting greater control over the Hong Kong populace and judiciary, and the city has created an incentive program to attract talents to replace the ongoing exodus.

# US-China Relations

## Military Tensions

### Minihan's memo and the 'first island chain'

General Mike Minihan, Commander of the US Air Mobility Command (AMC), sent out a memo on 27 January telling his troops, "I hope I am wrong, my gut tells me [China and US] will fight in 2025," as first reported by NBC News.

He pointed to 2024 presidential elections in both Taiwan and the US, predicting the US will be "distracted" and China will have an opportunity to move on Taiwan.  He wants his units to be prepared to include building "a fortified, ready, integrated, agile Joint Force Maneuver Team ready to fight and win inside the first island chain" (i.e., the defensive line that runs from Japan's main islands through Okinawa, Taiwan, and the Philippines south to Malaysia).


**General Minihan's Memo:**
Minihan's memo was sent to all air wing commanders in AMC and other Air Force operational commanders ordering them to report by the end of February all major efforts being undertaken to prepare for a conflict with China.  He directed all AMC personnel to "consider their personal affairs" and ensure that their legal matters are in order should they become combat fatalities.

The Pentagon press secretary commented on the report only by saying, "The National Defense Strategy makes clear that China is the pacing challenge for the Department of Defense, and our focus remains on working alongside allies and partners to preserve a peaceful, free, and open Indo-Pacific."  According to an unnamed Pentagon official speaking to NBC News, "These comments are not representative of the department's view on China."

**The reaction of Chinese state media:**
Chinese state media blasted Minihan's memo and said it was designed to justify the enormous US defense budget.  One article published by the People's Daily, China's most authoritative vehicle for government views, said China should not be influenced by US war mongering rhetoric but "stay focused on China's own agenda…Time is on China's side to resolve the Taiwan issue."

> In November 2020 President Trump signed an executive order to force three Chinese SOEs to withdraw from the US stock market for alleged ties with the Chinese military.
>
> Given current China-US relations, the Chinese government is worried that additional Chinese SOEs could be targeted. More importantly, seeing the consequences Russia faced after its invasion of Ukraine, China fears that SOEs could be the first group of Chinese companies whose assets the US would freeze, if there is a major conflict between the two countries.

## Aviation

### Boeing loses out in rapidly expanding market

Boeing is fast losing the China market. In 2022 Boeing delivered only eight aircraft to China while Airbus delivered more than 100. China announced a purchase of 292 Airbus aircraft in July 2022 and another 140 in November.

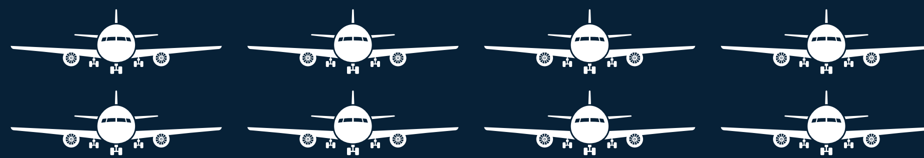
Meanwhile, Commercial Aircraft Corporation of China (COMAC) delivered its first domestic large passenger plane, the C919, to commercial service in December. COMAC said it has received more than 1,000 orders for its C919.

According to a COMAC estimate, more than 40,000 passenger aircraft will be needed globally over the next 20 years for a total value of $6.4 trillion. China will be the world's largest aviation market with a requirement for 9,284 aircraft.

By 2041, China will have 10,007 passenger aircraft or 21.1% of the world total.

**BY 2041 CHINA WILL HAVE**
**10,007**
**PASSENGER AIRCRAFT OR**
**21.1%**
**OF THE WORLD TOTAL**

# IN 2022 BOEING DELIVERED ONLY EIGHT AIRCRAFT TO CHINA

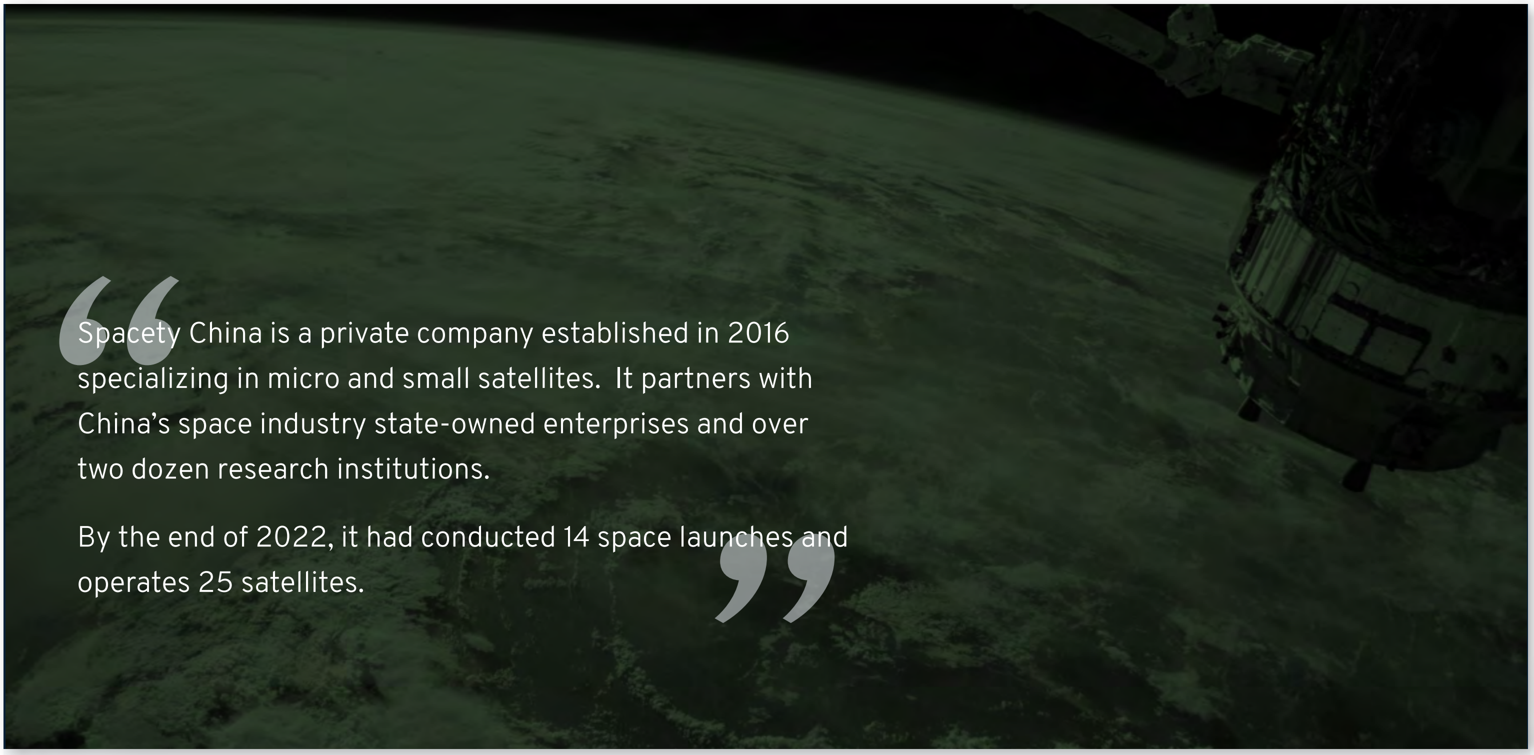


### Dodging the prospect of invasive audits or potential seizure

China Southern Airlines' decision in January to withdraw from the US stock market marks the total delisting of Chinese state-owned enterprises (SOEs). As of October 2020, 13 Chinese SOEs were listed in US markets. Earlier in January China Eastern applied to delist.

- Last August, China and the US reached an agreement on auditing Chinese companies listed on the US stock market. US auditors successfully conducted their first round of auditing in December 2022. However, Chinese media commentators say the Chinese government decision to withdraw all Chinese SOEs from the US stock market is for strategic considerations.
- In November 2020 President Trump signed an executive order to force three Chinese SOEs to withdraw from the US stock market for alleged ties with the Chinese military. Given current China-US relations, the Chinese government is worried that additional Chinese SOEs could be targeted. More importantly, seeing the consequences Russia faced after its invasion of Ukraine, China fears that SOEs could be the first group of Chinese companies whose assets the US would freeze, if there is a major conflict between the two countries.

**CHINA HAS A FORECAST REQUIREMENT OF 9,284 AIRCRAFT OVER THE NEXT 20 YEARS**



> "Spacety China is a private company established in 2016 specializing in micro and small satellites. It partners with China's space industry state-owned enterprises and over two dozen research institutions.
>
> By the end of 2022, it had conducted 14 space launches and operates 25 satellites."

## Space

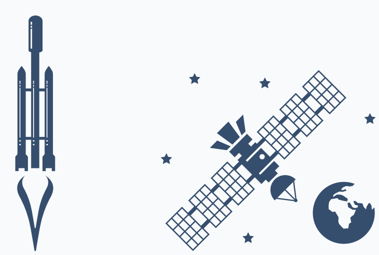
### US sanctions Spacety for support of Wagner Group

On 26 January the US government sanctioned China's Changsha Tianyi Space Science and Technology Research Institute (Spacety China) and its subsidiary, Spacety Luxemburg S.A., for providing support to the Wagner Group, Russia's private military company involved in the Ukraine war.

Spacety China is accused of providing "Terra Tech synthetic aperture radar satellite imagery orders over locations in Ukraine. These images were gathered to enable Wagner combat operations in Ukraine."

Earlier on 24 January, "The US has determined that some Chinese companies are providing non-lethal assistance to Russia for use in the Ukraine war and officials are noting their concerns to the Chinese government," according to western media reporting.

White House Press Secretary Karine Jean Pierre said, "We will continue to communicate to China the implications of providing material support to Russia's war against Ukraine."



**SPACETY HAS CONDUCTED**
**14 SPACE**
**LAUNCHES AND OPERATES**
**25 SATELLITES**


## Semiconductors

### South Korea indicts suspected technology thieves

On 16 January South Korea's Suwon District Prosecutor's Office indicted five people for passing to China the world's first supercritical semiconductor cleaning equipment technology developed by SEMES, a key subsidiary of Samsung Electronics. The SEMES equipment can lower the defect rate of ultra-micro semiconductors and is designated by the South Korean government as "a core national technology."

Pamir determines the case to be a classic instance of insider knowledge used to perpetrate technology theft. According to the prosecutor's office, one of the indicted was a former SEMES employee. He quit SEMES in 2016 and set up his own company in 2019. He acquired SEMES key drawings through the CEO of a SEMES partner company, then handed the drawings over to a technology broker in June 2021. The broker sold the technology to China.

The prosecutor's office said, "From 2009 to 2021, SEMES invested about 35 billion won ($284 million) in research and development of the supercritical technology. This crime caused a direct loss of over 35 billion won, but it is feared that SEMES will suffer a loss of over [$325 million] annually if orders to SEMES drop by only 10% due to a decline in the company's technology power."

According to South Korean media, SEMES and Shibaura Mechatronics of Japan are the only two companies that have developed this technology. Pamir observes that China is putting a lot of resources into developing its chip independence – including through commercial espionage – to combat US sanctions.

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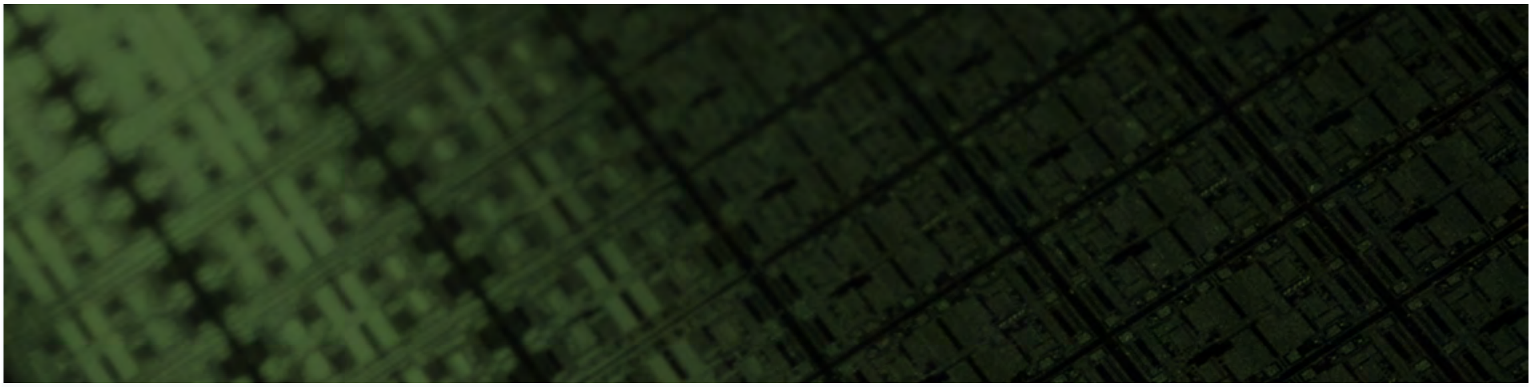


### Sanctions gather pace

On 17 January the US included Macau in its chip export ban out of concern that Macau could be used as a backdoor through which banned products could make their way to China; Hong Kong already is on the banned list. Both Macau and Hong Kong are independent members of WTO as customs territories separate from China.

On 29 January Holland's national TV, NOS, reported that millions of semiconductors made by Nexperia and NXP Semiconductors had been sold to Russia by Chinese intermediaries. Sinno Electronics, a Chinese company sanctioned by the US, is the largest intermediary. The Dutch Foreign Ministry said it is concerned about the report and is working with other EU partners to address the problem.

- Nexperia, headquartered in the Netherlands, is a Chinese-owned company with production facilities in England and Germany. NXP is a Dutch company. Qualcomm tried to acquire NXP in 2016 but failed due to blocking by China's antitrust authority.

The US, Holland, and Japan reached an agreement on 27 January to restrict export of some advanced chip manufacturing equipment to China. The export control will apply to the world's top three chip manufacturers: ASML Holding NV of Holland, and Nikon Corp and Tokyo Electron of Japan.

The Chinese government-run Global Times criticized US pressure on Holland and Japan to agree to the deal and said the US action will only make China more innovative and self-reliant.

- In 2021, 33% of Japan's semiconductor equipment was sold to China; ASML had over €2 billion in revenue from China, accounting for 15% of its total. ASML currently has more than 1,500 employees in China or 14% of its labor force.

On 29 January Thierry Breton, EU's Commissioner for Internal-Market, expressed EU support for US resolve to choke China's advanced chip technology. Speaking at a CSIS seminar in Washington, DC, he said, "We fully agree with the objective of depriving China of the most advanced chips."

He further stressed, "We cannot allow China to access the most advanced technologies." An editorial in the Chinese Global Times called Breton's remarks "arrogant and ignorant [and] do not serve the EU's interests in any way."

It warned, "We have to make one thing crystal clear: China's development has never and will never rely on charity from any country or region."

# Hong Kong

Two developments indicate Beijing will continue its heavy-handed control over Hong Kong.

**On 14 January**

The Chinese government appointed Zheng Yanxiong, 59, as the new director of the Liaison Office of the Central People's Government in Hong Kong, the top representative of the Chinese government in the city.

Zheng previously served as Director of the Hong Kong Office for Safeguarding National Security after China imposed a national security law in Hong Kong in June 2020.

Zheng is known for cracking down on a mass protest in the village of Wukan, Guangdong Province, in 2011 when he was Party Secretary of Shanwei City. Zheng has been very hostile to the foreign press and once said, "If foreign media could be trusted, then pigs could climb trees." In August 2020 the US sanctioned Zheng for his role in suppressing Hong Kong democracy.

**On 17 January**

Hong Kong's top executive officer, John Lee, said that Hong Kong will enact an Anti-Subversion Law no later than in 2024. The law covers seven offenses: treason; secession; sedition; subversion against China's central government; theft of state secrets; foreign political groups conducting political activities in the city; and local bodies establishing ties with foreign counterparts.

In 2003 the Hong Kong government had to shelve enactment of Article 23 after mass demonstrations spread throughout the city.

Greg May, US Consul General in Hong Kong, said Hong Kong's implementation of the National Security Law imposed by Beijing in 2022 "could further undermine the independence of Hong Kong's judiciary system by expanding the Hong Kong executive branch authority to make decisions affecting cases without judicial oversight." Speaking on 25 January during a seminar organized by the Center for Strategic and International Studies, May added, "In light of these and other developments, companies should be aware that the risks faced in mainland China are now increasingly present here in Hong Kong."

*...companies should be aware that the risks faced in mainland China are now increasingly present here in Hong Kong.*

***Greg May,***
***US Consul General, Hong Kong***

Although May's warnings about Beijing commandeering the Hong Kong judiciary are not new assessments, China's Foreign Ministry representative in Hong Kong immediately issued a statement repeating the notion of hostile foreign intervention in Chinese affairs: May "vilified Hong Kong's rule of law and freedom, showed support for anti-China forces in Hong Kong, and talked down Hong Kong's development prospects, [which] only exposed his sinister intention of disrupting Hong Kong and containing China." The Hong Kong government also condemned May's remarks.

In apparent expectation that the tightening of security laws and a declining judicial system will negatively impact the city's ability to retain talent and businesses, Hong Kong's government has introduced an aggressive recruitment program —Top Talent Pass Scheme (TTPS)— to boost Hong Kong's competitiveness. US Consul General May estimates that about 15,000 US citizens, or 20% of Americans in the city as of 2019, have left Hong Kong over the last two years. Covid would have been one reason for the foreign exodus from Hong Kong, where over one-third of the populace contracted the virus, but experts in many fields have been leaving for more hospitable work environments.

TTPS recipients and their families will be given special immigration privileges to the city. Criteria for TTPS mirror those of many mainland incentive programs, targeting experts with annual income of HK$2.5 million (US$320k); graduation from a Top 100-ranked university; and at least three years of work experience.

The HK government expects to recruit 45,000 talents annually through TTPS and already has approved 90% of the 5,300 applications it received within two weeks of the program's introduction. There is yet no breakdown on the relative percentages of incoming foreigners and "returning Chinese" is these numbers.

On 27 January China's Foreign Ministry denounced a US decision to extend Deferred Enforced Departure (DED) for certain Hong Kong persons as "smearing Hong Kong's rule of law and human rights record" and "interfering in Hong Kong and China's internal affairs." The policy allows these Hong Kong residents to remain in the US on the grounds of China's continued violation of human rights in Hong Kong.

Pamir estimates that the actual Covid-related death rate is considerably higher than official data from the Chinese government.

# Covid Management

Local Chinese governments suffered enormous economic losses from the now defunct Zero-Covid policy. Data from Guangdong Province showed the provincial government devoted RMB 71.139 billion ($10.94 billion) to fight Covid in 2022, up 57% over 2021. Over the last three years, the province spent RMB 146.793 billion ($22.5 billion) on Covid control. The unsustainable financial burden was one of the main reasons for the Chinese government to abandon its Zero-Covid policy in December.

Dr. Wu Zunyu, Chief Epidemiologist for China's CDC, reported that about 80% of 1.4 billion Chinese had contracted Covid and, as a result, "The likelihood of a large nationwide rebound or a second wave in the next two to three months is now small."

Meanwhile, as of 17 January, China's National Health Commission (NHC) said the number of fever cases in China dropped 94% from the peak on 23 December; the number of severe Covid cases dropped 44.3% from their peak on 5 January. China's CDC also reported that China's Covid-related deaths were trending down from 59,938 (8 December–12 January); 12,658 (13 19 January); to 6,364 (20-26 January); however, China only counts Covid deaths when patients die in a hospital.

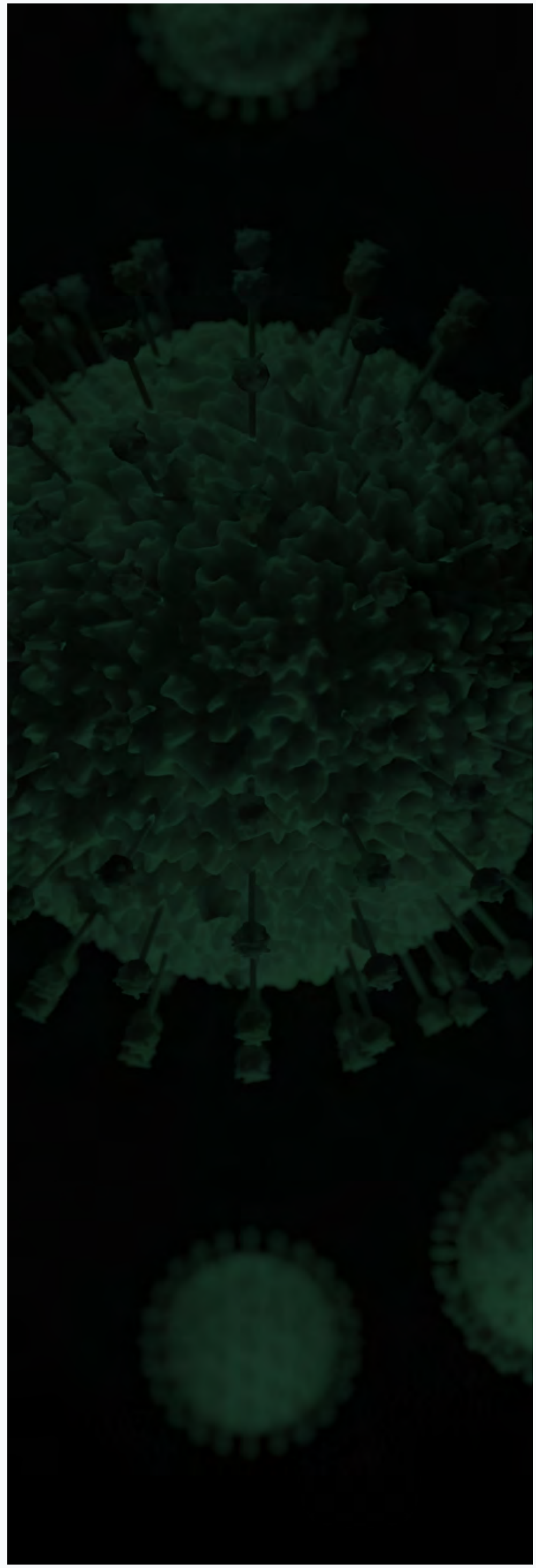
Pamir estimates that the actual Covid-related death rate is considerably higher than official data from the Chinese government.

DATA FROM GUANGDONG PROVINCE
SHOWS THE PROVINCIAL GOVERNMENT SPENT
**$22.5 BILLION**
ON COVID CONTROL
OVER THE LAST THREE YEARS

On 20 January Beijing announced that Chinese tourist companies can resume organizing overseas tour groups to designated countries starting 6 February. The 20 authorized countries on the government's initial list are mostly in Asia, but political considerations are also clear in the decision.

- For example, Japan and South Korea, two of the most popular Chinese tourist designations, are not included—the Chinese government recently criticized Japan and South Korea for Covid discrimination against travelers from China. In Europe, only Switzerland and Hungary, which are viewed as China-friendly, and China's ally, Russia, and are on the list. New Zealand is also an approved destination, while Australia, another popular Chinese vacation spot, is not authorized due to tension between the two countries.
- On 23 January Japan resumed processing visas for Chinese; on 29 January China followed with a resumption of visa processing for Japan.

The number of individual Chinese traveling internationally for Lunar New Year jumped 640% compared with last year, according to China's top travel website, Xiecheng (trip.com). After the government relaxed future group travel, searches for overseas tours on Xiecheng increased 330%. Thailand, Vietnam, Singapore, Indonesia, and Cambodia were top searches. According to the UN World Tourism Organization, China is the world's largest tourist source. In pre-pandemic 2019, 155 million Chinese tourists went overseas and spent $254.6 billion or one-fifth of the world total.



# Strategic outcomes

### Escalating US hostilities

LEVEL OF CONCERN

5 4 3 **2** 1

Pamir assesses that China's leadership will view General Minihan's memo as official US policy, despite the Pentagon's downplaying. The Pentagon's comments on China as a "pacing challenge" confirm that the timeline for potential hostilities is contracting. China's total withdrawal of state-owned assets from US stock markets further suggests that Beijing is taking steps to protect strategic holdings from possible US sanctions.

### Hong Kong's Anti-Subversion Law

LEVEL OF CONCERN

5 4 **3** 2 1

Hong Kong's stated commitment to enacting its Anti-Subversion Law will act as a deterrent to investment and is certain to spur the relocation of foreign businesses to cities with stable and predictable legal frameworks.

### 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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