EST 2020

AMERICAN COMPASS

POLICY

A Hard Break from China

Protecting the American Market from Subversion by the CCP

June 2023

Table of Contents

Executive Summary

The dream of a liberal, democratic China is decidedly dead, and U.S. policymakers are finally beginning to grapple with the reality of having an authoritarian adversary as a global peer. But this thinking remains dangerously underdeveloped and naïve, as reflected in recent speeches by Secretary of the Treasury Janet Yellen and National Security Advisor Jake Sullivan, in which they emphasize narrow concerns about military technology while expressing optimism that our two nations can remain integrated economically. Yellen still envisions "a growing China that plays by the rules" and fosters "rising demand for U.S. products and services and more dynamic U.S. industries," while Sullivan advocated a policy of "de-risking and diversifying, not decoupling."

The China challenge is not only, or even primarily, one of national security. It is that too, to be sure. But the fundamental problem is that America's free market economy is incompatible with China's state-controlled one, and American liberty and democracy are incompatible with Chinese communism. America must sever its economic relationship with China to protect its market from subversion by the Chinese Communist Party (CCP). Disentangling our economies will be costly, but the alternative of accepting CCP control of our assets and investments, dominance in our supply chains, and influence over our institutions will cost far more. This paper demonstrates how integration with China undermines American economic sovereignty across three critical dimensions and describes the unprecedented policy response necessary.

I. Investment

American capital flowing into China implicates American investors in the People's Republic of China's (PRC) human rights abuses, subsidizes development of its military capabilities, and subjects retirees and other savers to the risks of a poorly regulated and CCP-dominated market. When American firms invest directly in China, typically through state-mandated and -subsidized joint ventures, they transfer jobs and technology across the Pacific. In both cases, the PRC actively distorts market incentives to attract investment and then uses its leverage over the investors to force support for CCP priorities and propaganda. Flowing in the other direction, PRC-based capital is taking control of American corporations and real estate, establishing a foothold in the American market that current U.S. law is incapable of managing.

The United States should:

1. Prohibit PRC-based entities from acquiring and operating in the American market, participating in American funds, and holding American real estate;

2. Prohibit American firms from forming joint ventures in or transferring technology to China and American investors from providing capital to PRC-based firms; and

3. Reject the premise of a bilateral investment treaty with China or any request for assistance to American firms in the Chinese legal system.

II. Supply Chains

The PRC has adopted an explicit economic agenda of government subsidies, market access restrictions, and intellectual property theft intended to establish technological superiority and secure control of key supply chains. It complements this approach by suppressing worker power and consumer demand, generating an enormous trade surplus with the United States that has hollowed out American productive capacity and led to the transfer of trillions of dollars in assets. Basic trade in goods and services can still benefit both countries so long as it occurs in a balanced manner, the American market is insulated from PRC distortions, and resilient supply chains operate beyond PRC control.

The United States should:

1. Revoke China's Most-Favored-Nation status and impose tariffs to disfavor Chinese supply chains in the American market;

2. Develop the state capacity to monitor supply chain resilience and create industrial policies that rebuild American capabilities in critical sectors; and

3. Foster economic conditions that channel capital toward the major long-term investments necessary to support domestic industry.

III. Institutions

The CCP uses its economic leverage in financial markets and supply chains to corrupt American institutions and undermine democratic norms. Capitalism encourages whatever activities will produce the greatest profit and, in America's current relationship with China, the pursuit of profit often calls for kowtowing to the CCP. As a result, American movie studios and sports leagues self-censor in keeping with the CCP's preferences, American universities partner with affiliates of the Chinese military, and American business leaders fall over themselves apologizing for any possible slight. Preventing such subversion in a free society is not easy. Steps to limit economic interaction with China and thus the incentive for such behavior are most important. But policymakers can also act in some instances to interdict the influence directly.

The United States should:

1. Ensure research integrity and security by prohibiting flows of funds between American institutions and PRC-based ones;

2. Limit PRC-based tuition revenue to universities and access of Chinese nationals to American graduate programs in sensitive fields of study; and

3. Renormalize free speech through cultural export controls that eliminate incentives for placating the CCP and public forums that reward honest discussion of its true nature.

The Appendix provides a list of significant and thoughtful bills addressing the U.S.-China relationship from the 116th–118th Congresses. See page 22.

Introduction

If there ever was a consensus in Washington on confronting the People's Republic of China (PRC), it has already collapsed. President Joe Biden maintained the tariffs imposed by his predecessor, but in recent months his administration has sprinted back toward the naïve globalism that characterized American foreign policy at the start of this century. In April, Secretary of the Treasury Janet Yellen delivered a perplexingly anachronistic speech at Johns Hopkins University, in which she envisioned "a growing China that plays by the rules" and fosters "rising demand for U.S. products and services and more dynamic U.S. industries." One week later, National Security Advisor Jake Sullivan took the stage at the Brookings Institution to announce the administration's strategy of "de-risking and diversifying, not decoupling," in which a "small yard and high fence" would safeguard a narrow set of critical military technologies while otherwise permitting commerce to flourish. As the American Enterprise Institute's Danielle Pletka observed recently in *Foreign Policy*, the White House seems persuaded by dire warnings from spokesmen of the foreign policy establishment like Thomas Friedman, Fareed Zakaria, and Graham Allison that China must be accommodated.

Republicans seem generally to have coalesced behind support for "strategic decoupling." But what that means, or how to achieve it, is anyone's guess. Tariffs to disfavor Chinese imports remain controversial, as do Buy American provisions to favor domestic production, or industrial policies to boost domestic capacity. Opponents of the *CHIPS and Science Act* argued for stronger "guardrails" to prevent semiconductor companies from investing in China, but thus far the GOP majority in the House of Representatives has shown little interest in taking action that might obstruct the free flow of capital to America's economic adversary.

Meanwhile, trade with China continues to grow. "Made in China 2025" (*MIC2025*) the ambitious program of the Chinese Communist Party (CCP) to capture vital global markets, proceeds apace. Semiconductor companies continue lobbying for more flexibility to invest in China and license their technology there. In late May, the COMAC C919 completed the first commercial flight by a Chinese jetliner—thanks to more than a decade of joint ventures and technology transfer imposed upon western companies that wanted a piece of the action. The federal government itself still permits its employees to invest retirement funds in sanctioned Chinese military companies and federal funds have been flowing to a variety of Chinese research programs—for instance, gain-of-function research at the Wuhan Institute of Virology, to take a random example. Even banning TikTok, a PRC-based mobile application of virtually no economic importance but enormous data-gathering and propaganda potential, has proved too difficult.

To its credit, the Biden administration has taken some important steps—most notably, export controls imposed last year on chip-making equipment that significantly handicapped the Chinese industry. But officials also seem deeply uncomfortable with the implications of such policy. Jay Shambaugh, undersecretary for international affairs at the Treasury Department, emphasized that "it is important for the U.S. to be clear [that] we do not seek to decouple from China or seek to limit China's growth in any way" and that the actions are "not things we're doing to benefit the U.S. economically vis-a-vis China." When the PRC took its own action, banning Micron Technologies chips in some key sectors, Secretary of Commerce Gina Raimondo reacted with incongruous indignation that the United States "won't tolerate" such "economic coercion."

The PRC, by contrast, has made clear that it will use any tool at hand in its long-term struggle to displace the United States, from hacking federal personnel records to facilitating the flow of deadly fentanyl across our southern border. For the CCP, the conflict is a whole-of-society priority, demanding a level of state control and action that is barely conceivable to citizens of western democracies. As Robert O'Brien, National Security Advisor in the Trump administration, observed, the idea that "individuals are merely a means to be used toward the achievement of the ends of the collective nation state … remain[s] as fundamental to the Chinese Communist Party as the Constitution and the Bill of Rights do to us as Americans."

This paper argues that the posture of U.S. policymakers, and the current contours of the decoupling debate, is inadequate to the nature of the challenge posed by economic relations with China. The China challenge is not only, or even primarily, one of national security. It is that too, to be sure. But the fundamental problem is that America's free market economy is incompatible with China's state-controlled one, and American liberty and democracy are incompatible with the CCP's authoritarianism. Only a hard break from China will protect America's market from subversion by the CCP. Separating our economies will be costly, but the alternative of accepting foreign control of our assets and investments, dominance in our supply chains, and influence over our institutions will cost far more.

* * *

Never in human history have nations with such different economic and political systems attempted economic integration. Before the modern era, neither the markets nor the technology existed to facilitate it. In the twentieth century, efforts at American engagement with Nazi Germany neither lasted long nor ended well. During the Cold War, integration was never permitted, or even seriously considered, by either side—the suggestion would have been regarded as plainly insane. PepsiCo's opening of a Soviet bottling plant was front-page news in 1972 and represented, according to CEO Don Kendall, the "culmination of our work since that day 13 years ago" when Nikita Kruschev had been photographed at a trade fair sipping a Pepsi. Even then, rubles were not convertible to dollars, and so the Soviets paid for the bottling equipment with vodka. Not by coincidence did globalization gain steam only after the Berlin Wall fell.

Guiding the world's sole superpower at the outset of globalization, American theorists and policymakers never considered the implications of integration with an authoritarian peer. Globalization meant the economic liberalization, political democratization, and cultural Americanization of the world. The United States set the rules for international institutions and called the tune for multinational corporations, most of which were American or else relied heavily on access to American technology and the American market. Under these conditions, economic entanglements were largely beneficial: opportunities to exert American leverage and impose American norms. Incursions in, and distortions of, one market by another were always some other nation's concern.

From this lofty pedestal, the United States eagerly welcomed China into the international community in the late 1990s. At that time, China looked much like other developing nations. Its GDP was roughly one-tenth that of America's, closer in scale to Brazil or South Korea. Per capita, it was one of the world's poorest countries, ranked between Sri Lanka and Guyana. In a report titled "China's Hollow Military," scholars at the Brookings Institute concluded that "recent clamor over China's strategic ambitions is greatly overblown. Most of the Chinese aims that run counter to U.S. interests are in fact not global or ideological." American economists and policymakers from across the political spectrum, believing themselves to have arrived at "the end of history," were unified in their confidence that permitting China's ascension to the WTO and integrating it into the global economy would ensure its development as a constructive participant in an American-led world order.

China certainly developed—much faster than anyone had expected. But it did not liberalize. To the contrary, under the leadership of President Xi Jinping over the past decade, the CCP has become more authoritarian, and even genocidal; asserted greater control over the economy through state ownership, influence, and subsidy; and accelerated its aggressive industrial policy built on intellectual property theft and manipulation of foreign firms, with an explicit goal of weakening American industry and seizing global leadership. Through its "Military-Civil Fusion," a strategy overseen personally by Xi, "the CCP is acquiring the intellectual property, key research, and technological advancements of the world's citizens, researchers, scholars, and private industry in order to advance military aims," warned the State Department. "Joint research institutions, academia, and private firms are all being exploited to build the PLA's [People's Liberation Army] future military systems—often without their knowledge or consent."

As American defense officials and China experts observed last year in *Foreign Affairs*, the CCP produced "weeks of propaganda and publications" around the celebration of Karl Marx's 200th birthday to "establish Xi as the designated heir to Marx, Lenin, Stalin, and Mao." In a speech later that year, Xi "exhorted CCP cadres to remember their duty to 'liberate all of humanity' and serve as the 'gravediggers of capitalism.'" A textbook for the PLA explains, "Xi Jinping has emphasized that our state's ideology and social system are fundamentally incompatible with the West. Xi has said 'This determines that our struggle and contest with Western countries is irreconcilable, so it will inevitably be long, complicated, and sometimes even very sharp.'" The book also recommends gaining "a grip on foreign government leaders and their business elites by encouraging our companies to invest in their local economies."

The CCP's political and economic model poses a far greater threat to American democratic capitalism than does its two-million-man army. Whether Lenin ever said that "the capitalists will sell us the rope with which we hang them," he did write that they "will furnish credits which will serve us for the support of the Communist Party in their countries and, by supplying us materials and technical equipment which we lack, will restore our military industry necessary for our future attacks against our suppliers. To put it in other words, they will work on the preparation of their own suicide." The vision may be nefarious, but the observation itself is purely descriptive—and quite accurate.

Capitalism operates on the assumption that economic actors in a free market pursuing their self-interest—namely, profit—will advance the public interest as well. This holds true only under certain conditions, when socially valuable activities like investment in technology development, capacity expansion, job creation, and productivity enhancement are the best path to profit. On one hand, when everyone plays by the same rules, government constrains unproductive behavior, and a strong social fabric supports workers and their families, the assumption does hold and the market can generate unparalleled prosperity. On the other hand, bring the capitalist market into contact with a state-controlled one, allow foreign policymakers to create conditions in which the most profitable activity is serving the foreign state in word and deed, and too many capitalists will gladly do just that.

Even were China to disarm tomorrow, credibly foreswearing any aspirations beyond its borders, its influence as an economic actor would remain deeply corrosive to American liberty and prosperity. Asking American firms and workers to compete with their Chinese counterparts grants CCP policymakers the power to shape American capital allocations and labor-market conditions from the far side of the Pacific. Allowing Chinese firms to access American capital markets subjects the American people's savings to the whims of CCP regulators and leaves American financiers ham-handedly complicit in human rights abuses, while allowing Chinese capital access to American firms puts corporations under the control of a foreign government. And the more distortion China introduces on behalf of its producers, the greater the pressure on the U.S. government to respond in kind. *Free markets, free trade: pick one.*

Markets also transmit authoritarianism. If American firms are tasked with maximizing their profits, and the greatest profit can be had by kowtowing to the CCP, that is what American business leaders will do. "Most foreign business executives go to extreme lengths to avoid saying anything that could remotely antagonize the Chinese government," explained the Wall Street Journal. Michael Bloomberg will apologize for Boris Johnson's criticism of China at his conference (and ensure next year's conference is more CCP-friendly). If a substantial share of moviegoers is in China, Hollywood will gladly apply the standards of CCP censors before releasing films in America. If universities rely on students from China paying full price to fund operations, they will admit students whose speech is monitored and punished, allow the promotion of CCP propaganda, tolerate espionage, and even silence protest that might cause offense. *Free speech, free trade: pick one.*

* * *

America is struggling to grapple with the enormity of its wrong turn. Had we known in 2000 what we know now about China's future, we would not have conducted the reckless experiment of tightly coupling ourselves to a communist, authoritarian dictatorship that controls a market of 1.4 billion people. Our folly has produced an unprecedented situation that demands an unprecedented response—one that will take time and impose costs along the way.

Indeed, the goal of a hard break—protecting the American market from subversion by the CCP—requires greatest intervention precisely in those areas where it will be most expensive. Those supplies that are available *only* from China are the ones for which alternative sourcing must be found. Those investors *most* reliant on the Chinese market for their profits are the ones that must be forced to leave. Nearly every action that must be taken will fail the conventional cost-benefit analyses constructed by economists, which should not be surprising seeing as, under their definition and measurement of costs and benefits, America's economic relationship with China has been a great success. Policymakers often perform poorly in these circumstances.

What's required is a clear concept of and commitment to economic sovereignty, defined as

America's ability to decide for ourselves the parameters of economic activity in our domestic market. In a global economy, economic sovereignty is a crucial component of political and even territorial sovereignty and should take precedence over concerns of efficiency. Otherwise, we are susceptible to subversion by those who will sacrifice efficiency for control. In *On China*, Henry Kissinger relates how "a Han Dynasty minister described the 'five baits' with which he proposed to manage the mounted Xiongnu tribes to China's northwestern frontier." He quotes the minister's plan:

> To give them … elaborate clothes and carriages in order to corrupt their eyes, to give them fine food in order to corrupt their mouths, to give them music and women in order to corrupt their ears, to provide them with lofty buildings, granaries and slaves in order to corrupt their stomach… and, as for those who come to surrender, the emperor [should] show them favor by honoring them with an imperial reception party in which the emperor should personally serve them wine and food so as to corrupt their mind. These are what may be called the five baits.

In a capitalist economy, such bait is tempting, and each individual actor will usually be rational in taking it. Only a collective response, which requires public policy's coordination, provides a bulwark.

A hard break must occur across three related dimensions of economic interaction: investment, supply chains, and institutions. Policymakers have begun engaging in each case, but generally with a narrow emphasis on the politically salient issue *du jour*. Investment concerns have focused on holdings of China-based entities in America's public pension funds and China-based acquisition of American farmland. Supply chain concerns have focused on those products like semiconductors and personal protective equipment that experienced shortages during the COVID-19 pandemic. Institutional concerns have focused on revelations of CCP police stations operating in American cities and propaganda outlets on American campuses.

These issues are all concerning, and policymakers should address them. But they are best understood as illustrations of the broader incompatibility that makes a hard break necessary. Choosing high-salience issues and crafting specific bills in response will not work—at best it simply encourages both market actors and the CCP to find new paths to achieving the same ends. At worst it is directly counterproductive. A good example is the debate over "guardrails" to prevent investment in China by semiconductor manufacturers that accept federal subsidies through the *CHIPS and Science Act*. Congress wanted to prevent federal funds from reaching China, but the result is to make accepting those funds less attractive in the first place. If the goal is to prevent investment in China, the correct policy is a prohibition on investment in China, not a too-clever-by-half set of weakened constraints.

Conditioned to seek out "market failures" and craft tailored interventions that enhance economic efficiency, American policymakers must shift their mindset to one that prefers the blunt and the bold. The goal is not to make a "Chimerican" market work better; it is to obstruct and discourage operation of such a market altogether. Burdensome regulation that makes investment unattractive is a feature, not a bug, in that context.

In many cases, achieving the hard break will require entirely new policy frameworks and mechanisms, just as the international economy's development did after World War II and the control of illicit finance did after 9/11. For instance, this paper refers frequently to PRC-based and CCP-affiliated entities. U.S. law will need to improve its capacity to determine who and what counts. Likewise, the paper proposes scrutiny of the participants in various investment vehicles that likely requires greater disclosure from financial institutions, and export controls on products and services difficult to monitor in the traditional manner. Such tools would be important for preserving economic sovereignty in the twenty-first century's global market regardless; for executing a hard break from China, they will be indispensable.

The global market presents many other challenges, which this paper does not address. Globalization, with its unfettered flows of goods, capital, and people, would wreak havoc in the American market regardless of China. American Compass's *Regaining Our Balance* collection and *The Balancing Act* policy paper analyze those issues in depth and provide a range of proposals for ensuring that trade and immigration work for American workers. Here, the question is how to deal with China, a nation whose authoritarian government and anti-market policies make it unfit for participation in any global order.

I. Investment

The problem of capital flows between the United States and China has a telling asymmetry. PRC-based ownership of American assets—real estate and corporate equity, in particular—presents significant challenges. American ownership of assets in China does, too. Common sense would suggest that if Americans were concerned about the CCP exercising control in the United States, they should conversely be delighted by the prospect of the United States exercising control in China. But this common sense makes the common mistake of assuming that the American and Chinese economic and political systems are similar, so that the implications of foreign ownership would be similar as well. Instead, the interaction of China's state-controlled economy and the American free market makes capital flows and the entanglement of ownership undesirable for the United States in both directions.

Americans invest in China as private individuals and firms. They use any control that they can exercise, or data and technology that they can access, to advance their private interest—generally, without consideration of their nation's interests. They subject themselves, meanwhile, to the control of an authoritarian government that has shown no compunction manipulating foreign investors and leveraging market access to advance *its* national interest. Firms have typically been required to enter the country through joint ventures with PRC-based entities, and transfer technology to them. If an American investor or firm were somehow to establish sufficient control to act contrary to the CCP's interest in China, the CCP could simply expropriate the assets.

Consider the case of Apple, the world's most valuable corporation, which has made enormous investments in Chinese supply chains and selling to Chinese consumers. In 2016, the PRC shut down the iBooks Store and iTunes Movies just six months after their launch and issued a patent ruling that put iPhone sales in jeopardy. According to reporting by *The Information*, Apple faced "threats that would have hobbled the company's devices and services, including Apple Pay, iCloud and the App Store" and "executives were scrambling to salvage the company's relationship with Chinese officials." CEO Tim Cook visited the country and signed "a pledge to help Chinese manufacturers develop 'the most advanced manufacturing technologies'" and "promised to use more components from Chinese suppliers in its devices, sign deals with Chinese software firms, collaborate on technology with Chinese universities and directly invest in Chinese tech companies." The secret agreement committed Apple to $275 billion in investment over five years, an amount that would exceed Apple's total revenue in China over the period.

Americans investing in China met a worse fate with Didi, the ride-sharing service that raised $4.4 billion in a New York Stock Exchange IPO in 2021 valuing the company at more than $75 billion. Less than a week later, CCP regulators announced that the service posed a cybersecurity risk and banned it from app stores. Within a year, under a continuing regulatory assault, it had lost 90% of its value and was delisted from the NYSE.

China uses the leverage of market access to draw investment and technology out of the United States. For instance, the state-owned Commercial Aircraft Corporation of China (COMAC) required foreign firms supplying components for its first commercial airliner, the C919, to form joint ventures with PRC-based firms and transfer advanced technology to them. To gain access to the lucrative Chinese market, General Electric agreed to form a joint venture with the state-owned Aviation Industry Corporation of China (Avic) and share its "most sophisticated airplane electronics." Avic also produces the Chinese military's most advanced aircraft.

PRC-based investment and ownership in the United States poses its own problems. Avic is an active acquirer in the United States as well. "Chinese firms have acquired at least 11 U.S. aviation companies, established three joint ventures, and signed five cooperation agreements since 2005," according to a 2018 report from the U.S. Trade Representative, with Avic itself spending more than $3 billion on U.S. and European acquisitions since 2010. The state-owned Shanghai Pudong Science and Technology Investment Company (PDSTI), meanwhile, has found itself engaged in litigation over its gradual takeover of Icon Aircraft. PDSTI began amassing a stake in Icon in 2015, held a dominant share by 2017, and then began appointing executives and "laying plans to transfer Icon's technology to China," according to a group of American shareholders that filed suit. The U.S. government's Committee on Foreign Investment in the United States (CFIUS) determined that there were "no unresolved national security concerns" and permitted the takeover.

PRC-based investors are also active as limited partners in American private equity and venture capital funds, where they have deployed nearly $10 billion over the past decade. This allows them to influence fund allocations and the behavior of recipient firms, while making few public disclosures of their participation. In a less obscure instance, China's largest sovereign wealth fund, the China Investment Corporation (CIC), partnered with Goldman Sachs in 2017 to create a $5 billion "China-U.S. Industrial Cooperation Fund," though it struggled to complete deals as economic tensions between the nations rose.

A final category of PRC-based ownership in the United States is real estate. This category of investment is lower in absolute terms but has attracted significant political attention, particularly in the cases of farmland and residential purchases. While PRC-based entities increased their acquisition of foreign farmland ten-fold from 2009 to 2018, China ranks 18th among foreign holders of agricultural land in the United States and accounts for less than 1% of total foreign ownership here. The presence of PRC-based entities in residential real estate is larger—China ranks first in purchases by dollar amount—but the $6.1 billion spent in 2022 accounted for about 10% of the $59 billion in foreign residential purchases during the year, which in turn was less than 3% of the $2.3 trillion spent on existing-home sales. While small, individual purchases warrant less concern, large purchases or those in sensitive areas (for instance, near military installations) raise many of the same issues as other forms of asset ownership.

* * *

Several longstanding policies provide tools for sanctioning foreign adversaries and preventing acquisitions of American assets that threaten national security. These have been employed by the Trump and Biden administrations with increasing aggressiveness to curtail partnerships and investments that affect sensitive technologies or have the potential to buttress Chinese military development.

- **Committee on Foreign Investment in the United States (CFIUS).** The United States has an existing framework for restricting foreign purchases of American assets. CFIUS is an interagency committee authorized under the Defense Production Act to review "transactions" (broadly defined) that offer a foreign person substantial influence or control over an American business; non-controlling investments that nevertheless offer investors access to sensitive information in critical sectors; and real estate transactions in sensitive cases like ports of access or proximity to military facilities. Review "focuses solely on any genuine national security concerns raised by a covered transaction, not on other national interests." Passive investments that result in a stake below 10% and do not offer the investor nonpublic information are exempt.

- **Export Controls.** The Commerce Department's Bureau of Industry and Security (BIS) maintains an "Entity List" of foreign persons, organizations, and governments to which certain products cannot be exported without special licenses. The controls imposed on advanced semiconductor equipment by the Biden administration expanded the set of PRC-based companies on the Entity List and the set of products subject to license. Because entities and products are by default not listed, and licenses can be issued for listed entities, significant exports still occur—for instance, BIS released data in October 2021 indicating that, from November 2020 to April 2021, it had licensed more than $60 billion in exports to Huawei and $40 billion to China's Semiconductor Manufacturing International Corporation (SMIC) while denying less than 1% of applications for them.

- **Office of Foreign Asset Control.** The Treasury Department imposes a wide range of financial sanctions that prohibit American investment in various foreign entities, including those listed on the Non-SDN Chinese Military-Industrial Complex Companies List (NS-CMIC List). However, as the Coalition for a Prosperous America has shown, this list includes only a small subset of those companies on the Entity List (1,167 on the Entity List compared with 68 on the NS-CMIC List, and only 14 appearing on both). American holdings of Chinese securities exceed $1 trillion, and those securities are embedded within countless mutual funds and index funds, including many offered through the federal government's own Thrift Savings Plan (TSP).

- ***National Emergencies Act.*** In November 2020, President Donald Trump issued Executive Order 13959, declaring American financing of China's military development to constitute a national emergency and prohibiting transactions in securities of Chinese military companies. On June 3, 2021, President Joe Biden issued Executive Order 13974, expanding the Trump order to additional companies involved in research, development, and surveillance. The Biden administration has indicated that it is in the process of developing broader investment prohibitions.

- ***Holding Foreign Companies Accountable Act.*** Enacted in 2020, this legislation led by Senator John Kennedy (R-LA) delists PRC-based firms from U.S. securities exchanges that fail to comply with Public Company Accounting Oversight Board's audits for two (formerly three) consecutive years.

- ***CHIPS and Science Act*** "Guardrails." With the advent of an American industrial policy aimed at boosting the domestic semiconductor industry came a set of "guardrails" prohibiting companies that accepted federal funding from making certain investments in China. The stringency of these restrictions was debated in Congress and ultimately loosened prior to passage of the legislation.

While tools like these have had substantial effect where employed, they respond to a narrowly defined problem of national security and seek to obstruct as few transactions as possible. Thus, they take free commerce as the default and exclude only specified entities, technologies, and transactions. This leaves most investment unconstrained and, as in the case of the various overlapping sanctions lists, fails to disqualify consistently even those organizations identified as threats or to disqualify many transactions with those organizations. This model is consistent with the Biden administration's commitment to a "small yard" and "high fence," but facilitates further entanglement of financial flows and ownership and thus further subversion of the American market.

Preventing CCP Control

To protect America's economic sovereignty and counter CCP subversion, U.S. policymakers must prohibit capital flows, technologies transfers, and economic partnerships between the United States and China by default and permit them only in limited and clearly defined circumstances. Prohibiting American investment in China will protect American investors from the CCP's market manipulation, prevent inadvertent strengthening of an adversary's industrial base, and discourage technology transfer and offshoring. Prohibiting PRC-based investment in the United States will prevent CCP control of American assets and potential disruption in the American market.

1. Prevent PRC-Based Investment in America

The CFIUS framework, with its broad definitions of transaction and control, provides a useful starting point for broader investment restrictions. However, its model of scrutinizing only a limited set of transactions and then considering only their national security implications is inappropriate to the China context. U.S. law should define a class of "Disqualified Foreign Investors" (DFIs) that includes Chinese nationals who are not permanent U.S. residents, PRC-based entities, and any other entities that are affiliates of the CCP or subject to CCP control. It should then establish a presumptive prohibition on activities comparable to those that CFIUS might typically scrutinize.

POLICY **Prohibition on DFI Acquisitions.** Expanding on the CFIUS framework, legislation should adopt the CFIUS definition of a "transaction" and prohibit all such transactions involving a DFI.

POLICY **Prohibition on DFI-Controlled Corporations.** A DFI establishing new business operations in the American market poses all the same problems as one acquiring an existing business. Parallel to the expanded prohibition on transactions, U.S. law should prohibit DFIs from forming corporations or partnerships in the American market.

POLICY **Prohibition on DFI Participation in Limited Partnerships.** A substantial share of capital raised each year in American markets takes the form of "unregistered securities" and other private funds in which limited partners pool capital—for instance, through venture capital and private equity funds. U.S. law should prohibit DFIs from acquiring such securities or participating as limited partners in such funds.

POLICY **Prohibition on DFI Real Estate Purchases.** Recent disclosures of large-scale farmland purchases have prompted numerous proposals to restrict or ban foreign ownership of American farmland—or real estate generally. For instance, both Florida and Texas have recently pursued state laws that would ban any Chinese national from purchasing land in the state, which have proved overly broad in their effect even on legal, permanent U.S. residents. U.S. law should set a clear national standard, permitting legally present individuals of any nationality to purchase personal residences while prohibiting DFIs from acquiring properties with aggregate value above a reasonable threshold. CCP-connected billionaires purchasing hundreds of thousands of acres have the potential to subvert the American market and national security; individuals purchasing quarter-acre lots do not.

2. Prevent American Investment in China

U.S. law cannot exercise jurisdiction in China, which means that efforts to prevent American investments there must focus on constraining the investor's actions while in the United States. The American firm or investor will always have the option of leaving and then proceeding to invest. Thus, prohibiting investment in China is best understood as forcing a choice between continuing to operate in the United States and doing business in China instead. If Elon Musk would prefer to leave the United States for China, rely on PRC-based capital markets, and subject himself and his assets to CCP control, he should be welcome to do so. What he should not be able to do is reap all the benefits of American democratic capitalism while also serving predominantly PRC-based stakeholders.

POLICY **Prohibition on Outbound Investments and Joint Ventures.** American investors are already reconsidering their exposure to China given current geopolitical tensions and several proposals would create an outbound investment review mechanism, comparable to CFIUS, empowered to review and block transactions that present risk to American national security or economic resilience. But as noted above, case-by-case review subject to national security criteria are poorly tailored to the challenge. Legislation should prohibit Americans and U.S.-based entities from pursuing "transactions" as defined by CFIUS that entail the acquisition of equity, debt, or real estate in China. The prohibition should extend to joint ventures formed between American and PRC-based entities for conducting business in any jurisdiction.

POLICY **Entity List Harmonization.** The federal government already maintains multiple lists denoting foreign entities to which goods, services, or capital cannot be provided. However, they are dispersed across different agencies, use different criteria, and overlap only partially. At least with respect to China, legislation should consolidate these lists to a single one managed jointly by the Defense, Treasury, and Commerce Departments that imposes the restrictions on exports and investment contemplated by each.

POLICY **Intellectual Property Sanctions.** The United States and its allies already operate a sanctions regime for prohibiting the transfer of military technology to certain nations, called the Wassenaar Arrangement. U.S. law should apply this same framework to all technology transfer into China. The United States should pursue comparable commitments from allies but proceed regardless of their participation.

POLICY **Exclusion of PRC-Based Entities from American Listings.** U.S. law should prohibit American stock exchanges from listing PRC-based entities and prohibit index funds and mutual funds listed on American exchanges or offered via tax-exempt retirement plans or public pension plans from including the foreign listings of such entities. The *American Financial Markets Integrity and Security Act of 2021*, introduced by Senator Marco Rubio and five cosponsors, would have applied such exclusions to PRC-based companies on some of the entity lists mentioned above. This framework helpfully identifies the types of capital market access that should be denied, but the law should apply to all PRC-based companies rather than relying on national security-focused criteria.

3. Withdraw Investment Protections

The United States has Bilateral Investment Treaties (BITs) in force with more than 40 countries, helping to protect private American investments abroad. The Obama administration pursued a U.S.-China BIT with enthusiastic support from the *Wall Street Journal* editorial board, which saw CCP engagement in the project as evidence that "China's new leader Xi Jinping will follow through on promises to restart economic reforms." Early in the Trump administration, Secretary of the Treasury Steven Mnuchin said completing such a deal was still on the agenda.

POLICY **Withdrawal of Investment Protections.** American diplomats often work to protect and advance the interests of American businesses operating in foreign countries. This should not be the case with China. To the contrary, American investors should understand that national policy discourages investment in China and no help will come if their interests there are threatened by the CCP. The United States should abandon pursuit of any BIT with China.

> "Societies that open to commerce will one day open to liberty."
>
> PRESIDENT GEORGE W. BUSH, 2001

II. Supply Chains

In principle, traditional trade in manufactured goods could be the least concerning element of the U.S.-China economic relationship: America puts things on boats, China puts things on boats, the boats pass each other somewhere in the Pacific and get unloaded on the far side. But that form of trade, described by classical economists like Adam Smith and David Ricardo, bears little relationship to the imbalanced and distorted exchanges occurring between the two nations today. In 2022, the United States imported $537 billion in goods from China while exporting only $154 billion in return. For the most part, the PRC refuses to open the Chinese market to American exports and instead trades its own exports for American assets. This not only compounds the problems of investment and control, described above, but also hollows out American industry, as production for the American market moves offshore but no commensurate foreign demand emerges for what America might produce.

Nor is this hollowing out merely random, or concentrated in areas where China has a genuine "comparative advantage." The CCP has pursued an explicit industrial strategy to capture critical supply chains and leadership in the most promising industries. As Ambassador Robert Lighthizer noted in his recent testimony before the House Select Committee on the Chinese Communist Party, "The Chinese economic system is designed to exploit foreign commerce to advance China's geopolitical power." The CCP has used subsidies, market-access barriers, and outright intellectual property theft and espionage to manipulate American firms, talent, and funding into developing China's industrial capacity while undermining America's own.

The CCP does not even bother to disguise the strategy. Its *MIC2025* plan, launched in 2015, describes the goal of becoming the global leader in innovation and manufacturing by 2049, the CCP's centennial. As the *New York Times* reported, the plan "would provide large, low-interest loans from state-owned investment funds and development banks; assistance in buying foreign competitors; and extensive research subsidies." Germany's Mercator Institute warned that "Chinese high-tech investments need to be interpreted as building blocks of an overarching political program. ... In the long run, China wants to obtain control over the most profitable segments of the global supply chains and production networks." According to a report issued by Senator Marco Rubio, "The Chinese government is doing more than breaking the formal rules of trade: it is seeking, through state policy and the power of its domestic market, to dictate the real terms for how global trade will proceed, and to whose benefit."

MIC2025 focuses on ten advanced industries, most of which the United States pioneered and historically dominated, including aerospace, robotics, energy and power generation, and agricultural machinery. China now controls approximately 90% of the global supply of inputs required to make generic antibiotics. Its subsidies for solar panels caused prices to plummet by 80% as it flooded global markets with below-cost products that allowed it to build domestic scale while suppressing investment elsewhere. China's share of all solar panel manufacturing stages exceeds 80% and may reach 95%; the top ten solar panel suppliers are based there. This is one of many industries that the PRC supports through the dominant position that it has cultivated in rare earth elements, where China accounted for approximately 70% of global mine production in 2022. That same year, the United States accounted for 14%. These elements are used in advanced technologies like batteries, avionics, and energy machinery, often with defense applications. The PRC maintains export quotas and levies export taxes, advantaging domestic industry and incentivizing foreign entities to produce in China where inputs are cheaper.

Thus, trade with China presents a three-fold problem:

1. **Imbalanced Trade That Mortgages the Future.** The PRC suppresses household consumption to increase investment, allowing it to trade cheap goods in exchange for assets. This builds China's manufacturing capacity and expertise, while reducing American capacity and committing the American economy's future produce to China.

2. **Loss of Strategic Leadership in Critical Industries.** The PRC deploys industrial policy and mercantilism to warp market incentives, drawing American capacity to China in the most critical sectors like aerospace, energy, and health care. To participate there, American firms are forced to transfer technology to local entities through joint ventures.

3. **Dependence on an Adversary.** Once dominance is established, the PRC uses its position to leverage further market distortions. As more components of supply chains become entrenched in China, moving related production becomes more attractive as well. The COVID-19 pandemic illustrated how supply chain shortages could cripple American industry and endanger American citizens. From washing machines, to clothing, to F-35 fighter jets, American supply chains are disturbingly reliant on China.

* * *

Under President Donald Trump, the United States initiated efforts to move production out of China, insulating American producers from PRC distortions, and rebuilding domestic capacity. Where the United States imposed tariffs, for instance, imports fell dramatically.

- **Section 301 Tariffs.** Section 301 of the *Trade Act of 1974* empowers the president to respond to unfair trade practices with tariffs. The Trump administration conducted a Section 301 assessment, revealing PRC abuses like forced technology transfer, licensing restrictions, and cyberattacks. Tariffs were imposed, primarily targeting products in strategic sectors, like cars, machinery, and chemicals. The tariffs remain largely in effect and have substantially suppressed imports from China of affected products. Trade with China has also been affected by global tariffs imposed by the Trump administration under Sections 201 (safeguards) and 232 (national security).

- *Note: this report initially described the Section 201 and Section 232 tariffs mentioned above as anti-dumping and countervailing duties.*

Under the Biden administration, the *CHIPS and Science Act* has demonstrated not only the potential for private industry to invest domestically when given the incentive, but also the high level of coordination required among federal, state, local, and private actors. Unfortunately, in other sectors like solar panels, the administration has doubled down on dependence.

- ***CHIPS and Science Act.*** Federal investment in the semiconductor industry has successfully attracted private investment throughout the technology ecosystem. Congress provided $54 billion in federal incentives for semiconductor manufacturing and R&D. As of January 2023, the value of U.S.-based, private-sector semiconductor projects underway, announced, or under consideration totaled over $260 billion through 2030. Investments range from fabrication plants (fabs) to semiconductor tool R&D facilities.

- **Moratorium on Solar Panel Tariffs.** In 2022, the Commerce Department found that the PRC was circumventing countervailing duties on solar products by shipping them to the United States via Cambodia, Malaysia, Thailand, and Vietnam (CMTV). This should have prompted imposition of tariffs on solar imports from those countries, however President Biden issued a two-year moratorium to ensure continued American access to cheap panels. Congress passed a bipartisan *Congressional Review Act* (CRA) resolution overturning the moratorium but this was vetoed by the president, allowing the illegal CMTV panels to continue entering the country unimpeded.

Attempts to excise CCP-controlled supply chains from the American market have been sporadic and inadequate. The *CHIPS and Science Act* encapsulates the challenge: Legislation took years to complete and the ambitious *Endless Frontiers Act* and *United States Innovation and Competition Act* (USICA) were eventually scaled down to investment in a single industry. Prior to passage, Congress then weakened restrictions on investment in China to accommodate industry demands for continued access.

Preventing CCP Dominance

To protect America's economic sovereignty and counter CCP subversion, U.S. policymakers must rebalance trade flows, prevent CCP dominance in critical industries, and reinvigorate domestic production. Policy should rely upon the private sector to drive this effort by fostering the conditions for American enterprise to invest and innovate. American firms must develop talent, conduct research, and expand capacity. Federal, state, and local governments must channel private capital toward productive uses.

1. Disfavor Chinese Supply Chains

The PRC uses a range of trade abuses to distort global markets and establish a dominant position in strategic supply chains, strengthening the Chinese economy while weakening the American one and giving the CCP economic leverage. Trade that occurs under these conditions is neither efficient nor based in comparative advantage—to the contrary, it reflects decisions by the CCP to build advantages in strategic sectors. Such a trading relationship is not in America's interest and should be disrupted by any means necessary. Trade with China can still be constructive, but only if distortions are countered and dominance prevented.

POLICY **Revocation of MFN Status.** A World Trade Organization (WTO) member like the United States is expected to grant all other WTO members "Most-Favored-Nation" (MFN) status, meaning the most favorable trade terms that it offers to any country. As part of China's ascension to the WTO, the U.S. Congress granted it this status, trusting that the WTO would hold the PRC accountable for adhering to its own commitments. This has not happened. The United States should reclaim its authority to dictate the terms of its trade with China by revoking its MFN status. The *Ending Normal Trade Relations with China Act* introduced by Senator Josh Hawley (R-MO) would do just that. Another approach, proposed by Senator Tom Cotton (R-AR) in the *China Trade Relations Act*, would force annual review of MFN status. The immediate effect of revoking MFN status would be to replace the near-zero tariffs for MFN trading partners in "column one" of the Harmonized Tariff Schedule (HTS) with the high tariffs of HTS "column two" that the United States charges to the few nations not granted MFN status.

POLICY **Additional Tariffs.** The tariffs in HTS column two are not necessarily well tailored to the challenges posed by China. Ideally, Congress would update the column or create a new one specific to China. But if it does not, the president should also retain the Section 301 tariffs and countervailing duties first imposed during the Trump administration and consider continued use of those authorities to address further PRC distortions. The United States should also expand its use of Section 337 of the *Trade Act of 1974*, which provides additional authority to exclude altogether imports that benefit from stolen intellectual property and other forms of unfair competition.

POLICY **Anti-Monopoly Tariff.** Existing antidumping tariffs and countervailing duties are designed to counter specific distortions in foreign markets. But for China in particular, policymakers should be concerned more generally with the CCP's holistic strategy to achieve dominance in vital supply chains. A market power analysis comparable to that used for antitrust in the domestic context would be most appropriate, identifying situations where Chinese imports dominate a market. U.S. law should authorize the Commerce Department, in conjunction with the U.S. Trade Representative, to conduct such analyses itself or when prompted by complaints from domestic industry and to impose tariffs targeting those products until market share of Chinese imports falls to an acceptable level.

POLICY **Lower De Minimis Threshold.** Current U.S. law allows shipments of "de minimis" value to enter the American market free from tariffs that might otherwise apply. The *Trade Facilitation and Trade Enforcement Act of 2015* raised this de minimis threshold from $200 to $800, allowing enormous e-commerce retailers in China to ship nearly any consumer product duty-free into the American market—in 2022, nearly 500 million packages entered the United States from China under the exemption. The U.S. threshold is the world's highest—the European Union maintains a de minimis threshold below $200; in China, the threshold is $8. U.S. law should apply a reduced threshold for imports from China—at least returning to the $200 threshold and perhaps reducing it to a genuinely *de minimis* amount or eliminating it entirely.

2. Structure Institutions for Industrial Policy

Preventing dependence on China also requires developing the capacity for domestic supply. The federal government has long eschewed this responsibility, which has left existing programs scattered across agencies, with uncoordinated funding and little competency in strategy or execution. The Biden administration's recent attempt at studying supply chains and developing strategies yielded disparate reports from agencies with widely varying understandings of their roles and objectives.

POLICY **Consolidation of Functions and Strategies.** Rebuilding domestic industrial capacity will require new institutional capacity within the federal government and a clear mandate for action. Legislation should establish a cabinet-level National Development Council (NDC) tasked with identifying and prioritizing challenges, setting clear goals, delivering practical and industry-specific roadmaps, and coordinating execution across agencies. The *National Development Strategy and Coordination Act* introduced by Senator Marco Rubio (R-FL) and Congressman Ro Khanna (D-CA) provides a useful model for establishing an interagency body tasked with creating a national development strategy.

POLICY **Industry-Specific Strategies.** The years-long legislative process leading to passage of the *CHIPS and Science Act* and its semiconductor-focused industrial policy, followed immediately by challenges at every level of government and among industry participants, none of whom knew how to proceed with implementation, underscored the importance of a holistic and repeatable process for spurring private investment with public support. Legislation targeting vital sectors should adopt a replicable baseline model provided by the NDC that addresses workforce, regulatory, and supply-chain issues in a predictable manner from the start. For instance, in an initial stage for a given industry, the NDC should lead a supply-chain assessment that highlights existing gaps in development and provides a clear picture of existing private initiatives and federal, state, and local involvement.

POLICY **Development Bank.** Private firms and investors in financial markets hesitate to take on ambitious industrial projects, citing high upfront costs, long time horizons, and uncertainty of returns.Even when firms are willing to engage in public-private partnerships, unnecessary bureaucratic barriers and naked politicization can make the public side an ineffective partner. U.S. law should establish a national development bank to finance long-term, capital-intensive projects vital to national economic and security priorities. The bank would attract private capital by using a federal equity commitment to reduce risk and increase returns for investors. Its capabilities should include direct debt issuance, credit and completion guarantees, equity lending, syndication authority, and technical assistance. Its policy mandate should focus on reshoring domestic manufacturing, strengthening the defense industrial base, modernizing the commercial maritime industry, expanding and securing critical infrastructure, and supporting strategies developed by the NDC. The *Industrial Finance Corporation Act* proposed by Senator Chris Coons (D-DE) provides an example of this kind of financing mechanism.

3. Accelerate Productive Investment

U.S. domestic business investment is in long-term decline, industrial output has stagnated, and productivity growth has turned negative. Public policy must play a vital role in reversing these trends by creating new demand for domestic production, supporting investment in innovation, and removing barriers to building.

POLICY **Local Content Requirements.** U.S. law should stimulate demand for domestic production through imposition of local content requirements (LCRs), leaving the market to determine how best to fulfill that demand through investment and innovation. LCRs specify a percentage of domestic labor and components that a good must contain to be sold in the American market. The *Make in America to Sell in America Act* introduced by Senator Josh Hawley (R-MO) and Representative Claudia Tenney (R-NY) provides a useful model, establishing a 50% LCR for manufactured goods critical to national security or the protection of the domestic industrial base.

POLICY **Precompetitive Consortia.** In precompetitive R&D consortia, firms in a given industry collaborate on development of a common technology platform, sharing the resulting intellectual property from which they can develop differentiated downstream products to compete against each other. The collaboration pools resources and expertise and provides a site at which public policy can constructively subsidize investment without "picking winners and losers." U.S. law should clearly define the parameters of a Pre-Competitive R&D Consortium (PCC), provide matching public funds to any industry whose members establish a consortium within those parameters and commit their own capital, and exempt the consortium from antitrust prohibitions.

POLICY **NEPA Repeal.** Current U.S. law discourages industrial development with lengthy environmental reviews and litigation that stall projects regardless of their economic importance and even when they pose no substantive threat to the environment. The main culprit is the *National Environmental Policy Act* (NEPA), which mandates years and thousands of pages of review for any project that involves the federal government and invites legal challenge of the review process. Various proposals, including some in the 118th Congress's H.R. 1, the *Lower Energy Costs Act*, attempt to streamline NEPA processes or exempt certain types of projects. But the fundamental problem is the law itself, which offers no substantive environmental protection and simply adds procedural complexity—slowing development and creating opportunity for obstruction is its premise. Congress should repeal NEPA, encouraging America to build again.

> "I believe that having [China] in the WTO will not only have economic benefits for the United States and other countries [...] but will increase the likelihood of positive change in China and therefore stability throughout Asia."
>
> PRESIDENT BILL CLINTON, 2000

III. Institutions

The most overt instances of CCP influence-peddling and outright repression on American soil have begun to attract widespread attention. For instance, the PRC opened more than 100 "Confucius Institutes" on American college campuses beginning in 2004, offering credit-bearing coursework to American students under the tutelage of PRC officials subject to their country's speech restrictions. These have been mostly shut down, though in many cases they appear to have undergone a rebranding and resurrection with the encouragement of university administrators eager for funding. The Justice Department recently filed charges against agents of the PRC for "establishing a secret police station in the middle of New York City." At the same time, it charged 40 officers of China's National Police with perpetrating "transnational repression schemes targeting U.S. residents whose political views and actions are disfavored by the PRC government."

Such programs represent a fraction of the influence that the CCP exerts over American institutions, and in some respects the least troubling form, insofar as they can be identified and excised. More influential to American universities than funding for Confucius Institutes is the $1 billion in gifts and contracts received from PRC-based entities over the past decade, research partnerships with Chinese military institutions, and the tuition from more than 300,000 Chinese nationals attending American universities and often paying full price. One university found itself so dependent on this revenue that it took out an insurance policy against any drop in enrollment of Chinese nationals. In another instance, a university president was goaded by an organization representing students from China into rebuking an effort to protest China's human rights abuses. Students with family in China, and academics who need access there, increasingly self-censor.

Self-censorship has become pervasive in other institutions as well, yet it is almost impossible to either prove or prevent. Hollywood studios, for instance, adopt wholesale the standards of CCP censors in their own moviemaking, lest they lose access to the lucrative Chinese market. Americans are mostly oblivious to the reality that they are seeing only what the CCP will allow, except when the occasional misstep by a star or executive leads to groveling. Celebrity tough-guy John Cena posted an apology in Mandarin on Chinese social media after referring to Taiwan as a country while promoting a movie from "The Fast and the Furious" franchise. No harm done—the film went on to gross more than $100 million on its opening weekend in China.

The National Basketball Association's (NBA) posture is especially contorted, as it attempts to pair a courageous and outspoken stance on social issues in America with absolute silence on abuses in China. When Houston Rockets general manager Daryl Morey tweeted support for Hong Kong protestors in 2019, the PRC responded by cancelling sponsorships and broadcasts of the NBA's exhibition games in the country. The NBA then cancelled the players' media availabilities, lest they have to answer any questions. LeBron James later criticized Morey, saying he "either was misinformed or not really educated on the situation" and that "many people could have been harmed, not only financially, but physically. Emotionally. Spiritually." James also warned, "Yes, we do have freedom of speech, but there can be a lot of negative that comes with that, too."

NBA Commissioner Adam Silver has been admirably frank about how these calculations work. "There are not a lot of fundamental protections afforded Chinese citizens that are afforded to American citizens," he acknowledged. "And I … I don't have a cut-and-dried response to that. … The fact is, we think by bringing the NBA to China and exposing the Chinese people to the NBA … it's net incredibly positive for us to be engaged in that activity."

Intel apologized for its efforts to comply with U.S. law and exclude slave labor from Xinjiang from its supply chains, emphasizing its commitment to "accelerating joint development with China." Jamie Dimon, CEO of the world's largest bank, apologized for making a joke that JPMorgan would outlast the CCP and then issued a second apology when the first was apparently deemed insufficient. Months earlier, JPMorgan had received the PRC's approval to open the first fully foreign-owned brokerage in China. Michael Bloomberg, among the ten richest people in the world and owner of an immensely influential financial news network, apologized at his Bloomberg New Economy Forum in Singapore after former UK Prime Minister Boris Johnson delivered a speech critical of the Russian and Chinese regimes.

The presence of Bloomberg's conference in Singapore was notable because it marked a shift in venue from his intended location—Beijing—where he had partnered with a Chinese think tank controlled by CCP leaders to create a rival to the World Economic Forum's Davos conference. He is not the only billionaire hoping to leverage China's ascendance for his personal brand. Stephen Schwarzman, CEO of the Blackstone Group, partnered with Tsinghua University to create the "Schwarzman Scholars" program, intended to rival the Rhodes Scholarship. CCP officials help select the Chinese participants. Daniel A. Bell, founding chair professor of the program, took to the New York Times opinion page to describe China's political system as "Chinese-style democratic meritocracy." One gets the idea, and cannot help recalling the fifth bait. *For those who come to surrender, the emperor should show them favor by honoring them with an imperial reception party in which the emperor should personally serve them wine and food so as to corrupt their mind.*

Perhaps Schwarzman will succeed in establishing Beijing as the most prestigious place for top American students to study, perhaps he will fail. Rooting for his success is fellow finance billionaire Ray Dalio, whose name adorns the program's auditorium. In late 2021, following reports that Dalio's Bridgewater Associates had raised more than $1 billion for new investments in China, he defended his work there by dismissing China's human rights issues as "behav[ing] like a strict parent" and pleading that he "can't be an expert in those types of things."

The *New York Times* summarizes the situation well: "American institutions may have to make their own choice: Reject censorship or maintain access to China. Right now, desire for access is winning."

* * *

The threat posed by CCP entanglement with American institutions extends far beyond particular examples of groveling apologies issued or compromised programs established. Each apology should serve primarily as a reminder that for every honest but errant comment uttered, hundreds more truths presumably go unspoken. Any aspiring academic, investor, or public figure must ask himself from the start what he stands to gain or lose by acting in ways contrary to the CCP's interests.

The American culture of free speech and inquiry is built upon an assumption that no actor in the system will possess the power to coerce or manipulate individual citizens—and the one that does, the government, will be constrained by law and custom from doing so. China alters that calculus. An open society cannot tolerate the imposition of authoritarian incentives and penalties from afar, and must be insulated from them. As China becomes richer, the draw of access to its market will only become stronger. As it becomes more technologically advanced, the ability of PRC-based entities to engage directly with Americans will only increase.

To date, policymakers have done little to address this challenge. A range of bills aim to curb PRC access to the American higher education system, mostly for purposes of protecting sensitive American intellectual property. Others require disclosure of PRC funding. The *Safeguarding American Innovation Act*, introduced by Senator Rob Portman (R-OH) in 2021 with a large and bipartisan group of cosponsors, would have substantially increased oversight and control of federally funded research projects and disclosure of foreign funding. The legislation was initially included in the *CHIPS and Science Act* but was stripped at the last minute under heavy pressure from universities, which had long opposed such safeguards.

One notable policy that has taken effect is Proclamation 10043, issued by President Trump in 2020, which prevents Chinese nationals with a connection to the CCP's "Military-Civil Fusion" (MCF) strategy from receiving F or J visas for graduate study or research in the United States. The pervasive nature of MCF, overseen personally by President Xi, leaves the proclamation covering many of the most prominent PRC-based universities and companies and most STEM-related fields of study, potentially excluding a substantial share of visa candidates. The Biden administration has retained the policy, leading to the refusal of nearly 2,000 visas in 2021 and frustration from American universities with its breadth and ambiguity.

Preventing CCP Influence

In many respects, the most important steps for preventing excessive CCP influence in American institutions are those described above, for protecting America's economic sovereignty and preventing CCP subversion of the American market. If American firms are not dependent on PRC-based supply chains, not raising money from the PRC, and not subjecting themselves to its jurisdiction, American business leaders and investors will have far less reason to care what the CCP wants them to think, say, or do. But this still leaves special cases where further intervention is both possible and necessary.

1. Ensure Research Integrity and Security

American research institutions, whether operated by government, within academic institutions, or as tax-exempt nonprofits, are less susceptible to market logic and more properly targeted by public policy. They rely on public funding or subsidy and are expected to operate in the public interest. These institutions should not partner with the CCP and must accept processes and controls designed to ensure the integrity and security of their work.

> "No nation on Earth has discovered a way to import the world's goods and services while stopping foreign ideas at the border. Just as the democratic idea has transformed nations on every continent, so, too, change will inevitably come to China."
>
> PRESIDENT GEORGE H.W. BUSH, 1991

POLICY Prohibition on PRC Funding of American Research. U.S. law should prohibit American universities, research institutions, and nonprofit organizations from accepting funding from PRC agencies or PRC-based entities. Any university or institution found to accept such funding should lose its federal funding and any tax-exempt status. Employees of such institutions should not be permitted to accept gifts, honoraria, or reimbursement from PRC-based entities in conjunction with travel to China.

POLICY Prohibition on American Funding of PRC Research. The question of whether the National Institutes of Health funded gain-of-function research at the Wuhan Institute of Virology that led to the COVID-19 pandemic obscures the more basic question of why the federal government would fund the Wuhan Institute of Virology at all. U.S. law should prohibit federal and state agencies, universities and research institutions receiving federal funding, and nonprofit organizations from entering partnerships with or providing funding to PRC-based entities.

POLICY Safeguarding American Innovation. The *Safeguarding American Innovation Act* would have taken important steps toward monitoring and controlling the access of foreign students and researchers to American technology and data and should become law.

2. Protect the Academy

America can benefit when students from China attend American universities. But the control that the CCP exercises over those students, and the revenue they bring, also poses a unique threat of subverting the schools they attend. In sensitive fields where the PRC has made industrial espionage and intellectual property theft a priority, participation by students and researchers from China will often have costs that outweigh benefits and should by default be prohibited.

POLICY Tuition Cap. In keeping with the prohibition on acceptance of PRC funds at research universities, described above, U.S. law should prohibit colleges and universities that receive federal funding from collecting more in tuition and fees from any Chinese national holding an F-1 student visa than the average amount collected from American citizens and permanent residents enrolled in the same program of study. Universities should not gain a financial advantage from admitting Chinese nationals instead of other candidates.

POLICY Study in Sensitive Fields. Proclamation 10043, supported by both the Trump and Biden administrations, provides an effective framework for disconnecting the CCP from programs in American academic institutions that could advance its agenda. That policy should be codified in legislation and its scope clarified through listing of the institutions that "implement or support MCF" and the relevant fields of study. Relevant fields should include not only those in STEM with the potential to advance CCP military strength, but also ones in business, law, economics, and public policy where subversion of American values is central to the CCP's ideological program. In parallel, U.S. law should expand eligibility for the permanent EB-2 visa ("an employment-based, second preference visa if you are a member of the professions holding an advanced degree or its equivalent, or a person who has exceptional ability") to graduate students and researchers affected by 10043 or subsequent law who can demonstrate independence from the CCP and an intention to move permanently to the United States.

3. Re-Normalize Free Speech

The PRC has created strong financial incentives for influential Americans to promote CCP propaganda, or at least remain silent about the truth. The United States cannot outbid the PRC in the matter or prohibit certain viewpoints and compel others, nor should it want to. What policymakers can do is lower the economic stakes by foreclosing profits in China regardless of what one says and raise the reputational stakes by creating a high-profile forum that embarrasses people who toe the CCP line.

POLICY Cultural Export Controls. For a unique set of cultural exports, "the people are the product." U.S. law should designate a class of products and services where the creation of intellectual property, performances, or products is connected to the participation of specific individuals such as actors, singers, athletes, or other entertainers. U.S. law should prohibit revenue-generating exports of such products and services and licensing of associated brands and content to China—including films, musical recordings, broadcasts of sporting events, personalized footwear and apparel lines, and live performances. In many cases, free, unauthorized, or pirated versions of these products will still circulate in China, but this is a feature of the law. While American producers will lose the incentive to kowtow to CCP censors, some American cultural influence and soft power will still reach the Chinese market and create demand within China for greater openness to the free world.

POLICY **Select Committee on the Chinese Communist Party.** The select committee convened by the House of Representatives is already playing a valuable role in highlighting the challenge posed by the CCP. While the committee has thus far declined to seek public testimony from prominent business and cultural leaders, a high-profile congressional committee is an ideal forum in which to place America's public figures on the record about their own experiences with the CCP and their perspectives on its policies. The CEO of the Walt Disney Company and the commissioner of the NBA, for instance, would both make excellent witnesses, as would Stephen Schwarzman and Michael Bloomberg. The American public deserves to hear their testimony under oath. The Committee should hold regular hearings for this purpose, placing all public figures on notice that they are accountable for their views and values. These would not be "gotcha" hearings or "witch hunts"; to the contrary, witnesses could expect to earn widespread praise simply for describing what they have actually experienced and what they actually believe. Those who chose to speak honestly would fatally undermine the CCP's efforts to cow Americans into silence. Those who might choose to remain silent, or simply lie, would at least face much higher reputational costs for doing so.

IV. The Rest of the World

U.S.-China relations do not operate in a vacuum. U.S. allies are themselves entangled with China economically and have thus far shown less interest than the United States in doing anything about it. The PRC is also making a full-court press to establish strong and often coercive economic relationships with developing nations. U.S. diplomats fear that if forced to choose a side, many countries will choose China's. American business leaders fear that if they are isolated from the Chinese market while European and Asian competitors are not, they will lose a source of both cheap inputs and profitable sales that is vital to remaining globally competitive.

One implication of these challenges is that the United States must decide the extent to which it will tolerate third parties acting as intermediaries that leave it exposed to China. Here, the three dimensions of economic sovereignty provide a useful guide. For institutions, where people themselves are at issue, intermediaries are of least concern. If Chinese nationals and American nationals are both conducting research at a German university, for instance, American interests are barely implicated.

Supply chains raise a greater concern, as goods are more fungible than people. If America imports a product from several foreign countries, all of which themselves are dependent on China for a critical input, America would in a sense remain dependent itself. But China's dominance would be mitigated because it would be difficult to exercise; rather than simply manipulate or cut off the American market, the PRC would have to apply its action across all its exports—a more difficult and costly move. Still, in crafting its own strategy, the United States should scrutinize where the PRC might have underlying dominance in a global market and use both tariffs and domestic development to prompt the creation of alternative sources.

The United States should also seek to build a broader partnership of allied countries willing to make similar commitments in their own supply chains and on issues like technology transfer and research funding. Participants in such a trading bloc should have preferential access to the American market—or, more precisely, they should retain the preferential access that the Untied States currently grants almost universally. Nations declining to join should face worse terms of trade, and nations committing fully to the Chinese sphere should face the same treatment as China. Developing countries in Latin America represent a notable case where China has made an especially aggressive push that the United States has an especially strong geopolitical interest in countering. A new strategy for engaging the region, focused on providing investment and trade preferences to support the massive near-shoring that a hard break with China would trigger, could succeed where other recent American efforts have failed.

Investment poses the greatest challenge, because financial flows most easily reshape themselves around any obstacles they encounter. A "Disqualified Foreign Investor" from China may not be able to invest in America, but what about a London-based fund whose partners happen to be CCP members? U.S. law will have to be strictest on this question, continually refining the DFI definition as necessary to prohibit inbound investment from any entity whose controlling owners are PRC-based. Fortunately, these "edge cases" will represent only a sliver of the economic interactions addressed by a hard break and cannot themselves threaten America's economic sovereignty. These cases are also among the easiest to deter: U.S. law should force divestment and impose penalties retroactively where PRC-based involvement comes to light, making subterfuge an unattractive risk. One might construct an opaque holding structure to execute a transaction unnoticed, but if and when it did become noticed (as it likely would, if the CCP attempted to leverage it) the control and any benefit would quickly be lost.

Investment flows from other nations into China are of much less concern. All things equal, as a matter of superpower competition, the United States would prefer that less capital flow to China. Agreements among nations prohibiting it should be a key element of the potential trading bloc described above. But investment by other nations in China would not interfere with America's goals in pursuing a hard break; rather, it would be their own loss.

The business community should receive a similar answer regarding its own fears. Firms that currently rely on the Chinese market will have to look elsewhere, but policymakers should not accept their complaints that this will put them at a disadvantage. Betting on China is a losing bet, as many firms are already discovering. While profits from that market could hypothetically fund investment and innovation elsewhere, there's little evidence that this happens in practice. To the contrary, America's industrial crown jewels—companies like Intel, Boeing, and General Electric—all delivered far better performance before they abandoned their American-engineering-led models for offshoring, financialization, and high shareholders returns coupled with declining technological prowess. Being forced out of China is the best thing that can happen to American business; staying in may well lead to catastrophe for the nations and firms unwilling to make the difficult decisions now.

A resolute United States that shows a clear commitment to action has the potential to build a coalition of market economies that prefers acting together to proceeding on the present trajectory. Not all will go, or go as far, but this should not slow the United States in making its own hard break. For a nation with America's power and scale, there is no difficult game theory problem when it comes to China, no collective action problem or prisoner's dilemma; only the straightforward choice between protecting our economic and political system or enabling its irrevocable corruption.

Conclusion

For policymakers and analysts catechized in the tradition of globalization and conditioned to fear any inefficient overstepping in the market, a hard break from China may seem implausible. But where economic sovereignty is at stake, the goal is not to ensure that the market continues working as well as possible but rather to dissolve one that does not and cannot work at all. A commitment to free markets entails doing whatever is necessary to ensure that the American market remains free.

Anyone inclined to assert indignantly that "you can't do that" should take note that the United States just did. In response to Russia's invasion of Ukraine, the United States revoked Russia's MFN status and imposed aggressive sanctions designed to separate Russia from the international economic system. This was the hardest of breaks and was supported most strongly by those most vocally enthusiastic about global engagement and a rules-based international order. Whether the United States should take action on a similar scale against China is not a question of legality or capacity, but of values and will.

Appendix

China Legislation, 116th–118th Congresses

The glaring problems in the U.S.-China relationship have prompted a wide range of legislative proposals in recent years, attempting to address in piecemeal fashion many of the issues raised in this paper. While the full list runs into the hundreds of bills, this appendix highlights some of the most significant and thoughtful efforts, from which frameworks and legislative language might be drawn in composing a more comprehensive agenda.

I. Investment

Preventing PRC-Based Investment in America

Chinese Communist Party Influence Transparency Act: Requires agents of PRC-based business entities to register under the Foreign Agents Registration Act.

H.R. 1092 – To place temporary restrictions on acquisitions by the People's Republic of China, and for other purposes: Requires CFIUS to review acquisitions by PRC-based entities of American assets deemed critical to national security, critical infrastructure, or of cultural significance; would sunset at end of COVID-19 economic impact.

Transparency for Malign Chinese Investments in Global Port Infrastructure Act: Directs the Director of National Intelligence to report to Congress on PRC-based investment in global port infrastructure since 2012.

SPACE Act: Prohibits purchase of telecom equipment from PRC-based entities by American space companies; strengthens space company ownership standards; prohibits Commerce Department and NASA funding for PRC-based entities; directs the Secretaries of Defense, Commerce, and Treasury to report annually to Congress on foreign investment in American space activities.

This Land Is Our Land Act: Prohibits PRC-based and CCP-affiliated entities from purchasing farmland in America.

Preventing American Investment in China

Protecting American Capital Act of 2023: Directs the Treasury Department to report annually to Congress on American investments in China since 2008, including investments routed through a jurisdiction outside the United States.

American Financial Markets Integrity and Security Act: Prohibits listing of Chinese military companies on American exchanges; directs the Office of Commercial and Economic Analysis of the Air Force to report to Congress on the strategic implications of American capital flowing to China.

Federal Acquisition and Contracting Transparency Act: Requires disclosure by federal contractors of contracts with PRC-based entities; directs the General Services Administration to maintain a public database of said information.

Time to Choose Act: Prohibits the federal government from entering contracts with management, scientific, and technical consulting firms simultaneously contracting with covered foreign entities, including CCP- and PRC-affiliated entities.

Turn OFF THE TAP Act: Prohibits federal agencies from entering contracts with or funding Chinese military companies, entities on the Treasury Department's SDN List and Non-SDN Chinese Military-Industrial Complex Companies List, the Commerce Department's Entity List, and the FCC's Section 2 List.

II. Supply Chains

Disfavoring Chinese Supply Chains

American Security Drone Act of 2023: Restricts federal procurement of drones made in China for five years; directs the Office of Management and Budget to coordinate with relevant agencies to develop a government-wide drone procurement policy; directs the Defense Department to report to Congress on the drone supply chain, including existing deficiencies and plans to mitigate them.

Bring American Companies Home Act: Allows expensing of costs associated with reshoring from China to the United States.

Ending China's Developing Nation Status Act: Changes China's status from "developing nation" to "developed nation" and commits the United States to implementing that change of status in international bodies.

Structuring Institutions for Industrial Policy

BRIDGE Act: Directs the State Department to report to Congress on China's Belt and Road Initiative (BRI), and existing U.S. efforts to counter it; directs the State Department to submit to Congress a plan to counter BRI, in coordination with the Secretary of Commerce and other relevant agencies.

Industrial Finance Corporation Act: Establishes within the executive branch the Industrial Finance Corporation, to provide support for manufacturing and supply chains in critical industries.

Federal Infrastructure Bank Act: Establishes the Federal Infrastructure Bank to fund construction or maintenance of infrastructure projects in the United States.

National Development Strategy and Coordination Act: Establishes an Interagency Committee for the Coordination of National Development Financing Programs within the Executive Office of the President; directs the Committee to develop a national strategy to address vulnerabilities in the domestic supply chains of critical industries, strengthen American industrial and manufacturing capabilities, and support targeted job growth and economic development.

Industry: Pharmaceuticals

Protecting our Pharmaceutical Supply Chain from China Act: Directs the Department of Health and Human Services to create a registry of drugs produced outside the United States; phases out purchase by federal programs of drugs with active ingredients manufactured by China; mandates country of origin labeling; allows tax expensing for domestic pharmaceutical and medical device property placed in service between 2020 and 2026.

Strengthening America's Supply Chain and National Security Act: Directs the Defense Department to report to Congress on its reliance on Chinese-made pharmaceuticals, with assessment of supply chain resilience, recommendations to end procurement from China by 2025, and recommendations to diversify pharmaceutical procurement generally.

Industry: Critical Minerals

ONSHORE Manufacturing Act: Directs the Department of Energy to create programs for financing domestic rare earth mineral facilities and developing the rare earth workforce; directs the Secretary of the Treasury to establish the Minerals Security Partnership Fund to finance rare earth supply chains; directs the President to submit a plan of action to Congress on deploying the Defense Production Act to enhance domestic rare earth production.

American Critical Mineral Independence Act: Directs the Critical Minerals Subcommittee of the National Science and Technology Council to coordinate American critical mineral supply chains; directs the National Science Foundation and the Department of Energy to fund critical mineral research programs; includes a variety of measures to expand the domestic exploration, development, and processing of critical minerals.

Critical Mineral Independence Act: Directs the Defense Department to report to Congress on the critical mineral supply chain and enact a strategy to ensure that the supply chain for the National Defense Stockpile is based in the United States and allied countries by 2027.

RE-Coop 21st Century Manufacturing Act: Directs the Commerce Department to establish a privately funded Thorium-Bearing Rare Earth Refinery Cooperative to create a fully integrated domestic rare earth value chain.

Industry: Energy

Keep China Out of Solar Energy Act: Prohibits federal procurement of Chinese solar panels and requires a federal study of domestic solar panel production.

Accelerating Productive Investment

Make in America to Sell in America Act of 2021: Requires the Commerce and Defense Departments to create a list of finished and intermediate goods whose production is critical to the domestic industrial base or national security; mandates that listed items contain at least 50% domestic value content.

III. Institutions

Ensuring Research Integrity and Security

Preventing PLA Acquisition of United States Technology Act: Prohibits federal agencies and American companies and universities that receive federal assistance from engaging in certain research or technical exchanges with PRC-based entities of concern; requires all recipients of federal assistance to annually report to the Defense Department their engagement with PRC-based entities of concern.

Stop Funding Our Adversaries Act: Prohibits federal funding of research in China.

Chinese Research Funds Accounting Act: Directs the Government Accountability Office to conduct a study on federal funding to PRC-based entities within the past five years.

Safeguarding American Innovation Act: Increases oversight and control of federally funded research projects and disclosure of foreign funding.

FOIA Fix Act: Prohibits Chinese, Russian, North Korean, Iranian, Cuban, Syrian, and Venezuelan persons or entities from obtaining U.S. government records via the Freedom of Information Act.

Think Tank Transparency Act: Requires think tanks to submit disclosure reports to the Attorney General on any foreign sources of funding.

Disclosing Foreign Influence Lobbying Act: Amends the Lobbying Disclosure Act of 1995 to require lobbyists to identify any connection with a foreign government or political party that plans, supervises, directs, or controls any effort of that lobbyist, regardless of those entities' financial contributions to the lobbying effort.

Protecting the Academy

Preventing Malign Chinese Influence on Academic Institutions: Requires universities to disclose contracts or gifts over $5,000 received from PRC-based entities.

Dump Investments in Troublesome Communist Holdings Act (DITCH) Act: Denies tax exemptions to organizations that hold any interest in a disqualified PRC-based company or fail to transmit required annual reports on time.

End College CCP Act: Prohibits universities that have contractual partnerships with PRC-based entities from receiving federal funds.

Countering China's Theft of American Research and Innovation Act: Modifies provisions related to reviewing visa applications for risks, including illicit transfer of sensitive research from American institutions.

Protect Our Universities Act: Establishes a task force (including representatives from the Director of National Intelligence and the Defense, Education, Energy, and Justice Departments) within the Department of Education to address espionage at universities; creates a sensitive research projects list and bars Chinese, North Korean, Russian, and Iranian nationals from participating in such projects without express approval from the Director of National Intelligence.

SECURE CAMPUS Act: Prohibits Chinese nationals from receiving Schedule F or J visas for study in STEM fields; prohibits federal funding for research in STEM fields by Chinese nationals or participants in PRC talent recruitment programs; requires participants in such talent recruitment programs to register under the Foreign Agents Registration Act; directs the State Department to publish an annual list of PRC foreign talent recruitment programs.

AMERICAN COMPASS

POLICY