



MERICS

Mercator Institute for China Studies

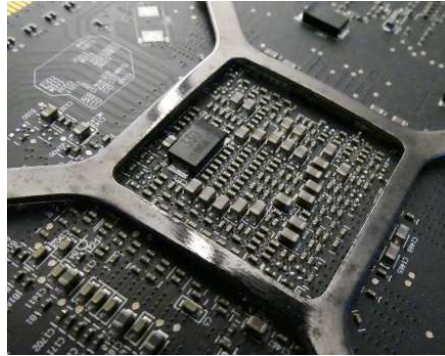
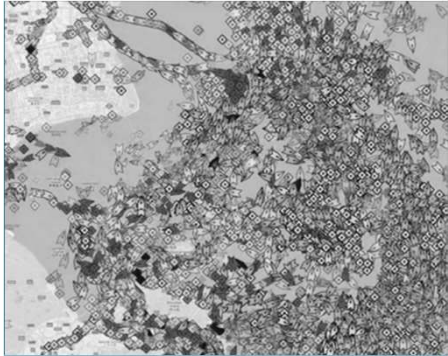
ISLA | 10. May 2023

China's quest for global tech leadership: What are the challenges European manufacturers must cope with?

Max J. Zenglein, Chief Economist

China is entering a „new political and economic era“

... creating a high-stress environment for international counterparts



Pressure is rising

Cyclical, structural
and economic policy
factors combine with
a tense political
environment and
geopolitical
turbulences

XI'S RECIPE

Common prosperity

共同富裕
Gòngtóng fùyù

Dual Circulation

双循环
Shuāng xúnhuán

**Nat. self-confidence +
new development stage**

新发展阶段
Xīn fā zhǎn jiēduàn

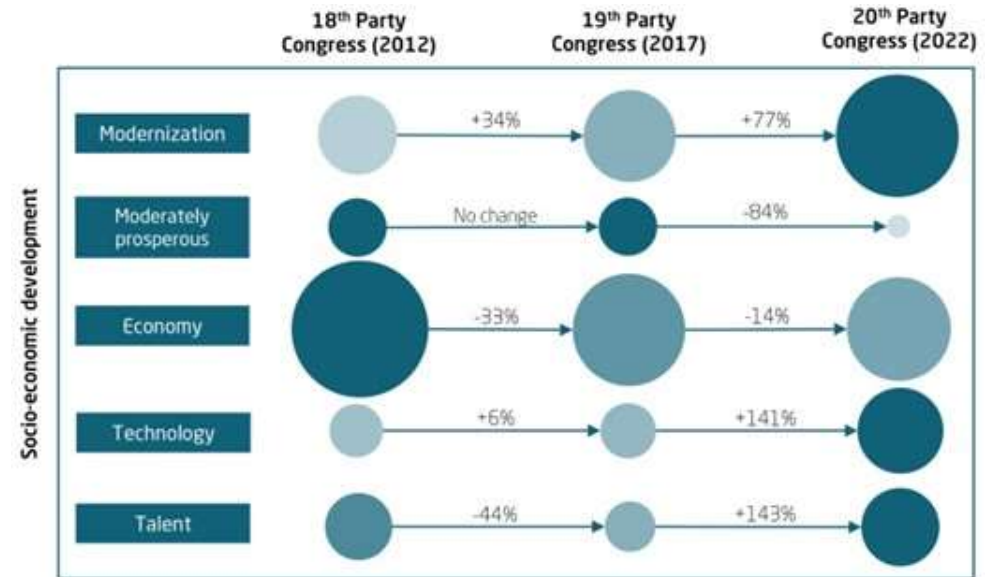
**Indig. innov. + techn.
indep. + self-reliance**

自力更生
Zìlìgēngshēng

Economic policies prioritize long-term strategic targets

- Reform shift under Xi boosted the CCP's position in the economy:
 - The return of the Party as a central economic actor
 - An emphasis on securitization - including economic and technological security
 - Rising nationalism and a politicization of economic decision-making
- Economic challenges ahead and rising geopolitical tensions are accelerating this trend

Mentioning of terminology in government work report

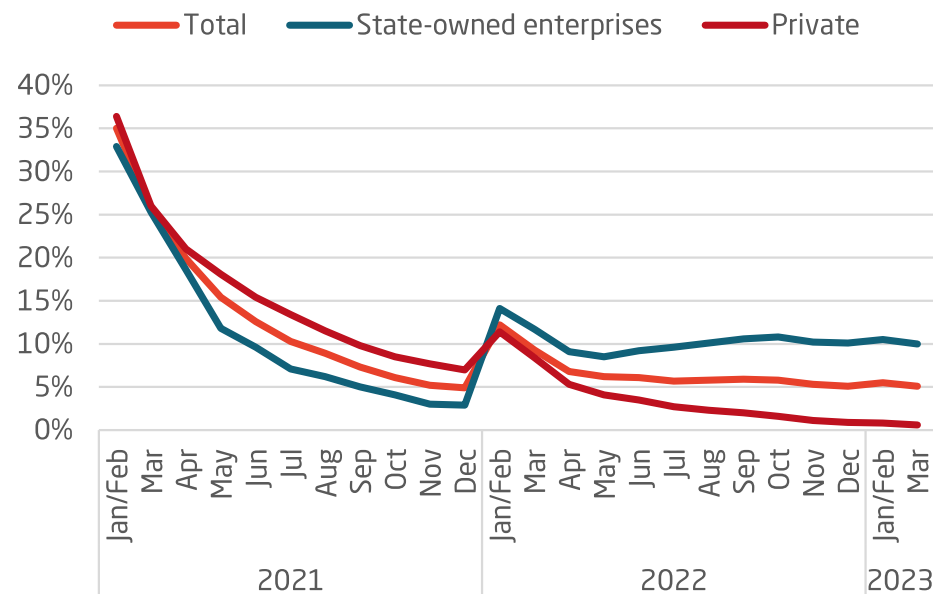


Source: MERICS PoliXi Tracker

Ideological driven policies are geared towards shaping China's economy

- The economic slowdown in 2022 is largely self-induced
 - **Zero-Covid exhaustion:** reoccurring lockdowns and lack of exit strategy weighed down confidence
 - **PoliXi-overdose:** Tech and real estate crackdown, Common Prosperity, reducing emissions and financial risks all cut economic growth and have unknown side effects

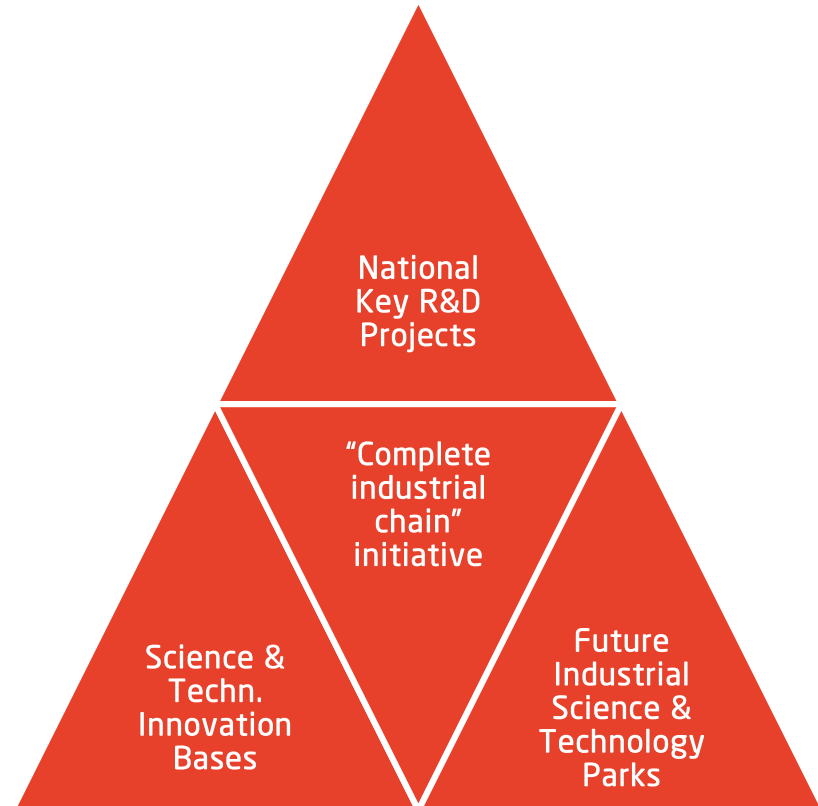
Fixed asset investment by ownership, ytd yoy



Source: NBS

All nation effort: economic actors need to align with national goals

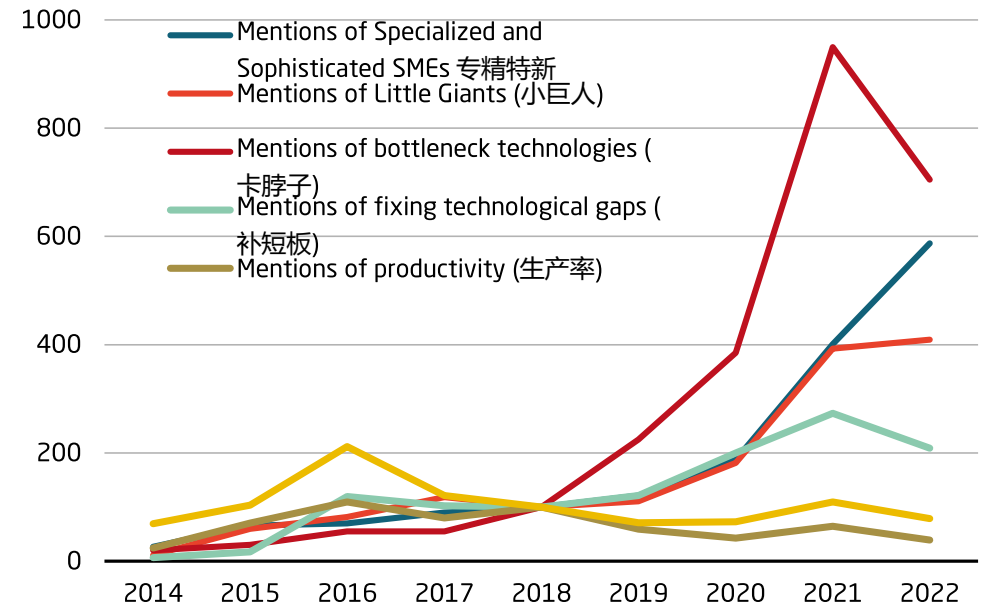
- The CCP prioritizes the achievement of national strategic goals in order to become a global technology leader....
-and expects companies to follow suit
- Clear distinction between strategic and non-strategic business areas:
 - Strategic: Industry and research
 - Non-strategic: consumer internet or real estate
- China is building a new innovation ecosystem:
 - National Research Laboratories
 - Orientation of the financial system
 - “Little Giants” - Empowering SMEs



The incubator state: A new-style of industrial policy

- Unleashing innovation under guidance of the Party:
 - „Science has no borders, but scientists have motherlands“ (President Xi in 2020)
 - Politburo study session in January: “We must mobilize resources nationwide to build up China’s strategic scientific and technological strengths”
- New efforts focus on breaking foreign tech reliance “strangleholds”
- The private sector and SME’s have a vital role to boost China’s innovation capabilities

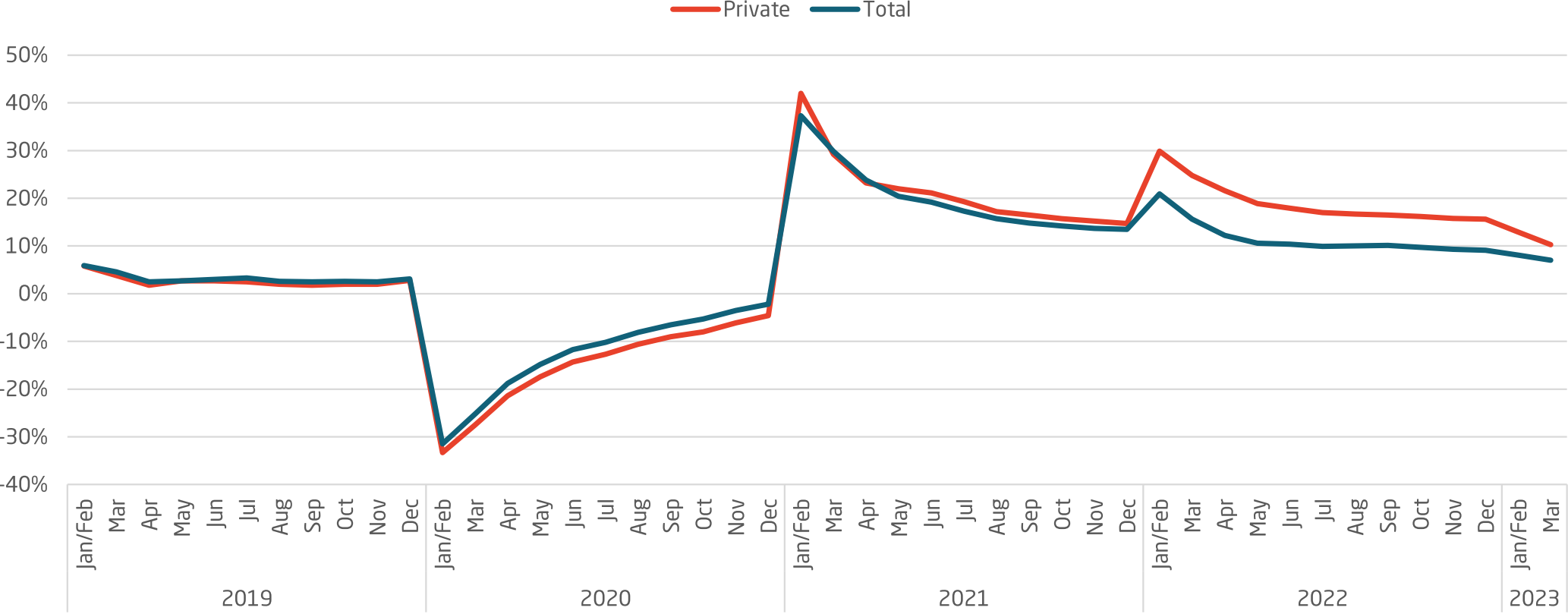
Mentioning in national and provincial policy documents, index 2018 = 100



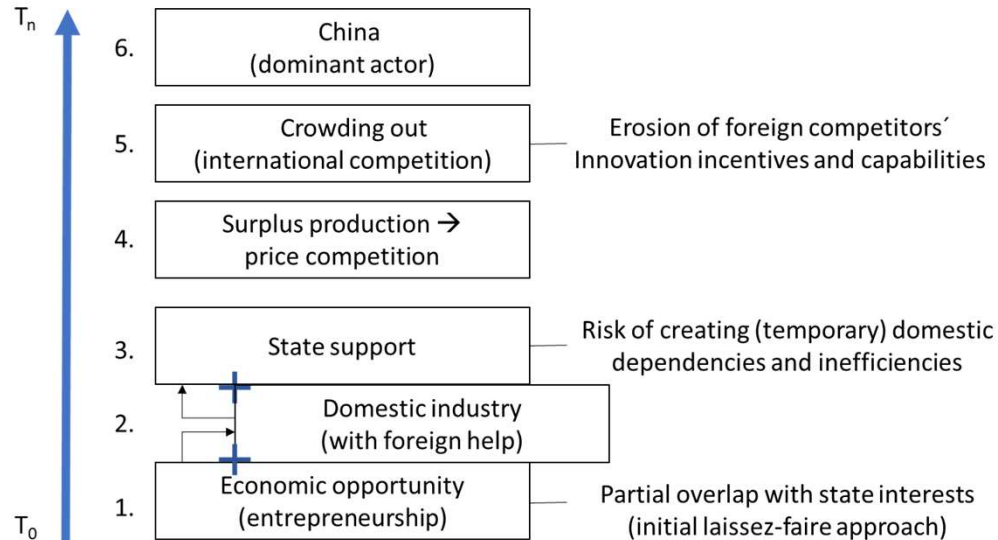
Source: MERICS PoliXi Tracker

Prioritizing the real economy: Private sector investment is responding to national needs

Fixed asset investment in manufacturing, ytd yoy



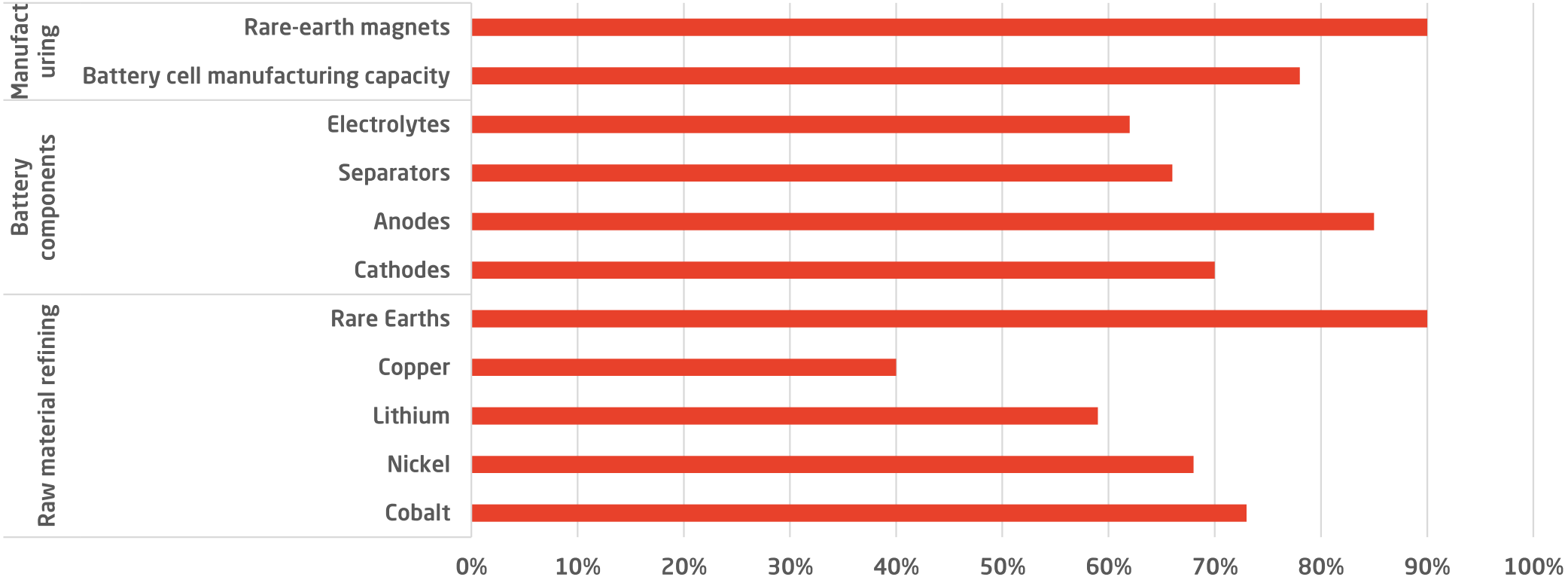
China is optimizing its industrial policy implementation



- Key focus on innovation, emerging tech and digitalization – and national pride
- Guided market mechanisms have a vital role in improving efficiency in strategic sectors
 - Improve capital allocation by improving financial system
 - Encourage establishment of „hidden champions“
- Beyond market share: focus on cross horizontal policies including smart manufacturing, digitalization, AI and standards

China dominates the EV supply chain

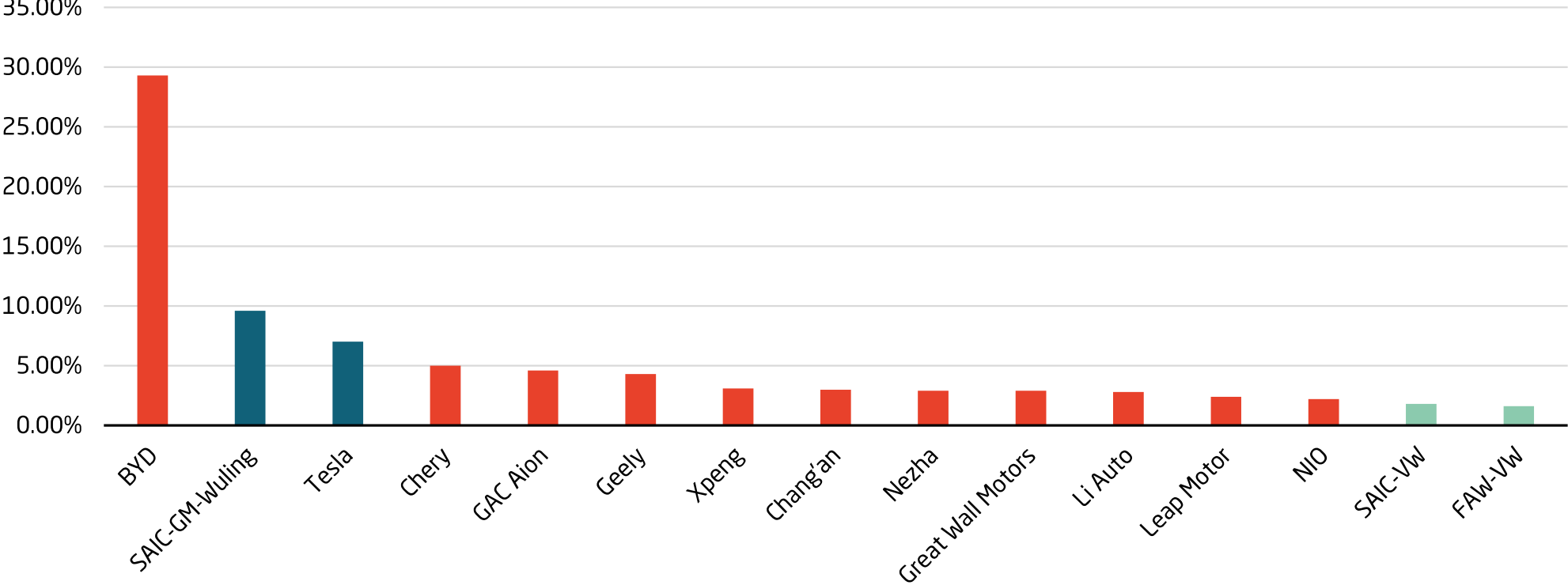
China's share of global refining and production of raw materials and EV supply chain components



Source: Brookings; IEA; East Asia Forum.

Chinese producers dominate China's EV market

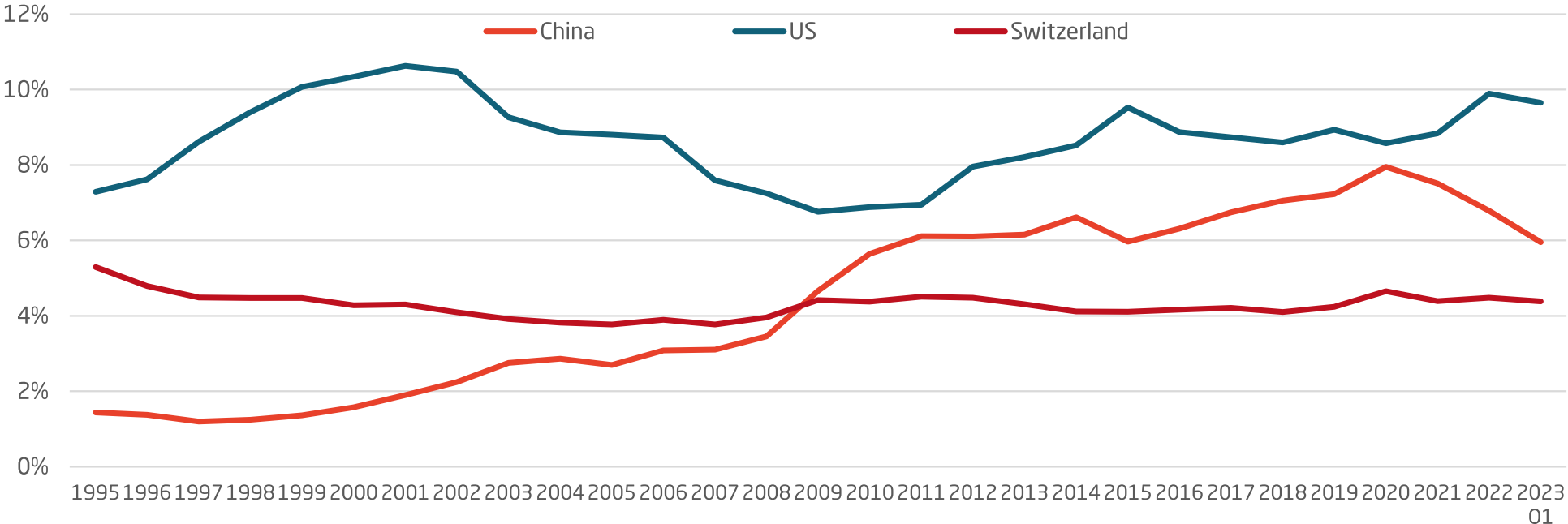
Top 15 EV producers in China by market share in terms of units sold (Jan-May 2022), carmakers with foreign (blue) / German (turquoise) ownership stake highlighted.



Source: CPCA. Note: EV includes BEV, PHEV and FCEV.

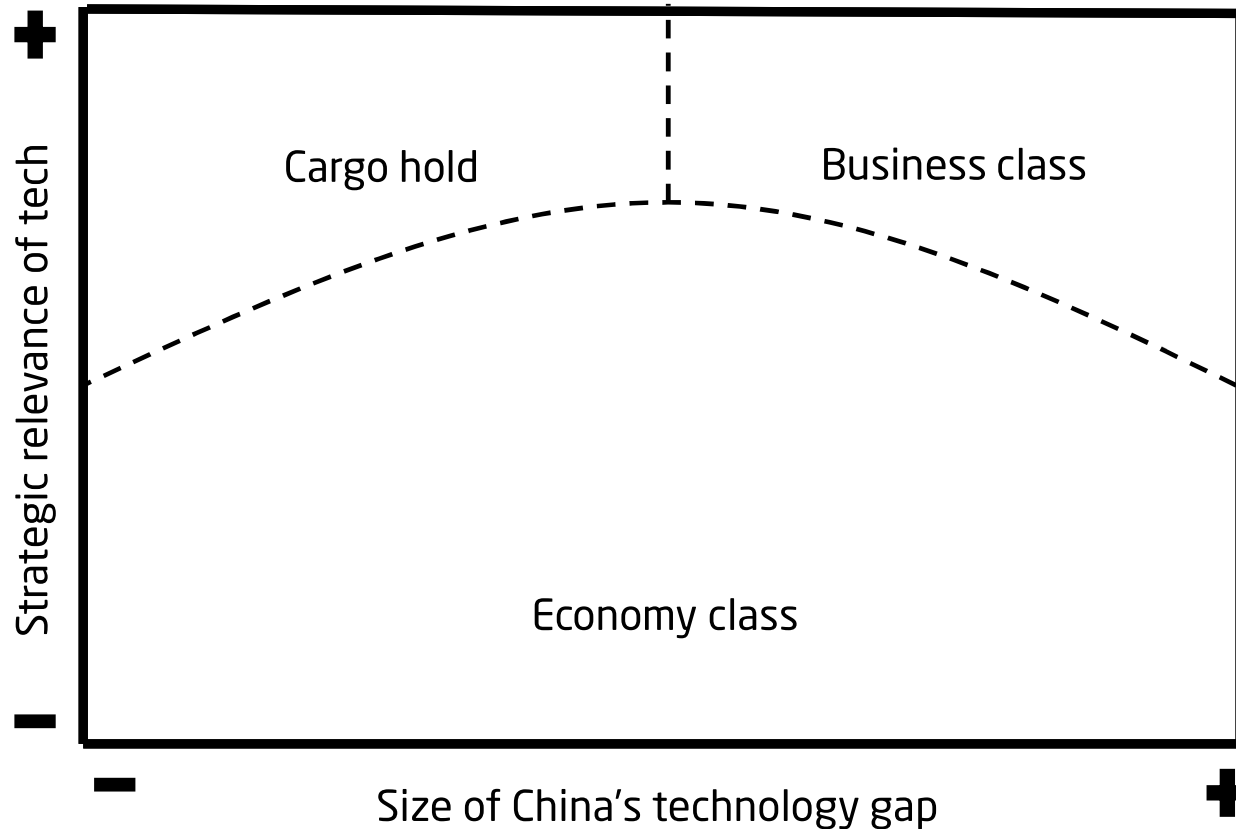
More self-sufficiency reduces the prospects for exports to China

Share of German exports by destination



Source: Destatis

The market environment for foreign business is quickly changing



- China's innovation system (still) relies on foreign expertise
- The market size as well as the dynamic technological environment make China very attractive for foreign partners
- Foreign companies and academia should help:
 - Bringing technology and know-how into the country
 - Increasing tech **self-sufficiency** and supply chain security
 - Strengthening competitive conditions in China
- Increasing competition in third-party markets



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GETTING CHINA **RIGHT**

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