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US confronts China with broad-based China Initiative

On Dec. 20, 2018, the United States Department of Justice unsealed indictments against two Chinese nationals for allegedly working with the Chinese Ministry of State Security in a long-running campaign to hack into managed service providers and obtain sensitive economic and business information. According to the indictments, Zhu Hua and Zhang Shilong are members of Advanced Persistent Threat 10 or “APT10,” a hacking group that has been infiltrating networks around the globe since at least 2006.

“Today’s charges mark an important step in revealing to the world China’s continued practice of stealing commercial data,” said U.S. Deputy Attorney General Rod Rosenstein in a press release. “More than 90 percent of the Department’s cases alleging economic espionage over the past seven years involve China. More than two-thirds of the Department’s cases involving thefts of trade secrets are connected to China. ... We want China to cease illegal cyber activities and honor its commitment to the international community, but the evidence suggests that China may not intend to live up to its promises.”

The indictments are part of a concerted effort by the U.S. government to confront and combat China on a wide economic front; the effort even has a name: the China Initiative. On Nov. 1, 2018, then-Attorney General Jeff Sessions announced the “China Initiative” to combat economic espionage, specifically cybertheft and the theft of innovative and foundational technologies.

“This Initiative will identify priority Chinese trade theft cases, ensure that we have enough resources dedicated to them, and make sure that we bring them to an appropriate conclusion quickly and effectively,” Sessions said. “This administration’s new initiative will also address two major responsibilities of our National Security Division: the Foreign Investment Review Staff’s review of investments and licenses in U.S. infrastructure and telecommunications, and the Foreign Agents Registration Act Unit’s work to counter covert efforts to influence our leaders and the general public.”

But in a broader sense, the China Initiative represents the new normal between the two largest economies in the world. Despite signs of a thaw (both countries agreed to a “truce” at the G20 Summit in Argentina), the issues at stake are difficult and have been on the negotiating table for many years. The trade war between China and the U.S. will most likely continue into 2019, affecting the export, investment and supply chain strategies of companies on both sides of the Pacific Ocean for some time to come.

Status report

For those following the ongoing trade war between China and the U.S., this announcement is the culmination of a series of actions precipitated by a report delivered by the Office of the United States Trade Representative on March 22, 2018. The report came at the behest of the Trump administration, which instructed the office to “determine whether to investigate under section 301 of the Trade Act of 1974 (Trade Act) (19 U.S.C. 2411), laws, policies, practices, or actions of the Government of China that may be unreasonable or discriminatory and that may be harming American intellectual property rights, innovation, or technology development.” The report found that China’s policies were indeed unreasonable and a burden on U.S. commerce, mentioning joint ownership, cybertheft, technology transfer requirements, market access, and other restrictions, including tariff

and non-tariff trade barriers. The U.S. acted quickly:

- The government produced a list of goods subject to tariffs, and then imposed tariffs on those goods.
- U.S. President Donald Trump signed both the Export Control Reform Act of 2018 and the Foreign Investment Risk Review Modernization Act of 2018 into law, tightening controls on “dual use items” and the transfer of “foundational and emerging technologies” to potential rivals.
- The U.S. also attacked several major Chinese tech firms The U.S. also attacked several major Chinese tech firms, including ZTE Corporation and Huawei Technologies Co., Ltd., in an attempt to curtail those companies’ efforts to expand their business and, in the eyes of the U.S., Chinese government influence beyond China. The U.S. and several other countries have pushed back against buying products and services from Huawei, while the Chinese government and many state-owned and private companies have thrown their support behind the company.
- The U.S. also filed charges against Huawei’s CFO (the daughter of the company’s founder), Meng Wanzhou, and demanded she be extradited from Canada, where she was arrested by Canadian authorities. The U.S. has 60 days to file a formal extradition request. China has denounced the action and, in a sign of retaliatory measures to come, detained three Canadians in the last two months.
- The U.S. Department of Justice indicted individuals involved with a Chinese and Taiwanese company for economic espionage and has stepped up actions against Chinese companies accused of fraud.

At the G20 summit in Buenos Aires, President Trump and Chinese President Xi Jinping came to an agreement, characterized by the White House as “highly successful.” According to a White House statement following the summit, certain conditions were agreed to: “On Trade, President Trump has agreed that on January 1, 2019, he will leave the tariffs on \$200 billion worth of product at the 10% rate, and not raise it to 25% at this time. China will agree to purchase a not yet agreed upon, but very substantial, amount of agricultural, energy, industrial, and other product from the United States to reduce the trade imbalance between our two countries. China has agreed to start purchasing agricultural product from our farmers immediately.”

Chinese statements (in Chinese) left out mention of intellectual property and trade concessions, instead stating, “We will implement the consensus of the meeting in Argentina between the China and U.S. heads of states, and we will advance China-U.S. trade negotiations.”

Multifront action with varied results

The China Initiative involves not just cybertheft and economic espionage, but also trade, geopolitical struggles in North and Southeast Asia, and high-level technological competition between established U.S. companies and their rising Chinese competitors. The struggle between the two great nations has already had a significant impact on supply chain strategies and risk assessments for companies doing business in the Asia-Pacific theater. While the U.S. and China compete with each other across the board, causing companies to seek alternative sources for goods and parts, entire industries are re-strategizing, such as American agriculture and automotive industries, and Chinese steel and electronics industries.

There is a glimmer of hope, as officials on both sides are trying to set up meetings in January 2019 to discuss trade and other issues. There is, however, a lot of uncertainty around both the willingness of China to concede to U.S. demands and the unpredictability of any unilateral White House actions.

But the dangers and risks are not just economic in nature. According to Session’s speech on Nov. 1, the China Initiative will also focus on noneconomic sectors in which China may be trying to gain influence or power. In that

case, the risk of ongoing tension and conflict between the two nations—which may spill over into trade, regardless of how negotiations proceed—looks to be the new normal going forward.

“Today, we see Chinese espionage not just taking place against traditional targets like our defense and intelligence agencies, but against targets like research labs and universities, and we see Chinese propaganda disseminated on our campuses,” Sessions said. “And so I have directed this initiative to focus on these problems as well and to recommend legislation to Congress if necessary.”

Takeaways

- The U.S. targets Chinese cyber-espionage activities and trade policies as part of a broad-based move to combat China’s influence abroad.
- The Sino-U.S. trade conflict looks to spill over into educational and social issues, as well, including U.S. investigations into possible Chinese influence in American universities and research labs.

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