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China invests in tech: Implications and opportunities

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Hanish Patel: I'm Hanish Patel, and this is User Friendly, the show where we explore emerging trends in tech, media, and telecom and how they impact business operations and the world around you. Around the globe, many countries are increasing their investments in technology in order to compete with the US and other leading countries. One country that certainly makes the top of that list, and that we've been hearing quite a bit about in the news of late, is China. Today, we'll dive into a fascinating discussion around China and technology, and some of the forces that have a wide-reaching implication for relations between US and China, as well as multinational corporations in the TM&T industry. Joining me is Ken DeWoskin, founder of Deloitte's China Research and Insight Center. He serves as a senior adviser and eminence fellow on the topic of China, so we're thrilled to have him here today. Ken, welcome to the pod.

Ken DeWoskin: Well, thank you very much. Pleasure to be here.

Hanish: So Ken, let's just jump straight into it, and I know you travel to China . . . I won't even say on a frequent basis, but you could set your watch to it in terms of the amount of times that you are going to China. What have you observed in the major Chinese cities—take Shanghai, for example—in terms of technology use, and how does it compare to what we're seeing in the US?

Ken: Well, I think the first thing that's very noticeable is the speed of adoption. I actually made my first trip to China in 1977, before economic reforms began. Extraordinarily rare for anybody even to have a black-and-white television set. Shanghai today, it's extraordinarily rare to see anybody walking on the street who is not looking at their mobile phone, either

paying bills, or shopping online, or playing some zombie game, or whatever. So there's been a dramatic transformation. And along with that, the providers of technology and technology devices in China have become very, very prominent, not only in that market, but globally.

Hanish: What you described there doesn't sound too different from what I see in LA, when I see a lot of people walking down the street with their face buried in their phone. But are you saying it's the pace of adoption, or is it just the spread of that technology across China that's just mind-blowing?

Ken: Well, it's both. And I think your question raises a really interesting point. There are characteristics of what you might call the life/work relationship in China which are very different from LA, for example. Very few people in China would drive to work. If the situation provides, they would take a DiDi vehicle, which is equivalent of a rideshare vehicle.

Hanish: Right.

Ken: Or mostly on the subway, or buses, or other forms of public transportation, which means that they are free to look at their devices to shop, to pay bills, to do the other sorts of things. We would hope that in LA, where most people are driving, that they wouldn't be shopping online, they wouldn't be texting. They might be paying their automotive liability insurance online, but other than that, they should probably be watching the road.

Hanish: So for someone who's—to your point earlier—that's been going out to China for so many years and looking at how the relationship has somewhat evolved between US and China over the many years, moving right forward to the current negotiations, I'm curious if you can break down for the listeners some of what you see are the key challenges as it relates to tech, to media, to telecom industry that are on the table?

Ken: Yeah, there's a very long list, really, of things that are interesting and, I think, worthy of attention. And I would hope that people would invest a little bit of time to understand better. One is that China is in many ways like previous waves of emerging markets, going back to the end of the Second World War—Germany, Japan, and then the Four Tigers: Taiwan, North Korea, Hong Kong, and Singapore—they all emerged in similar ways. But in those instances before China, as they emerged, they became very important developers of consumer technology products. Every one of them, actually, went through that stage. In many cases, they used technology that was developed elsewhere and applied it to commercial ends, which hadn't been done before. So in Japan you had, for example, the invention of all sorts of miniature consumer electronic devices, beginning with the Walkman. They used integrated circuit technology that had actually been developed in the United States, but never commercialized. So you had that pattern.

The other pattern that was important is that in each of those countries, as they enriched and as they developed, they became important supportive members of existing global institutions, including technology standards institutions. And China has taken a somewhat different path, in part because its market is so huge and its own economic model is so different. So China is serving its domestic population, it's expanding its global footprint in terms of technology projection, but it's also having a very mixed impact on things like global standards, organizations, and the global key international economic organizations that have been more stable up to that point. So we'll see. And I think that's one of the origins of some of the pressures now that exist in this trade and investment discussion that's going on.

Hanish: So let's talk a little bit about some of those pressures, or negotiations. When I think about some of the trade negotiations and how they're being portrayed in terms of just by the media between the US and China, do you see a difference between what we're hearing and what's going on? Given the amount

of frequency you're in China, you're in US, and you get a real balanced view of both of those.

Ken: Yeah. Well, definitely, the view of what's going on is extremely different. Almost . . . If you could construct it as polar opposites, you can fairly say that they're sort of polar opposite.

Hanish: Right.

Ken: In terms of what's fair and what's not fair, in terms of the applicability and the sort of correctness of the tactics being used on either side, and what the ultimate outcomes might look like. And for a start, I'd say we often talk about things like the art of the possible. What it's possible for either side to do—because either side isn't 100 percent flexible—there's certain things that China cannot do in terms of its basic economic model, and there are things that the United States cannot do in terms of its basic economic model.

Hanish: Mm-hmm (affirmative).

Ken: And then there are the political issues. We have elections in the United States; we don't have those kinds of elections in China. So the political pressures that bear down on the leaders who have to make these important decisions, and finalize these negotiations—I should say advance these negotiations—are very, very different.

Hanish: Mm-hmm.

Ken: Overall, if you were to sort of reduce it to a few simple comments, in China, the view remains very prominent that the US is trying to contain its growth. In the US . . . I think our listeners will be familiar with the view, which is to say that China has taken a lot of technology for which US companies have not been compensated. Their economic system, which is largely state-owned, or even state-supported—we're not explicitly state-owned—can compete unfairly globally and certainly compete unfairly in the domestic mainland market.

Hanish: And then, certainly with that backdrop—back to the negotiations—you're always hearing things with these trade frictions that are going on, so to speak, between US and China. What does that mean for our tech, media, and telecom companies here in the US that may be reliant on China for some of the production and aspects of their supply chain overall?

Ken: Yeah. Well, I'm very glad to hear you say "reliant" on China, because that is the reality.

Hanish: Mm-hmm.

Ken: And it's not a reality that is often recognized by our media. Our media tends to focus on the negative aspects of the relationship. But if you look back at China, especially since around 1995, China and Chinese assemblers have been major customers, or Chinese tech companies, possibly the most significant customers they have outside the United States. In fact, I think obviously the most significant customers they have outside of the United States. So the contribution of China to the top line of major chip makers, and major developers of technology solutions, and major software developers, is very, very high. And that needs to be recognized. And one reason that needs to be recognized is, if you want to look forward at the scenarios that might emerge over the next, say, five to 10 years, that history is important because there's going to continue to be a lot of commercial reasons that US companies are going to want to cooperate with Chinese companies and are going to want to work with them as customers and as suppliers.

Hanish: And let me drill a bit further on that topic. We both mentioned here the reliance, so to speak, of US on China, particularly from a production perspective, but let's look at it from the other direction. How do our tech and our media and our telecom companies think about how do they serve the China market? And kind of look at it from another perspective. What's your thoughts from there?

Ken: Well, I think that right now, contrary to the expectations we might have had, US tech companies are actually continuing to invest in China. There's some migration of supply chains, and some migration of customer bases out, but I think it's not as significant as the new investment going in. And the reason for that is that China has been very out-front about the reliability of its own supply chain.

Hanish: Mm-hmm.

Ken: And so they've constructed an unreliables list, and tech companies that have interrupted supply to China, even when under considerable political pressure in the United States, can find themselves on the unreliable list. And if they're on the unreliable list, they face the possibility that China will invest in import substitution, that China will try to develop products that substitute from what they're currently buying from the United States.

So we put ourselves, as US companies, we put ourselves in that high-risk situation right now, in a sense unnecessarily. One of the strategies that high-tech US companies have deployed is to move more operations to China, and actually, in a sense, localize them in China, including R&D support for their product development. In that case, it continues to be an asset for the US company, but it does involve new investment into China, and more localization, and in some respects, more exposure of intellectual property.

Hanish: So thinking about the constant negotiations that are taking place between US and China, I can only imagine that for the executives and leaders of multinational corporations . . . For them to plan for the future, what should these executives of those companies that are affected by these negotiations be mindful of?

Ken: Well, a couple of things. This is an important time. It's a time when traditional planning processes are no longer adequate to the challenge, I would say.

Hanish: Mm-hmm.

Ken: And to look at one aspect of it, if you look at supply chain migration, for example, which is an area where we have a lot of demand at the moment, companies really don't know enough about what's going on. They don't know enough about the prospects of settlement, and what a settlement might look like in the ongoing negotiations, to plan in a very granular and reliable way. And so what they now face is a possibility of building a high level of redundancy in their supply chain to avoid future spills, avoid future shortages and major disruptions. We talked about that as buying a kind of insurance against the future. Basically, what's happened—again, to put it in very simple terms—is that supply chain professionals in major tech companies, product development professionals, and marketing professionals in major tech companies may be very, very good in the traditional demands of those jobs, but they are not that experienced in the politics that now bear down on their responsibilities and the politics that will shape their future roles.

Hanish: Got it. So let me pivot a little, if I may, to a slightly tangential topic, but still very related to tech projection, particularly when it comes to China. If we look at even just the next five years, when we think about some of those critical areas around AI, and IoT, and different areas that are using data, and like I mentioned, just the proliferation of technology advancements

that are taking place, what do you see for the projection for China in that space?

Ken: This is a difficult and very sensitive area to talk about, because it's very easily interpreted as a comment on the people in the relative . . . in the two countries.

Hanish: Mm-hmm.

Ken: And I want to be very clear in commenting on this that we're not talking about the capability of the US population, or the Chinese population, to be innovative or to develop technology in the future.

Hanish: Right, right.

Ken: That's not the point of this. But economies at different states with different structures do have different competencies and do have different prospects for development. I already mentioned earlier in talking about emerging economies that they have often excelled at innovation at the application level of technology. So really, the answer to this question involves us to look a little bit at the tiers of technology—from basic research in things like semiconducting, superconductivity, material science, artificial intelligence, hypersonics, quantum computing—all the way up to the development of things like drones, and 3D printers, and surveillance cameras, and flat-screen television sets—curved and otherwise—and 8K, and all the things that are hitting the consumer markets.

It's at that application level that I would expect China to continue to be very innovative and very successful and probably become the dominant player in the world. I think that's actually the case. But the other layers, which include the basic science I just described, and intermediate levels of, say, very, very high-quality, very dense semiconductor creation, I think it's a while before China will reach world-class standards. Right now they're still dependent on foreign technology, and are likely to be so for the next decade or so.

Hanish: And then just continuing on from that, how do you see that directly impacting our tech companies in the US for sure?

Ken: Well, I think tech companies that look at those tiers, and understand where the future will bring cooperation opportunities and where the future will bring competition, can actually plan accordingly.

Hanish: Right.

Ken: Because it dictates that you would want a certain kind of relationship with, say, a Chinese counterparty—might be a customer, might be a supplier, might be an R&D partner, or whatever—at the basic intermediary level, and a different kind of relationship at the application level. And so that that level of analysis, I think, is really important for executives to think about. We tend to talk about technology competition in a very undifferentiated way. It is not one gross mass that in all respects is equivalent, as you well know. It's extremely complicated in terms of the whole process of developing something like the transistor, to the kind of devices we have today, and provide today, that have unbelievable capability—billions of circuits, essentially, in a postage stamp–sized chip.

So if you start to think about the long processes involved, the kind of investment involved, the kind of institutions that support that investment, and then take how these things are taken to market, you can understand that at the end of the day, there's a division of labor, even in technology development, even in technology deployment, which is going to be very important for defining the future, and quite frankly, important for companies to understand to succeed in the future.

Hanish: And Ken, to somewhat close out the episode, at the start, you kind of gave the example of when you first went out to China, and the black-and-white TV, to where we are today with everyone's face buried in some form of screen or another. Having been out there so much, what's the biggest leap that you've seen that's made you stand back and say, "Whoa, that's something pretty cool" or "That's something really innovative" that's taken place that you've seen come out to the consumer?

Ken: Well, that's a tough question, because so many things have happened, it's hard to isolate what the biggest one is. China has enabled the creation of companies that have a breadth of services that have not occurred in any other economy. And so the big platforms, the two big platforms in China, kind of do everything in their relationship with their consumers in a way that doesn't happen in the United States, doesn't happen in Europe, doesn't happen in Japan, really.

Hanish: Mm-hmm.

Ken: And that high level of integration of services permits people to do things like order food, pay all their bills, buy their clothing, buy their travel needs, all from essentially one vendor.

Hanish: Right.

Ken: And so they could build the skill to optimize their use of these platforms and actually use them very, very efficiently. On the other hand, that model also has all of the shortcomings of a duopoly situation in terms of efficiency, cost, innovation drivers, and other things. So we'll have to see how that works out. But I think the unique characteristic is the extent to which that huge population is tied to equally huge providers of digital platforms, and all the services that that implies.

Hanish: So Ken, before I let you go, any final thoughts that you want to add? Again, given your extensive experiences, spending so much time in both countries and seeing that evolution in technology, give us a final thought for our listeners.

Ken: Okay. Well, I would say this: The current situation I think is a little bit of an anomaly.

Hanish: Mm-hmm.

Ken: I don't think that what we're talking about right now and the issues and the frictions that affect not only trade, but also investment, I would have to say—and that's an important part of this story—are not really the long-term definers of what this relationship between the US and China will be. I think that we'll be able to stand up a better relationship in the near future. We are never going to be able to proceed without some level of negotiation, that's now baked in.

Hanish: Right.

Ken: Some level of competition across a wide range of technology fronts, that's now baked in. But by and large . . . I'm not quite a rose-colored glasses type person, but by and large, I'm actually quite optimistic that the positive relationship that we've talked about over the last 20 years will actually reform itself in a potentially even more positive way in the future. And I think US and China working together is a very positive combination in terms of the entire global population, and especially the emerging economies in the world, that they themselves will be huge consumers of technology products in the next decade.

Hanish: Brilliant. Well, we'll certainly be watching closely in terms of these trade negotiations as they continue to evolve, and China's investment in technology, and increased to see the implications that play out for tech and media and telecom companies in the US and across the globe. And with that, Ken, I really want to thank you for joining me today. It's been an absolute pleasure to have you on. And until next time, happy listening.

Ken: Thank you very much. My pleasure entirely.

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