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Editor's Note

Welcome to the June, 2024 edition of *Plugged In*. I am filling in this month for our editor, Heather Frayre, during her well-earned vacation.

This month we focus on the U.S. and China relationship as North America's EV transition is introduced to the "Trade War." Our colleague, Mark Heusel, Chair of DW's East Asia Practice, has recently returned from speaking at the China Auto Chongqing Summit 2024. Mark was the lone speaker on the U.S.'s drive towards electrification and what it meant for the Chinese auto industry. In an article he authored and in a short follow-up interview, he shares his insights and opinions regarding how Chinese OEMs view the proposed increase in tariffs to be imposed on Chinese imports and in general the progressively antagonistic relationship between Washington and Beijing. As you will undoubtedly note, Mark's take is that ratcheting up the Trade War through the use of tariffs and other regulatory measures may actually hinder the U.S.'s drive towards competing with China in the EV space over the long term.

Finally, we dedicate our In Case You Missed It column to bring to you attention a number of recent interesting articles on this subject.

I hope you will find reading this edition entertaining and informative.

Robert Weiss | Of Counsel | Co-Chair, EV Initiative

The Cost of a Trade War: Reflections from China and EVs Caught in the Cross-hairs

As I prepared to leave for the 2024 Chongqing Auto Summit, I was filled with both excitement and a bit of trepidation. Chongqing is a beautiful city in South-Central China tucked into the mountains and inhabited by over 30 million residents. It is known for its Hot Pot, home to the Ford joint venture with Changan, and many leading Chinese automotive companies. It has been a little more than 5 years since I attended (in person) an automotive conference in China where I had a featured speaking opportunity, and frankly I did not know what to expect. The agenda for the Summit was provoking: The topics were engaging and focused on both business considerations and technology development and the list of speakers was impressive. Nonetheless, the program had a distinctively Asian-based theme. I had the benefit of, and the isolation in, being invited to speak on the U.S. perspective, including trade policies, the U.S. initiative to electrify, and what it meant for U.S.-China relations. The last time I covered the importance of U.S. and China relations in the auto industry, the world had not gone through COVID, former President Trump had only tweeted about tariffs on Chinese goods and, but for Tesla, the West had not discovered its EV ambitions. In those days, the U.S. and China were celebrating collaboration, joint opportunities and the future. Blue and Red states were actively seeking Chinese investment, and N.A. OEMs were salivating over China's growing domestic consumer market.

Five years on and the world is a very different place. My trepidation for traveling, largely fueled by a constant barrage in the media around deteriorating relations between the U.S. and China, the ramping up of trade sanctions, and the dire travel warnings issued by the U.S. State Department added to this adventure. I have travelled to China many times over the years, and even as recently as May, but this trip felt different. I was headed into the eye of the storm; the Chinese auto industry of late has been maligned for all types of wrongfulness. Whether it is allegations of technology theft, market distortions, forced labor accusations, anti-dumping, or simply fears of unloading their overcapacity of EVs on western shores, the last few years have dramatically changed the U.S.'s perspective on China and, what was once, its nascent auto industry. GM's image in China had waned and even Tesla was now playing second fiddle to BYD (Bring Your Dreams).

These realities were not lost on the attendees of the Chongqing Summit. While the intensifying U.S. and China relations were not palpable, it was obvious that the Chinese domestic auto industry seems resigned to largely side-step the U.S. market for the foreseeable future. There was a time, not so long ago, that representatives like myself were the stars of the program when it came to China outbound foreign direct investment and the U.S. market. In those days, our tool belts were full of opportunities for growth in the U.S. and Chinese suppliers, in particular, were interested in "The [North American] Show." Today, the U.S. market is seen as less stable, filled with minefields and enemies are at the gate. No longer is the U.S. seen as the bastion of prosperity and stability for Chinese automotive companies. Instead, the Chinese OEMs are focused on other places in the world, including Southeast Asia, Central Europe, Africa, South and Central America. And, suppliers remain wary of changing U.S. policies and the acrimony that typifies our political rhetoric towards China. The U.S. cadence towards protectionism, isolationism and growing nationalism has encouraged the once unfathomable decoupling agenda espoused by some. Times have changed so dramatically that the U.S.'s recent increase on tariffs (even tariffs of 100% on Chinese EVs) is only met with a wilted smile by the attendees at the Summit.

China's EV industry clearly intends to push on with its own transition and its outbound objectives, but rather than focusing on the U.S., it will do so in places where Chinese investments have already dramatically shifted geopolitics. The transition of the Chinese auto industry, particularly in terms of its "NEVs" (our BEVs) has been nothing but remarkable. Some might argue that this could only occur with substantial government subsidies, but insiders to the industry understand this transformation has been decades in the making. Whatever the reason, China doesn't intend to give up on EVs and for China it is not a political debate, as it is in the U.S. today.

This is not to say, however, that everything in the Chinese EV industry is sunshine and rainbows – it too is struggling with price wars, extreme competition, upstarts that won't survive, legacy brands that are slower to evolve, and yes, tariffs in the U.S. and now countervailing duties from the E.U. Nonetheless, it was clear that Chinese automotive leaders in attendance at the Chongqing Summit were focused on addressing these challenges and moving forward with newer and better technologies and new ways of doing business. The focus was on what the Chinese call, "long termism" – mutual cooperation that ensured the future success of the EV industry for Chinese brands. The specter of tariffs, for the leaders of the OEMs, seemed to only re-enforce the fact that the Chinese auto industry was on the right path towards beating its foreign competition. But, Chinese automakers are not doing this alone. In fact, I was surprised to see the number of discussions around joint venturing and business collaborations ongoing throughout all of East Asia. At times, it seemed the only empty chair was that not occupied by the U.S.

It remains to be seen how Beijing responds to the increase in tariffs, but respond it will, as it has in the past. It also remains to be seen if the Chinese EV makers can weather the storm of closing markets in the U.S. and, to a lesser extent, in the E.U., but if they can, it will certainly expand the gap between China's EV industry and the nascent EV industry in the U.S. When the NA auto industry has to plan around the fickle nature of politics and react to the increased cost of building

EVs with fewer options, it is not hard to see that there remains challenges ahead, even with the U.S. government's incentives and subsidies. And, to the extent the industry is counting on those incentives to push the transition along, do they have the staying power that can weather 2-year election cycles? I for one am anxious to see what the next five years will bring in the U.S.'s EV transition, and yes, if or how the Chinese auto industry may factor in.

Mark Heusel | Member Partner | Chair, East Asia Practice Group

Interview with Mark Heusel: Chair of Dickinson Wright's East Asia Practice

Question 1

Bob: Welcome back from Chongjing. Before we jump into your observations of the status of the China/U.S. relationship, tell us a little about your practice representing both U.S. and Asian companies in the automotive space and, in particular, regarding EVs.

Mark: Thanks Bob for the opportunity to talk on this dynamic and fluid topic. I've had the privilege of working with Asian companies investing in North America for over two decades and the landscape is continuously changing. In that time, while most of our work has been in and around automotive and manufacturing, the evolving geopolitical relationships over the last 8 years has made the work even more challenging and, yes, fascinating. Our East Asia Practice Group primarily serves companies from China, Japan, Korea and the ASEAN region as they plan and implement their foreign direct investment in North America. Because many of our clients are connected in some way to electric and autonomous vehicle technologies, we have been able to engage at a high level in advising our clients on a host of issues that are unique to foreign investors in this space.

Question 2

Bob: Can you share with us your observations regarding the perspectives of the Chinese OEMs regarding the increasingly adversarial and competitive environment with the U.S.?

Mark: First, despite the proposed aggressive increase in Tariffs on Chinese semiconductors, battery components and EVs and escalating rhetoric between Washington and Beijing, our Chinese clients and colleagues remain gracious hosts and interested in hearing about developments in the US automotive industry and exploring business opportunities in the States.

On my recent trip, however, I was struck by the significant change in how the Chinese viewed themselves vis-a-vis the U.S. In prior years, when U.S. OEMs still had a substantial foothold on Chinese consumers, I would characterize the Chinese view of the relationship as akin to big brother and little brother (哥哥和弟弟), with China acknowledging that the U.S. OEM's enjoyed an engineering and technological material advantage over the Chinese OEMs. The China industry's objective was to engage, learn and emulate.

Today, the atmosphere is very different. The Chinese OEMs consider themselves at par if not exceeding the U.S. in all aspects of the manufacturing process and in particular in advanced technology, including electrification and autonomous driving. In addition, the Chinese OEMs have connected with their domestic market in ways that have significantly chipped away at the U.S. OEMs presence in China, even that of Tesla. This relatively new found confidence, I believe, will inform the Chinese response to the implementation of increased tariffs, especially in the EV sector where they will focus on what they can control (stabilizing the domestic market through consolidation, continuous technological improvements and market growth in regions that are receptive to their products). I believe the Chinese OEMs understand that the U.S.'s recent tariff hikes are a protectionist move and validate their competitiveness.

Question 3

Bob: How do you see the Chinese responding?

Mark: My sense is that primarily they will focus on penetrating more accessible markets, at least in the interim and watch the U.S. political and business environment develop. Their product, high quality/low- cost EVs, are well suited to emerging markets in South and Central America, the Middle East, Southeast Asia, Central Europe and Africa. So I think they will focus on those markets and the Chinese domestic market for the interim and await developments in the U.S.

Another way they may react is to retaliate by limiting the provision of critical raw and processed materials to suppliers, which could have a catastrophic effect on the supply chain here in North America. It is too early to tell how this all will play out; but it has the potential to turn pretty ugly.

Question 4

Bob: In your view, do you see the imposition of materially increased tariffs as a sound U.S. strategy?

Mark: I think it may well achieve short term benefits for the U.S. OEMs, affording a breathing period for them to protect their U.S. market, while they attempt to close the technology and cost gap between the U.S. and Chinese, with respect to available and affordable vehicles. However, I believe the long term future of the industry is in the EV platform and autonomous driving. The Chinese are "all in" regarding both; while the U.S. and other non-Chinese manufacturers are more equivocal and, figuratively and literally, less invested and focused in developing the advanced technology and cost reduction to compete with the Chinese. China is currently in the lead and is prepared to do whatever is necessary to maintain and perhaps increase that lead. There is no clear path as to if and when the U.S. will close that gap when the availability to affordable and attractive EVs in the U.S. lags behind those produced by Chinese OEMs and we continue to delay in promoting a cohesive strategy for building out the necessary charging infrastructure to reduce consumer range anxiety.

Bob: Mark, thanks very much for sharing your insights with our readers regarding this very important and dynamic topic.

Mark Heusel *is an experienced commercial business attorney and serves as Chair of the Firm's East Asia Practice Group, (China, Taiwan, Japan, Korea, ASEAN Region). He has more than 25 years of experience in representing multi-national companies in a variety of industries, including automotive, retail, technology, industrial and manufacturing. Mr. Heusel's experience includes advising foreign companies in the areas of foreign direct investment in the United States, business formation, Greenfield investment, international trade, commercial transactional matters, and dispute resolution. In his role as International Practice Group Chair, he serves as general counsel to companies throughout East Asia and Europe, directing the Firm's resources to better assist his clients.*

In Case You Missed It

This issue of *In Case You Missed It* focuses on articles which provide additional and, in some cases, different perspectives regarding the public and private entity responses to addressing the threat of Chinese competition.

Forging Deeper Ties with China

The premise of the article appearing in the June 3rd edition of Bloomberg Hyperdrive is summed up by the author as follows: "The U.S. and Europe are throwing up roadblocks to keep Chinese cars out of their home markets. But at the corporate level, their growing ever closer." The author suggests that the U.S. and European OEMs adopt the old adage "if you can't beat them, join them" in an acknowledgment of China's technological and manufacturing expertise. He cites as an example, the joint venture between Stellantis and Zhejiang Leapmotor Technology. The author describes Leapmotor as "currently a minnow in China's crowded EV market;" however, it is rich in technology (e.g. driver assistance software, etc.) that can be useful to Stellantis, which will provide access to its extensive European dealer network to market Leap's low-cost EVs.

Although for now the joint venture is limited to Stellantis getting a cut from profits generated by sales of Leap's vehicles through Stellantis' network, the author suggests that, "... there's room for deeper collaboration down the road."

China Tech Turns American

Another way Chinese automotive companies are responding to U.S. government restrictions/tariffs is by setting up shop in the U.S. In an article appearing in the June 2nd edition of WSJ Technology, the author cites a number of examples of what she describes as Chinese companies "rebranding." She cites the example of Hesai, a Chinese lidar maker, setting up a U.S. based subsidiary named "American Lidar."

A Chinese Phone Maker Did Something Apple Couldn't: Make an EV

The authors recount the story of Xiaomi, a Chinese manufacturer of rice cookers, robot vacuums, air purifiers and smartphones that in less than 5 years was able to design, manufacture and bring to market a technologically advanced, low cost EV. Xiaomi is the world's third largest smartphone maker after Apple and Samsung. The authors explain that, "As the hardware has become simpler, the focus for what makes an appealing product has shifted decisively to software and features."

The authors describe a "new reality" in the automotive business, i.e., "The barriers to entry for making a car have shrunk in recent years with the emergence of electric vehicles" which has allowed the Chinese start-ups not only to enter the market; but to potentially dominate the market in the future.

The US Finally Has a Strategy to Compete With China. Will It Work?

The author of an article appearing in the May 20th edition of the *Wall Street* Journal provides a historical perspective and critique of what he describes as Biden's "three legged stool" strategy in dealing with Chinese EV competition, comprised of (1) on-shoring a viable technology manufacturing sector; (2) imposing increased tariffs on Chinese imports; and (3) restricting access to money, technology, and know-how that could help China compete. The author recounts the evolution of the US's strategy and its deficiencies.

Another Hidden Benefit of Renewables

Finally, although our focus this week is on China, I found a short article appearing in the June 4th edition of Bloomberg Zero very illuminating. Entitled, "Another Hidden Benefit of Renewables", it contains some surprising (at least to me) statistics regarding the inefficiencies of using fossil fuels. For example, the author notes that, "We waste about a third of the total energy produced on mining, refining and transporting fossil fuels." He further states that, "Another third of the world's energy is wasted in burning fossil fuels in highly inefficient machines. For example, a fossil fuel powered car converts only a quarter of the energy in gasoline into motion." He notes that in contrast, an electric car converts more than three quarters of energy in the battery to motion.

Robert Weiss | Of Counsel | Co-Chair, EV Initiative

To learn more about our EV practice, visit our website at https://www.dickinson-wright.com/practice-areas/electric-vehicles?tab=0.

All views presented in this newsletter are those of the authors and do not necessarily reflect the views of Dickinson Wright.

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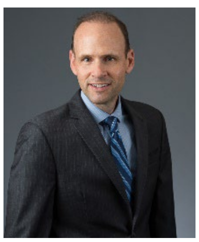

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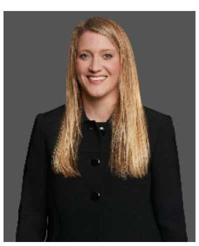

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