



The CCP's Tightening of Control over China's IT Sector

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Contrary to the Chinese Communist Party's (CCP) expectations that China will develop production of semiconductors, robots, and artificial intelligence (AI), the local IT sector has been most successful in creating social networking and trade-support platforms. The CCP is concerned about the growing political and economic influence of IT companies and their leaders, especially the potential of the data processed there. Consequently, it has adopted new regulations, started investigations of companies, and enacted repression of Chinese CEOs with the aim of subjugating the sector to the state.

Development of Chinese Technology Companies. China's technology sector remained mostly unregulated for a long time. In the 1990s, the government's role was limited to attracting capital through foreign direct investment and protecting local companies from foreign competition by erecting barriers to entry. At the local level, the government rewarded IT investment with various tax breaks and preferences, as well as free transfers of land for sector development. At that time, Chinese companies primarily copied successful foreign solutions that were either not available on the Chinese market or not adapted to it.

Permissive government policy and the potential of the domestic market, supported by foreign capital and management decisions, led to the dynamic development of Chinese technology companies. As a result, they began to develop original projects, including in new technologies, and entered foreign markets (e.g., in Africa), not giving way to the existing U.S.-based leaders. Successful examples are primarily companies focused on providing services, such as Alibaba (e-commerce), WeChat (messenger), Didi (ride-sharing). The value of China's technology sector exceeds \$4 trillion, which is still several times less than that of the U.S., and out of 160 "unicorns" (companies with capitalisation exceeding \$1 billion) almost half are involved in new technologies—robotics, AI, or processing large datasets. The key role in financing these companies is still played by foreign capital, which, as the scale of the Chinese companies' operations increases, is raised through initial public offerings (IPOs) on

stock exchanges, often in the U.S. Through IPOs, pre-market investors gain significant profits.

The Role of Big Tech. Chinese tech companies, thanks to their rapid development and the overall rise of technology in China, are exerting an increasingly strong influence on the economy, and their contribution to GDP continues to grow. At the same time, with the digitisation of more sectors of the economy, they have been taking dominant positions in new areas, such as payments. They also employ tens of millions of people and cooperate with hundreds of thousands of entities from various industries. Consequently, their actions have a significant impact on the functioning of the labour market and competition within the Chinese economy. Due to the lack of specific regulations in this industry (e.g., the rights of tech platform workers or the functioning of the digital market), IT companies use their strong position to force smaller competitors into exclusive cooperation or to sell their companies, while offering their own employees unfavourable working conditions (e.g., salaries below the official minimum wage per hour).

The consequence of foreign capital involvement is partial control over the companies' resources. For example, about a quarter of the shares of Alibaba or Tencent are controlled by foreign entities, including investors from the U.S., South Africa, and Japan. Through these ownership rights, these entities have influence over the operation of companies that are an increasingly important part of China's economy. Moreover, they have access to technologies that, in the face of growing

technological protectionism as a result of the Sino-American rivalry, poses a threat to national security according to the CCP. The technology developed by China's IT leaders is also seen as an important part of this rivalry. The Party, while providing generous funding to the industry, expects more development of quantum computing, AI, and semiconductors, rather than consumer solutions, even if more economically viable. Even more important, however, is these companies' access to vast datasets on Chinese citizens. Securing this data is one of China's key cybersecurity challenges. At the same time, the authorities seek to gain as broad and exclusive access to these data as possible by taking control of the companies (e.g., by putting CCP appointees on boards), as well as through the nationalisation of the collected data.

The model of management and financing of Chinese technology companies is based on the American tech sector. Some CEOs of Chinese companies such as Jack Ma (Alibaba) or Guo Guangchang (Fosun), enjoy celebrity status similar to that of top American executives. Their financial and political influence has grown steadily, like the companies they manage. They also in effect control the data on the behaviour or preferences of Chinese citizens. In addition to their increasingly frequent public appearances, these CEOs began to speak out on social issues, including indirectly criticising the government, despite their personal ties to the CCP. From the Party's perspective, contesting its monopoly on the flow of information or influence on public opinion is an existential threat.

Regulatory Offensive. The government's response to the CEOs' growing influence has been unequivocal. Since 2020, numerous companies have been investigated by industry regulators and others responsible for proper market functioning. CEOs have been summoned to interviews with officials to clarify their statements, after which they have changed their message, spoken less frequently, and some have withdrawn from public life altogether. Jack Ma has not been seen in public since November 2020.

The government has taken direct action against several hundred technology companies. The most high-profile so far were the numerous antitrust proceedings against two large conglomerates, Tencent and Alibaba. Alibaba was fined \$2.8 billion in April this year. In addition to antitrust actions, the government has blocked IPOs on U.S. exchanges (including Ant Group's planned late 2020 debut, which was to bring in

\$37 billion) and punished companies that have done so (Didi was forced to remove its app from stores after its debut). Investors have reacted to these actions by pulling funding—the capitalisation of Chinese technology companies on stock markets shrank by about 25% (\$1 trillion) by the last week of July.

The Chinese authorities have also prepared new data regulations that will come into force on 1 November. They specify the allowed purposes and how data may be collected and used, as well as the possibility of sharing data with foreign entities. Earlier this year, on 18 August, China's data regulator found that 43 apps, including one of the world's most popular, WeChat, were illegally using data and gave the companies responsible for it a week to make changes to how they process data.

Conclusions. The Chinese government's actions against the IT sector are part of a trend towards increased surveillance and control over society and the economy. At the same time, by acting against services companies, the government is taking a huge risk to try to redirect capital and human resources towards technologies it considers key for the future. The pace of development of these technologies is, however, not determined by the availability of financing, which so far is already hundreds of billions of dollars, but by the development gap and the time needed to catch up with the U.S. and EU.

As a consequence of the government's actions, China's largest technology companies will continue to suffer, which will significantly limit their opportunities for foreign expansion. The introduced regulations and restrictions on access to foreign capital will reduce their competitive advantage, which should positively influence the development of the technology sector in the U.S. and EU. As a result, the global attractiveness of the Chinese internet model will also decrease.

On the other hand, China's regulatory actions, in addressing similar problems to those in the EU and U.S., are much more radical; anti-monopoly proceedings are conducted effectively and quickly—in the Alibaba case, they took just four months. The government's attempt to break up monopolies, regulate standards for employees of social networking platforms, or nationalise data in the form of public digital infrastructure available to all companies could spur innovation and increase the competitiveness of the IT sector in China, as well as influence the way other countries regulate their markets.