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INVESTMENTS (PTY) LTD

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Why Is the US Worried About China?

China's rise from supplier to competitor is the reason Washington has spent eight years raising tariffs and, more recently, restricting the technology China can buy. The uncomfortable record is that each restriction has told China what to build next, and China has either built it or made it a strategic priority. This article looks at how China got here and where it still falls short. It also examines what the United States is doing about it and what all of this means for a globally diversified portfolio.

From trading partner to competitor

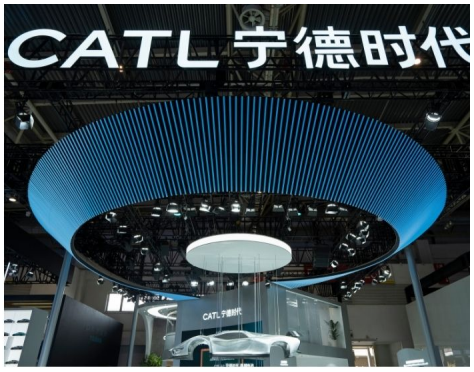
China's exports are increasingly sophisticated and compete directly with long-established Western consumer brands. For example, Xiaomi's latest mobile phone competes with Apple's recently launched iPhone. BYD's hybrid electric vehicles compete with incumbents like VW, BMW, Ford and Toyota. CATL is a Chinese company that manufactures the world's leading battery storage systems.



The new Xiaomi 17 Pro Max sounds and looks very familiar to a certain iPhone, but with a screen on the back.



The BYD Dynasty-D is the new flagship full-size SUV, competing with Range Rover, BMW X7 and Mercedes-Benz GLS.



CATL's supplies about 40% of world's electric vehicle batteries.

What makes China so hard to compete with

Five things stand out about China's progress, particularly over the past five years.

1. Scale

China is the world's largest manufacturer, producing close to a third of everything the world makes and its domestic economy is the single largest market for cars, phones and industrial machinery. A company that wins at home can operate at a scale that allows it to sell more, drive down its costs and then export at prices that other global companies struggle to match.

2. Innovation

Chinese applicants filed over 70 000 international patent applications in 2025, about 40% more than the United States. Huawei, a Chinese telecoms and technology company, has been the world's top corporate filer for nine straight years.

3. Speed

When ChangXin Memory Technologies (CXMT), China's leading memory-chip maker, needed a new factory, it built the clean rooms[1] in 12 months. That is half the industry norm for the most complicated part of the project and gets CXMT to the market faster.

4. A supportive state

China's government provides direct state support equivalent to about 1.7% of GDP, roughly four times the US figure on the same measure[2]. The money follows a plan. Each Five-Year Plan identifies the priority industries to be developed, and provinces, banks and state companies fall in behind it.

5. Control of raw materials

China makes around 90% of the rare-earth magnets used in electric motors and wind turbines. The original patents on these magnets were Japanese and expired some years ago, but Chinese producers have since patented the manufacturing processes for the high-performance grades that carmakers and turbine builders use. Holding both the production and the process know-how gives Beijing the ability to restrict exports when it chooses, and it has used that leverage in its trade negotiations with the United States.

Where China still lags, and why

China has come a long way in five years, but it does not yet dominate. In November 2025, a US congressional commission checked the 250 targets China set itself in its 2015 "Made in China 2025" plan[3]. About half were missed, mostly in high-precision tools and technology.

The pattern in the misses is useful because it shows that China copies quickly where a product can be reverse-engineered from the finished article or learned from a joint-venture partner, as happened with high-speed trains, solar panels and cars.

Where it struggles is when the know-how sits within protected intellectual property or resides with experienced engineers. For example, a jet engine or a precision machine tool can be taken apart, but the decades of test data that explain why each part is shaped the way it is cannot.

The US response: slow China down

Washington's strategy against China over most of the past decade has been to slow down China's technological advancement.

Export controls keep the most advanced chips and chipmaking equipment out of China. The enforcement side has sharpened as several Chinese nationals working at US companies like Google and Apple have been arrested or fled back to China for passing blueprints and research to Chinese institutions.

Tariffs raise the cost of Chinese goods entering the United States and limit access to the world's wealthiest market. The aim is to defend the top of the value chain while conceding the bottom. That explains the recent agreement on $60 billion of tariff relief, which lets more toys, car seats and Christmas decorations into the US.

Washington is asserting itself in the places that feed China's industrial machine with raw materials, from Venezuelan oil and Russian gas to Greenland's rare-earth deposits.

Each restriction became a target

When Nvidia's chips were cut off, a little-known Chinese AI research firm called DeepSeek released a model that matched the leading US systems at a fraction of the training cost. The announcement wiped close to $600 billion off Nvidia's market value in a single day.

Stanford University puts the cognitive knowledge gap between the best US and Chinese models at under 3%, according to its AI Index Leaderboard[4].

When the US restricted China's access to ASML's most advanced lithography machines[5], it highlighted another area in which China was dependent on foreign technology. Reuters later reported that a secret programme in Shenzhen developed a prototype alternative. The machine has yet to produce a commercial chip, but the episode illustrates how strategic dependencies often become priorities for Chinese industry.

What this means for investors

In 2026, the global economy would struggle to function without Chinese batteries, electric vehicles, phones and rare-earth magnets. In the future this is likely to extend to other industries and products, which are increasingly higher-tech products like robots.

There is pause for thought, though. Chinese industrial success and innovation do not always translate into shareholder returns. For most of the past decade, profit was downstream of strategic objectives, where capacity, employment and self-sufficiency took priority.

There is a Chinese term for it, *neijuan*, which is translated as involution[6]. BNP Paribas Asset Management refers to it as excessive and self-defeating competition among Chinese companies for limited resources and opportunities that pushes production up and drives prices down.

For example, in electric vehicles, solar panels and online retail, dozens of Chinese companies compete for the same customers and cut prices to win them, often below cost. Each company sells more but earns less profit on every sale. The trade figures show that since 2022, the volume of goods China exports has grown about twice as fast as the money it earns from them, because prices fell throughout. The companies became more efficient, but the saving went to the buyer, who is increasingly outside China, rather than staying with shareholders as profit.

We observe this in the financial performance results for BYD and Xiaomi, which have both struggled to sell everything their production lines make, and their profit margins and returns on equity have deteriorated against Western peers despite rising sales levels.

But Beijing has changed its view on involution. Share-price performance is now a KPI for state-run enterprises. It places pressure on companies to prioritise profitability over market share, raise dividend payout ratios and buy back shares, which now sits within the 15th Five-Year Plan[7].

The Chinese battery maker CATL is an example where fortunes are turning, where first-half 2026 saw improving profitability on increased sales and the board approved one of the largest share buybacks in history, plus an interim dividend. It's one of the most commonly held positions across funds in client portfolios.

Building a portfolio for the long term

The 10 largest Chinese companies make up about 1% of the global equity index[8] market value, compared to 24% for the US. How sustainable is this gap?

China has the characteristics of a growth market but trades on cheaper value multiples, which is why exposure varies so widely among the managers we allocate to. Our growth managers hold the largest positions, our value managers hold modest ones, and most of the quality managers hold nothing at all.

Global fund managers tend to have an attitude of *"if we don't need to go there, we won't".* There is an element of risk aversion here, different from that found in the tried-and-tested US market, where the interplay between companies, their customers and the government is well entrenched.

In China, these norms don't follow the US rulebook, but that may be where opportunity lies. If China can compete more broadly on innovation, while rewarding shareholders on commercial terms, then why wouldn't it be an attractive investment opportunity worthy of a larger portfolio allocation?

The average investor may be materially underweight direct China equity exposure, particularly if China successfully delivers on the objectives of its 15th Five-Year Plan.

Our role is to continually evaluate the investment case for markets like China and the managers who invest in them, weighing widespread manager reluctance against the skill of those who do commit capital. Combining these perspectives helps us build the optimal long-term equity portfolio.

[1] Memory chips (DRAM) are the working memory in computers and AI servers. Clean rooms are the sealed, filtered halls in which chips are made. They are the slowest and most expensive part of a chip factory to build.

[2] Centre for Strategic and International Studies (CSIS), Red Ink: Estimating Chinese Industrial Policy Spending in Comparative Perspective, May 2022. The estimate is for 2019

[3] The US-China Economic and Security Review Commission is an independent body that reports to Congress. Its assessment, Made in China 2025: Evaluating China's Performance, was published in November 2025. The plan, launched in 2015, set targets across ten strategic industries to be met by 2025.

[4] Stanford University's AI Index Report 2026. LMArena is a public leaderboard that ranks AI models through blind, head-to-head comparisons voted on by users.

[5] Lithography machines print circuit patterns onto silicon wafers. The most advanced generation uses extreme-ultraviolet (EUV) light. It is made only by ASML of the Netherlands, costs roughly $250 million per machine and has never been licensed for sale to China.

[6] BNP Paribas Asset Management: China: Involution, Deflation and Structural Reform.

[7] China's Five-Year Plans set national industrial priorities and funding for the following five years. The 15th plan, covering 2026 to 2030, was published in March 2026.

[8] The global equity index referred to is the MSCI All Country World Index (ACWI). It tracks large and mid-sized listed companies across developed and emerging markets and is the most common benchmark for global equity funds.

Market Report

30 September 2026

Market Performance (as a %)

Local Market Indices	CCY	3m	YTD	1yr	Ann. 3yr	Ann. 5yr	Ann. 10yr	5yr Vol	10yr Vol
SA Equity	ZAR	-0.4	-3.7	4.0	17.8	14.5	10.6	14.2	14.7
SA Listed Property	ZAR	-1.4	2.7	19.2	25.7	15.1	4.0	16.4	21.7
SA Bonds	ZAR	-0.8	3.2	12.3	17.1	11.6	9.7	7.9	7.9
SA Cash	ZAR	1.7	5.1	7.0	7.8	7.1	6.8	0.4	0.4
Balanced Benchmark	ZAR	-0.2	0.2	6.2	15.8	12.6	10.1	9.4	10.0
SA Inflation (1 month lag)	ZAR	1.1	4.4	4.6	4.1	4.9	4.7	1.5	1.6
Global Market Indices		**3m**	**YTD**	**1yr**	**Ann. 3yr**	**Ann. 5yr**	**Ann. 10yr**	**5yr Vol**	**10yr Vol**
Global Equity	USD	1.9	11.2	15.3	21.5	12.0	12.9	15.0	14.9
Emerging Markets Equity	USD	-0.3	23.7	29.4	24.5	8.9	8.8	18.5	17.6
Global Property	USD	-6.1	2.3	2.1	9.4	0.5	2.5	18.0	17.2
Global Bonds	USD	-2.5	-2.7	-2.5	3.7	-1.9	0.0	7.8	6.4
US Cash	USD	0.9	2.8	3.9	4.6	3.8	2.5	0.5	0.5
Major Indices Based to ZAR		**3m**	**YTD**	**1yr**	**Ann. 3yr**	**Ann. 5yr**	**Ann. 10yr**	**5yr Vol**	**10yr Vol**
SA Equity	ZAR	-0.4	-3.7	4.0	17.8	14.5	10.6	14.2	14.7
Global Equity	ZAR	1.9	9.8	9.6	16.0	14.0	15.0	14.1	14.6
Emerging Markets Equity	ZAR	-0.3	22.4	23.0	18.4	10.7	10.8	13.8	13.7
Global Property	ZAR	-6.1	1.0	-2.9	4.5	2.3	4.3	16.5	16.6
SA Bonds	ZAR	-0.8	3.2	12.3	17.1	11.6	9.7	7.9	7.9
Global Bonds	ZAR	-2.4	-3.8	-7.3	-0.9	-0.2	1.8	10.1	12.7
Commodities		**3m**	**YTD**	**1yr**	**Ann. 3yr**	**Ann. 5yr**	**Ann. 10yr**	**5yr Vol**	**10yr Vol**
Gold (US Dollars)	USD	3.7	-3.1	9.0	30.5	19.0	12.0	17.9	15.9
Gold (Rands)	ZAR	3.7	-4.2	3.6	24.6	21.0	14.0	16.4	17.5
Currencies		**3m**	**YTD**	**1yr**	**Ann. 3yr**	**Ann. 5yr**	**Ann. 10yr**	**5yr Vol**	**10yr Vol**
Rand / Dollar	ZAR	-0.2	0.9	4.9	4.6	-1.7	-1.8	11.7	13.6
Rand / GBP Pound	ZAR	-0.2	2.3	6.2	1.9	-1.4	-2.0	9.8	12.6
Rand / Euro	ZAR	0.5	4.2	8.3	2.4	-1.3	-1.9	9.3	11.8

Market index performance is based on publicly available returns from ETFs that track the relevant underlying indices.

Disclaimer: Users should be aware that short-term performance can be volatile and that past performance is not necessarily a good guide to future performance. The information in this report is for general guidance and does not constitute an offer or solicitation to purchase, sell or otherwise deal with any particular investment. This report is for the use of Fundhouse and its clients only and may not be published externally without permission first being obtained from Fundhouse. While great care and diligence has been taken in the compilation of the report with data provided by FE Analytics, no representation or warranty, express or implied, is or will be given by Fundhouse or its directors, partners, employees or advisers or any other person to the accuracy or the completeness of the information in the report or relating thereto. Fundhouse will not accept any liability for losses suffered as a result of inaccuracies.
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Spot Rates		30-Sep-26	Latest Quarter	1 Year Ago	5 Years Ago	10 Years Ago	20 Years Ago
Currencies							
Rand/US$	ZAR	16.4	16.4	17.3	15.0	13.8	7.8
Rand/GBP	ZAR	21.8	21.8	23.2	20.3	17.9	14.5
Rand/EUR	ZAR	18.6	18.6	20.3	17.4	15.5	9.8
Rates							
6m USD Cash	USD	3.9	3.9	4.4	0.0	1.3	5.1
Repo Rate	ZAR	7.3	7.3	7.0	3.5	7.0	8.0
Prime	ZAR	10.8	10.8	10.5	7.0	10.5	11.5
All Bond Index Yield	ZAR	8.8	8.8	11.6	11.6	9.1	9.7
Commodities							
Gold ($/oz)	USD	4 164.0	4 164.0	3 833.9	1 761.0	1 321.5	596.4
Platinum	USD	1 714.1	1 714.1	1 571.0	963.0	1 034.0	1 140.0
Oil (Brent Crude) $	USD	103.6	103.6	67.1	78.6	49.0	59.9
Inflation							
SA Inflation	%	4.4	4.4	3.4	4.9	6.0	9.4

data provided by FE Analytics

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Fundhouse was founded in 2007 by professionals from the investment management industry. We currently operate from offices in the United Kingdom and South Africa, where we cover the local and global fund industry first hand. Our business is 100% independent and owner managed which means we can offer objective advice and services in the best interests of our clients.

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