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Strategic Decoupling: How Great Power Competition Reshapes Domestic Economic Policy in the United States and China

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Abstract

The U.S.-China relationship has evolved significantly since it was primarily an economic relationship to one of economic integration and a relationship of strategic competition. Therefore, I have created a term called strategic decoupling. This study explores why the U.S. and China have taken different approaches toward domestic economic development policy when both countries are facing very similar types of geopolitical pressure. Using the theoretical frameworks of historical institutionalism, varieties of capitalism (VOC) and constructivist international relations, this research introduces a geopolitical filtering framework that explains how existing institutions provide a basis upon which countries develop their responses to external threats. The core idea of this research is that states react to great-power competitions using institutionally dependent paths: the U.S. uses regulatory tools such as export controls, investment screening, and targeted subsidies based on its fragmented, legally mediated-governance structure; whereas China uses state-driven tools such as central planning directives, State-Owned Enterprise (SOE) mandates, and Policy Bank lending driven by its hierarchical Party-State structure. The author compares the U.S.'s policy approach toward strategic decoupling via several key pieces of legislation including the CHIPS and Science Act, TikTok divestiture legislation and the Inflation Reduction Act to compare them to China's strategy for creating a parallel economy, including the Dual-Circulation framework, the National Integrated Circuit Industry Investment Fund, and indigenous innovation initiatives. The results show how these institutionally dependent paths produce two separate decoupling pathways despite having common security goals. Finally, the author concludes that strategic decoupling will create two parallel technology ecosystems, alter global supply chains and undermine the rules-based international order, leading to significant implications for the nature of twenty-first-century global governance.

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1. Introduction

The U.S.-China relationship has shifted dramatically from an economically based interaction to one of strategically based engagement. Therefore, this has resulted in a major restructuring of the global political economy. For decades, it was assumed by both policymakers and scholars alike that increasing levels of economic interdependence would lead to increased levels of political convergence and therefore greater cooperation. Liberal Internationalism, which is a central tenet of liberal internationalist foreign policymaking, is built on the assumption that increasing economic interdependence will lead to growing levels of political integration and cooperation. Thus, the U.S. government has pursued a variety of engagement-based policies since President Nixon visited Beijing in 1972. However, there have been significant changes over the past few years that reflect a dramatic shift towards the de-coupling of the two countries' economies. According to Farrell and Newman (2023), Roberts et al. (2019), and Weiss (2019), Strategic Decoupling refers to a deliberate attempt to reduce dependence in key areas including Semiconductors, Artificial Intelligence, Advanced Manufacturing and Emerging Technologies. The purpose of strategic decoupling is to limit exposure and increase national security. The beginning of these changes can be seen in the 2018 tariffs placed by President Donald Trump on Chinese goods - which were imposed unilaterally by the U.S. with no prior approval from the World Trade Organization (WTO) using Section 301 of the Trade Act of 1974 and Section 232 of the Trade Expansion Act. However, it is at this point that the U.S. abandoned many of its post-World War II multilateral trade standards.

The U.S. and China have adopted vastly different domestic economic policies to counteract the pressures created by intensifying global competition. The U.S. has relied upon an array of regulatory tools for its responses to increasing Chinese competitiveness, such as export control measures, foreign direct investment screening, and narrowly targeted industrial subsidy programs like the CHIPS and Science Act. These tools create incentives for private investment into specified sectors while simultaneously limiting the ability of those entities to cooperate with their Chinese counterparts (Evenett & Fritz, 2024; Miller, 2022); Conversely, China's response has been to expand state-led industrial development efforts through the dual circulation strategy, mandatory domestic procurement requirements, and large-scale government backed investments into the semiconductor and electric vehicles industries (Kennedy, 2025; Naughton, 2021). This difference provides a significant puzzle for this research paper: Why do similar geopolitical challenges lead to different domestic economic development structures in both countries?

The main thesis of this paper is that states use policy tools to address international pressures based upon their pre-existing economic governing institutions - they are institutionally path-dependent. As such, states will pursue different approaches to decouple from an increasingly competitive world economy, despite having similar goals for national competitiveness. Regulatory capitalism, which is exemplified by the U.S. model of governance, utilizes both market-oriented incentives and a myriad of legal mechanisms to restrict competition, all within a framework of decentralized, or at least fragmented institutional arrangements. State-led capitalism, which is used by China, represents a system of governance in which the government controls the economy and industry through a top-down approach. This includes industrial directives provided in medium - to long-term development plans, as well as

party/state-coordinated decision-making processes. These differences explain why the U.S. has pursued decoupling primarily through targeted sanctions and subsidies, while China's decoupling efforts have taken the form of comprehensive restructuring of its industries.

Methodology

This research utilizes a qualitative comparative case study model to compare how the U.S. and China have developed different forms of domestic economic policy in reaction to competing interests of being a global superpower. A comparative case study model is an ideal method of study for this research question because it provides a detailed exploration of the causal mechanisms which link geo-political pressure to the outcome of the policy, while also controlling for structural differences that exist between the two political systems (George & Bennett, 2005; Yin, 2018). The research design compares two primary cases: the U.S. and China. These are the two countries which represent the largest actors in the current process of strategic decoupling. Each country was studied through multiple policy episodes within each nation. For example, in the U.S., these policy episodes include the enactment of the CHIPS and Science Act (2022), the enactment of laws requiring TikTok to sell its assets in the U.S. (2024), the enactment of the Inflation Reduction Act (2022) and several export control regimes to restrict the ability of Huawei and semiconductor companies from exporting certain technologies. On the other hand, in China, these policy episodes were enacted under the dual circulation strategy (2020), the creation of a national integrated circuit industry investment fund and a portion of the "Made in China 2025" initiative. By studying multiple policy episodes in both nations, researchers can identify whether there are common patterns of institutional behavior which occur due to path dependent characteristics within institutions, while controlling for potential differences that may be present when comparing across cases.

The main tool used to analyze this project will be a qualitative content analysis of official documents as well as policy reports. Qualitative content analysis is the best methodology for analyzing how governments communicate their strategic objectives, provide justification for intervening in markets with policy tools, and portray competitive threats because all of these issues are fundamentally discourse-based and therefore need an interpreter to make sense of them using textual data (Neuendorf, 2018; Krippendorff & So, 2019). The document corpus for this study has four categories of primary source documents: (a) Policy documents from the U.S. government which include the CHIPS and Science Act, Inflation Reduction Act, executive orders pertaining to supply chain disruption, and Bureau of Industry and Security export control regulations; (b) Chinese policy documents that include: (i) The Five Year Plans (13th, 14th, and 15th); (ii) Central Committee Resolutions; and (iii) White Papers on Industrial Policy; (c) Congressional hearings, parliament session records/officials' statements, and other public statements from top officials in both China and the U.S.; and (d) International trade and technology treaties governing this relationship. Data collection covered the period from 2015 to 2026, allowing for an examination of the evolution of strategic decoupling. Analytically, I use a systematic review process to interpret these documents to find commonalities in how policymakers select policy instruments (administrative vs. regulatory mechanism) and the timing of those selections (short term electoral cycles vs. longer term planning horizons) while also finding commonalities in how institutions within each country constrain or facilitate policymaking (veto points vs. hierarchical decision-making processes). By comparing my

interpretations of similar policy issues across countries, as well as conducting close readings of the textual evidence presented in each set of documents, I trace how existing institutional structures in each country filter exogenous geopolitical pressures into divergent but coherent decoupling paths.

2. The Theoretical Framework: Institutional Path Dependency and Geopolitical Filtering

2.1. Historical Institutionalism and Path Dependency

Historical Institutionalism is the theoretical basis of this study. It focuses on the way in which institutional legacy can guide a country's response to external pressures by producing path dependency; it constrains some responses and enables others. According to James Mahoney and Kathleen Thelen (2009), Institutions do not stand still. They evolve over time, either gradually or dramatically, through one of three processes: layering, conversion, or drift (Menz, 2017). Orfeo Fioretos et al. (2016) extend this perspective to demonstrate how institutional configuration acts as an intermediary to filter external pressures and generate resultant policies. This filtering activity accounts for why similar geopolitical events may result in different national responses.

The use of path dependency helps us understand why there has been an American and Chinese divergence. Path dependence is "the propensity of institutions to replicate themselves" (Mahoney & Thelen, 2009) as individuals make their choices in light of the institutional framework within which they exist, limiting their options going forward. The cost of making fundamental changes to the way a government operates, whether it be under a regulatory capitalist model or a state-led capitalist model, will increase exponentially. Individuals, organizations and governments all begin to create expertise, expectations and interests as part of the existing framework. As such, when states are confronted with external pressures, states utilize the policy tools that currently exist instead of developing new ones (Edmond, 2026).

2.2 Varieties of Capitalism and State-Led Models

The literature of varieties of capitalism, notably the foundational work of Hall and Soskice (2001) distinguishes between liberal market economics (LMEs) and coordinated market economics (CMEs) with respect to how companies are able to coordinate their activities (Hall & Soskice, 2001, pp. 8–12). LMEs, like the U.S. and UK, utilize competitive markets, formal contracting mechanisms and pricing systems to co-ordinate economic activity. On the other hand, CMEs, like Germany and Japan, use mechanisms outside of the marketplace (non-market), strategic interactions and institutionalized cooperative arrangements among firms, banks and labor to co-ordinate economic activity (Menz, 2017).

However, this theoretical model is not intended to examine the nature of state-led capitalism of the Chinese type. A recent extension of the varieties of capitalism research by Schwartz and Blyth (2022) extend the theory to include state led capitalism, suggesting institutional structures influence both firm behavior as well as state capacity for industrial interventions ((Schwartz & Blyth, 2022, 2022). In terms of its resource allocation, investment direction mechanisms, China exhibits a unique type of capitalism; specifically, party/state coordination replaces marketplace-coordination as the predominant method for directing

investments and allocating resources. Subsequently, Hall (2024) has advocated extending the varieties of capitalism framework to account for the growth of state capitalism including in developing nations economies where there is an increased level of direct state involvement in industry government regulatory frameworks (Hall, 2024).

2.3 Constructivist International Relations and Threat Construction

Constructivism in International Relations shows us how individuals within nations build on their understanding of threats to other nations and explain why those nations should respond to the threats based upon common knowledge or stories. Ian Hurd writes that "legitimacy in international relations is not simply a matter of legal formality; it is a social construct which emerges from states' common expectations and practices" (Hurd, 1999), therefore when one nation identifies another nation as a threat, then the identification is likely to influence the public's perception of the nature of the threat and thus what responses are considered legitimate.

The Trump Administration's approach to China as a strategic competitor versus a trading partner was fundamentally a constructivist paradigmatic change in how U.S. policymakers perceived the U.S.- China relationship. To understand the rapid acceleration of decoupling post - 2017, it is imperative to recognize the importance of this constructivist element in understanding what precipitated such action. Top officials in the Trump Administration engaged in constructing this new way of thinking about the U.S.-China relationship through various public forums including media, speeches and policy documents.

White House Chief Strategist Steve Bannon offered a coherent nationalistic view of economics that stated globalization had provided wealth to Chinese state capitalism at the expense of working-class Americans. During his tenure as White House Chief Strategist, Bannon repeatedly referred to China as the "single greatest existential threat" to American prosperity stating that America has been "asleep at the switch" while China employed unfair trade practices to create an advantageous position. White House Director of the National Trade Council Peter Navarro wrote books titled "Death by China" and "Crouching Tiger: What China's Militarism Means for the World," where he characterized economic competition as an existential battle. Navarro and Autry (2011) defined China's trade practices as "economic warfare" against the United States and therefore required aggressive measures to be taken.

Stephen Miller, Senior Advisor for Policy who helped to create and implement many aspects of Trump's immigration and trade policies has played a role in furthering the administration's "anti-establishment" message concerning engagement with China. Miller has continually portrayed the administration's views about U.S. trade deficits and technology transfers as evidence of America's weakness and how it has been taken advantage of through Chinese State Capitalism. Although less involved in direct policy issues than his fellow advisors, Cory Lewandowski also continued the administration's anti-establishment messaging concerning prior administrations being too passive when dealing with China. As a group these advisors created an image of China not as a partner, but as an enemy; they developed a view that American economic openness has been taken advantage of by China, not shared or reciprocated.

2.4 The Geopolitical Filtering Framework

This paper builds upon what I call the geopolitical filter, which combines findings from historical institutionalism, varieties of capitalism as well as constructivist theory for understanding why different countries have had such dramatically different decoupling outcomes. The model outlines three mechanisms through which competition among states translates into various policy results at the national level.

Firstly, state capability configurations determine how much a nation can influence its private sector via government intervention. In the U.S., this has been done historically using regulators, laws and other forms of market incentive; therefore, it is part of a constitutionally based governmental system that distributes power among many entities and levels of government. According to Oona Hathaway (2008), the U.S. has "delegated authority to independent agencies" thus creating both expertise as well as disunity or lack of centralization in governance. Chinese leaders, on the other hand, rely heavily on state owned enterprises for direct coordination to drive economic growth and development under a single form of governance structure (unitary); wherein the communist party has complete hierarchical control of all economic decisions (Naughton, 2021).

Secondly, it is how business-government coalitions are structured that determine which pathway(s) of policy implementation are selected. In the U.S., because industrial policy has to be implemented through an interplay between the Congress, private firms and the national security agencies, there will be many more political obstacles to overcome before any decisions can be made. For instance, Miller (2022) explains that the CHIPS and Science Act was developed as a result of a long and complicated legislative process in which members of both parties negotiated and lobbied various industry groups, while at the same time coordinating their efforts across multiple federal agencies. By contrast, China's hierarchical system of government allows for the development of its policy initiatives quickly through a direct coordination between the State and strategic sectors of the economy. Furthermore, because all provinces in China are vying for status under the central government in Beijing, each province will do everything possible to meet those national goals and targets established by the central leadership (Kennedy, 2025).

Thirdly, the structure and functionality of the legal and administrative systems within a country determine how policy implementations are executed. Specifically, the U.S. relies upon regulatory enforcement based on rules regarding foreign technology transfers to implement its industrial policy. These include listing of products subject to export controls by the Bureau of Industry and Security, review of investments into U.S. companies by CFIUS, and investigation of complaints filed against unfair trading practices by foreign countries or entities by the ITC (Farrell & Newman, 2019). On the other hand, China uses strategic planning and industrial direction contained within its Five-Year Plans to execute its industrial policy. In order to carry out this planning, China coordinates its activities through its state-owned enterprises, policy banks, and provincial industrial policies (Naughton, 2021).

3. The United States: Regulatory Decoupling Through Institutional Fragmentation

3.1 The Trump Administration's Paradigm Shift and Unilateral Imposition of Tariffs

The Trump Administration's position toward China was an unprecedented departure from prior U.S. administrations' positions toward China. The Obama Administration's Pivot to Asia sought to build on existing relationships by promoting regional economic cooperation through the Transpacific Partnership while maintaining defense commitments. In contrast, President Donald Trump abandoned this strategy altogether. He withdrew the United States from the TPP, initiated a trade war against China imposing tariffs on over $380 Billion worth of Chinese imports (York & Durante, 2025). The Trump administration's new approach to China reflected a fundamental change in how American elites perceived China as well no longer just a partner in the management of the world economy but a competitor for hegemony challenging America's position at the top of the international hierarchy.

President Trump's primary contention that the United States has been "taken advantage of" in terms of its trade with China reflects a broader perception that China took full advantage of the United States' open policy environment while protecting itself domestically. Many Americans who have experienced job loss due to globalization are likely to believe that their job losses can be attributed to Chinese companies competing with them in the domestic market; many Americans do not see globalization as leading to increased efficiency or productivity in domestic industries. As such, the perception of being taken advantage of support unilaterally taking aggressive action without Congressional approval, including tariffs implemented under Section 301 of the Trade Act of 1974 and Section 232 of the Trade Expansion Act (Williams & Hammond, 2020).

The United States' trade war with China was an open question in terms of the application of international law. According to Zirpoli et al. (2025), both of the U.S. imposed tariffs under Section 301 and Section 232 were likely violations of the General Agreement on Tariffs and Trade (GATT) and the WTO Dispute Settlement Understanding (Zirpoli et al., 2025). Article I of the GATT established a "most favored nation" rule whereby trade benefits given to one country are extended to all countries. Likewise, Article XXIII provides for the resolution of disputes regarding the violation of treaty obligations using the WTO dispute settlement process as opposed to unilateral actions. The Trump Administration violated this process when it unilaterally applied tariffs based upon its own determinations rather than utilizing the WTO approval process; accordingly, the Chinese government claimed these tariffs violated international trade law (Zirpoli et al., 2025).

3.2 Banning Huawei: The Foreign-Produced Direct Product Rule (FDPR)

The U.S. government's actions against Huawei during the Trump Administration were an example of how regulatory action is part of America's efforts at decoupling. On May 15th, 2019, the Bureau of Industry and Security (BIS), placed Huawei Technologies Co., Ltd. and 114 non-U.S. affiliated entities on the Entity List. BIS alleged that Huawei had engaged in activities contrary to the U.S. national security or foreign policy interest. As such, any United

States-based firm wishing to export technology to Huawei would need to receive permission first.

After Huawei developed their own semiconductor products with the help of U.S.-originated technology and software through their internal production division called HiSilicon, the BIS took additional steps. On May 15th, 2020, the BIS expanded upon their prior foreign-produced direct product rule. With this expansion, it prohibited the sale of any foreign-made goods that were directly manufactured with U.S. originated technology or software if they were being sold to Huawei or its affiliated firms. Specifically, the rule was designed to target any semiconductor design created for Huawei using U.S. software, as well as any chips produced from those designs using U.S. manufacturing equipment.

The regulatory approach of decoupling represents a significant aspect of U.S. institutional path dependence. Instead of choosing to nationalize technology companies or create state owned competitors to Chinese companies the United States has chosen to utilize the existing legal and administrative framework; this includes Export Controls administered by BIS; Investment Screening through CFIUS; Executive Orders issued under the authority of the International Emergency Economic Powers Act (Rokneddini, 2025). In addition to these mechanisms operating within the realm of law and regulations, they do so without utilizing the same tools as state ownership or central planning.

3.3 The TikTok Campaign: Divestiture Through Legislation

The Trump administration's campaign against TikTok, the social media owned by China, provided an additional method for regulatory decoupling using legislative mechanisms; specifically, requiring the sale of a company's assets and associated data required to operate in the U.S. under threat of being prohibited from operating in the United States. On August 6th, 2020, President Trump issued Executive Order 13942 under IEEPA to restrict TikTok from conducting business in the U.S. and demanded that ByteDance, TikTok's parent company, sell all assets and data related to the use of TikTok within the U.S. (Congressional Research Service, 2025, para. 1-3). These actions taken by the president were contested in court, and a preliminary injunction was entered prior to the effective date of the executive action.

On April 18th, 2024, Congress passed PAFACAA – Protecting Americans from Foreign Adversary-Controlled Applications Act, which explicitly stated that TikTok is a "foreign-adversary controlled application" (Congressional Research Service, 2025). PAFACAA prohibits app store providers and Internet hosting service providers from distributing, maintaining or updating "covered applications," unless their owners execute a qualified divestiture agreement that prevents the foreign adversary from controlling and/or having an operational relationship with the application.

The Supreme Court decision, as stated above, was a challenge to PAFACAA by TikTok/ByteDance regarding violations of First Amendment rights of Editorial Discretion and users sharing their own Speech. On January 17, 2025, the U.S. Supreme Court upheld the D.C. Circuit's ruling, finding no violation of the First Amendment. The court determined that PAFACAA was "content-neutral", meaning that there is no mention of limiting or regulating speech based upon Content, Function or Purpose. The court also concluded that the content-

neutrality was justified due to protecting the nation's security and foreign policy interests by preventing China from gathering large quantities of very sensitive data. The court provided great differences to the government's decisions regarding national security and foreign policy issues when evaluating whether PAFACAA complied with the First Amendment. Therefore, the court applied Intermediate Scrutiny as opposed to Strict Scrutiny.

The Supreme Court case cited above illustrates how American Decoupling can be regulated through the legislative branch and judicial review; however, this regulatory approach has significant time constraints. It is clear that the regulatory path to achieve decoupling objectives takes considerably longer in America compared to more centralized systems.

3.4 The CHIPS and Science Act: Regulatory Industrial Policy

Beginning with the signing of the CHIPS and Science Act into law in August of 2022, this represents the first time since decades that an industrial policy has been developed by the U.S. Government. The CHIPS and Science Act allocate $52.7 billion dollars in subsidies and tax credits to encourage domestic semiconductor manufacturing. Of this total amount of money allocated, $39 billion dollars will be provided as incentives to fund manufacturing activities while $13 billion dollars will be used to provide research and development funding (Grimes & Du, 2024; Vyas, 2025). Additionally, the act provides for a 25% investment tax credit for equipment and facility construction related to semiconductor manufacturing.

The CHIPS Act is quintessentially American in its design. Rather than using direct state ownership, the act utilizes grant financing, loan guarantees, and tax incentives to realize its goals (Miller, 2022). The Department of Commerce houses the CHIPS for America program. The department facilitates administration of the incentives to applicants through a competitive application process. Applicants are evaluated on a number of criteria, including commercial viability, financial capacity, technical feasibility, workforce development capabilities, and their ability to contribute to national security and economic goals (U.S. Department of Commerce, 2023). As such, the CHIPS Act's use of government funding and evaluation processes rely on private sector initiative and competition in order to facilitate achievement of the goals set forth in the act.

While this law was enacted to support US-based semiconductor companies, it included many “guardrails” – significant restrictions on how these companies use their funding. Any company that receives funding of $150 million dollars or more will be required to give the U.S. Treasury Department a percentage of all projected cash flow generated beyond what they were originally forecasted to receive. Companies cannot use funding provided through the CHIPS Act to purchase back their own shares. Of much greater significance, the law prohibits the recipient companies from entering into any "significant transaction" which could lead to an increase in "the material expansion of semiconductor manufacturing" in China or any other "country of concern" for a period of ten years following receipt of funding.

Implementation of the CHIPS Act has been further hampered by partisanship in Washington D.C. House members of the Republican Party continue to advocate for cutting funding for the CHIPS Act, while Congressional oversight committees continue to review whether the CHIPS Act's requirements are being fulfilled. As a result, the fragmented nature of

authority within the United States means that U.S. industrial policy will always remain subject to revision, reduction or redirection by each new Congress. This creates uncertainty for long-term planning and investment decisions.

3.5 The Inflation Reduction Act and EV Supply Chain Restructuring

Although the Act establishes guardrails on the use of the provided funding that represent an additional level of security in terms of how federal monetary policies are established. Any organization that receives more than $150 million in direct funding under this Act will be required to share a percentage of their profits above projected profit levels with the U.S. Government and may not use funding for stock repurchases (Vyas, 2025). Additionally, the Act prohibits organizations from entering into "any material transaction" intended to expand the production of semiconductors in China or any foreign country designated as a country of concern for a period of ten years following receipt of funding (Grimes & Du, 2024).

Due to its bipartisan nature, the process for implementing the CHIPS Act has been complex. Congressional Republicans in the House of Representatives have consistently attempted to limit appropriations for the Act, while Congress continues to conduct oversight related to compliance with the Act's provisions (U.S. House of Representatives, 2025). Due to the division among different branches of government and the fact that there is no single governing body for industry-wide policy initiatives within the United States, it is unlikely that any type of industry wide policy will ever be completely finalized. Each new Congress can review existing appropriations for the Act and either eliminate them entirely or adjust their distribution to other programs thereby limiting organizations' ability to develop comprehensive plans over time.

While, the IRA has potential for limiting its impact due to global supply chain dynamics. As it stands today, China controls nearly all key aspects of critical minerals processing, as well as most battery components and electric vehicle assembly. Mandating that U.S. based automotive companies abandon Chinese supply chains would be extremely costly. In addition, many suppliers have developed workarounds which allow them to modify their operations in such a way as to continue to meet the requirements of FEOC while still retaining an operational relationship with their Chinese counterparts (Evenett & Fritz, 2024). The IRAs regulations are also limited to the United States marketplace.

3.6 The "One Big Beautiful Bill Act"

The "Big Beautiful Bill 2025" can be seen as one piece of a larger trend of "strategic decoupling," where growing competition for influence, especially among the U.S. and China, leads to changes in national economic policies to emphasize security, resiliency and technological independence and thus sovereignty over mere market efficiency. Such bills include large scale industrial spending, incentives for supply chains and protectionist mechanisms all represent a move towards what I will refer to as "geoeconomic statecraft," where domestic economic policies become instruments of competition for influence internationally rather than based upon economic interdependence. Instead of depending on extensive interdependence economically, decision makers are acting to limit vulnerabilities within key areas such as semiconductors, energy, and high-tech manufacturing. This reflects

the above-mentioned "decoupling" logic that attempts to isolate national economies from competing nations while at the same time increasing their capacity domestically. Therefore, the Big Beautiful Bill represents how internal economic management is becoming more influenced by external security issues and creates a vicious cycle where increased international conflict accelerates the economic disconnection of countries and increases domestic intervention.

3.7 Why Public Responses Are Slow and Partisan Backlash Persists

The U.S. response to Chinese competitive pressures has been to implement policies at a slow pace with considerable back-and-forth due to partisanship. There are two primary reasons for this type of response. Institutional fragmentation is one reason. Institutional fragmentation gives multiple entities (such as Congress, the Executive Branch, Independent Agencies, and the Courts) separate levels of authority and ability to either slow down, stop, or modify what other entities do. For example, it took 4 years for the divestiture of TikTok to go from an executive order to be enacted into law and receive approval from the U.S. Supreme Court (Congressional Research Service, 2025).

Additionally, party line division prevents industrial policy from being completely codified. Both parties believe there needs to be some form of policy to counter China's competitive advantage, however they fundamentally differ in how to accomplish this. Republicans tend to advocate for tariffs and strict export restrictions while Democrats prefer subsidy programs for industries and working cooperatively internationally. Although the CHIPS Act was passed by both sides of the aisle, its execution has also been hampered by Republican members attempting to reduce funding. The potential exists for this type of partisanship to create uncertainty that may impede long term planning.

Thirdly, the U.S. regulatory system uses legal means which allow for delays as well as lawsuits. Both Huawei and TikTok have taken their designations to the "Entity List" and “divestiture orders”, respectively. In 2025, the Federal Court overturned the tariffs based on IEEPA (Williams & Hammond, 2020). Legal challenges provide ample opportunity to delay or suspend implementation of a given measure. According to Williams and Hammond (2020), with the unprecedented reliance on IEEPA to place broad trade tariffs and later court decisions partially invalidate those measures; it creates uncertainty among trading partners about the reliability of U.S. commitments.

4. China: Strategic Decoupling Through State-Led Transformation

4.1 Institutional Foundations of Chinese Decoupling

The way China has responded to Great Power Competition is shaped by its unique institutional framework - a Leninist party-state that controls the hierarchy of economic decision-making from above yet delegates the implementation of decisions down to local (provincial) government, or State-Owned Enterprises. This institutional design allows for rapid implementation of policies; however, it creates Principal-Agent Problems because local governments are pursuing their own self-interests under the constraints of national frameworks.

Institutional mechanisms exist at both the national and provincial levels which enable the CCP to maintain control over the strategic direction of China's economy. At the national level this includes the Central Financial and Economic Affairs Commission, and the National Development and Reform Commission. The two main vehicles for announcing major policy directions in China are Five-Year Plans and Central Committee Resolutions. These provide the broad long-term guidance for China's development regardless of who is leading the country. In contrast to the U.S., where there is little continuity in economic policy from one administration to another.

Institutional path dependence in China has significantly diverged from the U.S. The United States utilizes regulatory mechanism operating through law and market incentive, whereas China utilizes an administrative mechanism operating by way of Party Directives, State Owned Enterprise Mandates and Policy Bank Lending. These mechanisms represent an adaptation of historical legacies of central planning into a new environment with private markets while ensuring the Party maintains control over strategic sectors.

4.2 The Dual Circulation Strategy

This strategy was adopted by the Chinese government in 2020 as an alternative way of addressing their perception that global markets are unreliable. The dual circulation approach focuses on internal circulation (i.e., production, consumption and distribution) for the purpose of generating economic growth primarily via the use of domestic production; international circulation will be secondary to this effort (Grieger, 2020).

The dual circulation strategy is included in China's Fourteenth Five-Year Plan (2021-2025), which considers technological independence to be among China's highest priorities (Bertelsen, 2020). In addition to developing China's domestic market, the Plan also includes plans to improve the technology base of China's manufacturing sector. Examples of key sectors include artificial intelligence, quantum computing, semiconductor manufacturing, health and life science, neuroscience, biological engineering, space-related technologies, and deep-sea research (Bertelsen, 2020).

The three main components of the dual circulation strategy are: improving and enhancing domestic consumption, promoting industrial development and technological improvement, and creating an integrated national marketplace (Naughton, 2021). These three main components provide support for domestic circulation in three ways: Consumption creates demand; Innovation generates supply; Market creation as a way to create institutions will allow these two elements to operate together.

4.3 State-Led Industrial Policy and Indigenous Innovation

China's approach to creating an industrial policy is drastically different compared to that of the U.S. As opposed to the U.S. method of using tax incentives and grants to incentivize private investment into target areas, China utilizes direct State funding, procurement requirements, and regulatory guidance to fund and guide resources directly into targeted sectors. Although less prevalent today than during its heyday a few years ago, the "Made in China 2025"

initiative set the stage for China's industrial upgrade within advanced manufacturing, IT, and EVs (Kennedy, 2025).

A prime example of the State led approach is China's Semiconductor Strategy. The government created the “National Integrated Circuit Industry Investment Fund”, also referred to as the “Big Fund”, and currently has in excess of $40 billion in assets to fund domestic silicon wafer manufacturing (Miller, 2022). In addition to receiving substantial state funding, SMIC, China's lead IC foundry has successfully developed a process for producing chips at a 7-nanometer node size utilizing Deep Ultraviolet Lithography with Multi-Patterning Techniques. This represents a significant advancement by China in spite of being prohibited from importing key equipment due to U.S. Export Control regulations.

The electric vehicle sector also presents an example. In order for the Chinese Government to promote the sale of Electric Vehicles within China, it has implemented incentives such as subsidies and consumer incentives along with procurement mandates which have promoted competition from over 100 EV manufacturers in China (Kennedy, 2025) and this competition has generated massive amounts of innovation and cost reductions resulting in lower costs for Chinese EV manufacturers than their Western counterparts; today, China is the world's leading automobile exporting country with over 7 million Electric Vehicles being exported each year. Approximately 7.1 million vehicles of various types were exported by China in 2025, with about 2.6 million exported as new-energy vehicles. The exports of electric vehicles were about 2.5 million, illustrating China’s growing importance in the international electric vehicle supply chains (International Energy Agency [IEA], 2026; Ministry of Industry and Information Technology [MIIT], 2026).

4.4 Why Path Dependency Operates Differently in China

The structural composition of institutions in China supports fast implementation of policies, however it is restrictive as well. The Leninist Party-State possesses a hierarchy of control which will be lost if performance legitimacy - providing higher levels of economic development and living standards, is undermined. The slowdown in Chinese growth since 2021 may affect the regime's ability to utilize resources to facilitate strategic decoupling at the detriment of general economic welfare.

In addition to providing for the speed of resource allocation into strategic areas, China’s banking system provides state owned banks with the ability to provide favorable access to funding for state preferred areas and companies. However, there is increased risk of moral hazard and misallocation of funds within these types of systems. The real-estate crisis associated with Evergrande, and many other developers has illustrated the limitations of state-controlled allocation of credit and potential risks of using excessive amounts of debt to stimulate growth.

Although there are many limits to the approach taken by China as compared to the United States - a key difference exists, however. The Communist Party has monopoly control of the Chinese political system; therefore, decoupling policy does not have the potential for policy reversals after an election. The long-term strategic planning is able to be implemented with less interruption caused by partisan changes. Therefore, it allows China to take decoupling

approaches that will need years of investments, whereas U.S. policies continue to be influenced by the time frame of the election cycle.

5. Comparative Analysis: Divergent Pathways to Decoupling

5.1 Institutional Mechanisms Compared

The United States and China are taking two completely different paths toward decoupling through institutions, which reflect their distinctly different political economic systems.

Table 1. Comparative Governance Mechanisms: United States vs. China - Tariffs as a primary instrument for both the U.S. and China

Dimension	United States	China
Primary Instruments	Tariffs, export controls, investment screening mechanisms, and tax-based industrial incentives	Tariffs, central planning frameworks, state-led investment, and government procurement mandates
Implementation Authority	Regulatory bodies such as the Bureau of Industry and Security (BIS), Committee on Foreign Investment in the United States (CFIUS), and the Department of Commerce	Chinese Communist Party (CCP) structures, National Development and Reform Commission (NDRC), and state-owned enterprises (SOEs)
Coordination Mechanism	Inter-agency coordination, legislative negotiation, and bureaucratic bargaining	Top-down hierarchical directives combined with competition among provincial governments
Time Horizon	Short- to medium-term policy cycles shaped by electoral timelines (approximately 2–4 years)	Medium- to long-term strategic planning through Five-Year Plans and national development strategies (typically 5–10 years or longer)
Constraint Mechanism	Judicial oversight, congressional scrutiny, legal accountability, and public transparency requirements	Internal performance evaluations, party discipline mechanisms, and anti-corruption enforcement overseen by the CCP
Strategic Objective	Enhance technological competitiveness, strengthen supply chain resilience, protect national security, and preserve economic leadership	Achieve technological self-sufficiency, accelerate industrial upgrading, enhance national security, and expand global economic influence
Policy Orientation	Market-oriented industrial policy with targeted state intervention in strategic sectors	State-led developmental model characterized by extensive government direction and coordination of economic activity

Source: Author's Compilation

These distinctions are not casual; they are really a product of the structural foundations of government in each country. The U.S. has a dispersed or fragmented system of governance that is based on many different authorities. In order for this to produce effective public policy it requires building coalitions and negotiating with other centers of power. China, which operates under a single or “unitary” system of government is able to implement policies very quickly due to its centralized control. However, this concentration of authority creates what are called “principal-agent” problems when lower-level government officials pursue self-interest rather than carrying out the will of higher levels of government.

5.2 Why Path Dependency in the US but Not in China?

The way institutions persist is explained by path dependence; however, the question remains as to why U.S. path dependence has been so strong while Chinese path dependence has been relatively weak. The reason lies in the differing origins of their respective systems' path dependencies.

U.S. path dependence is constitutional. The three branches of government, federalism, and judicial review were all created as "entrenched" or unchangeable characteristics of the political process. Therefore, these characteristics create many "veto points," which result in very slow and often contentious policy changes. While it may seem as though the American public agrees on what they want to do in terms of creating new policy and even though there seems to be much agreement on the necessity of implementing such policy, the U.S. political system itself demands extensive negotiations and compromises before and during the creation of policy. In addition, due to the many veto points inherent in its governmental system, much of the new policy will also require significant legal challenges before being implemented.

Chinese path dependence is ideological rather than constitutional. Although the Communist Party continues to dominate the political process in China, it is able to easily change how it utilizes that process at will. The rapid transition from focusing solely on exporting goods - export led, to utilizing both exports and domestic consumption - dual circulation, represent a fundamental change in China's economic development strategy - one that was made possible in just a few short years. The flexibility that China has demonstrated in changing course indicates that China does not have any institutional barriers that would force the party to negotiate with other independent power bases prior to making substantial changes to its strategies.

China does have some form of path dependence, but it is based upon maintaining performance legitimacy. As long as the Communist Party is able to deliver economic growth and improve living conditions for its citizens, then it will continue to enjoy legitimacy. Therefore, although China has maintained performance legitimacy and therefore has enjoyed relative stability since adopting its dual circulation strategy, China still faces limitations as a result of having to maintain performance legitimacy. Since the Communist Party has invested so heavily into maintaining performance legitimacy by providing a certain level of prosperity for its citizens and since the party fears losing its ability to provide such prosperity if it makes too abrupt of a change in its policies, the dual circulation strategy represents a continuation of those policies that have provided the high levels of economic growth experienced by China in recent decades and not a radical departure from them.

5.3 Convergence Pressures and Limits

Some researchers have suggested that the competitive nature of strategic competition may lead to an environment in which the United States and China converge by creating the same techno-nationalist systems of regulation and state-directed capitalism. However, there are already examples of this happening: The U.S. has passed the CHIPS Act, which can be seen as a major expansion of U.S. industrial policy. China has created its dual-circulation strategy, which includes using market-based mechanisms as part of a larger framework of state-led capitalism.

The institutional structures mentioned earlier also create limitations to how much the two nations will be able to converge. As stated previously, the U.S. uses regulatory incentives and restrictions to promote American industry and therefore is limited from using direct state-ownership or centrally planned methods to achieve goals. Instead of establishing state-owned semiconductor foundries, the CHIPS Act provides funding for private companies to invest in semiconductors. This limits the ability of the U.S. from implementing different types of industrial policy based upon its own institutional path dependency: regardless of whether or not the U.S. pursues industrial policy, it is still bound to use regulatory mechanisms versus administrative directives.

Similar to the U.S., Chinese industrial policy promotes growth through state-owned enterprises (SOEs), policy bank lending, and administrative guidance instead of solely relying on market incentives. For example, although tax credit programs may be used by the Chinese government to incentivize private investment, they do not provide primary financial support. State-owned banks provide financing for preferred sectors and regional governments provide support for strategically important areas in the direction of their national government. Therefore, similar to the U.S., China follows its institutional path dependency: even though China may include elements of market-based mechanisms into its system, it continues to retain ultimate control over those elements. Primary tools of Trade barriers such as tariffs, restrictions on exports, control mechanisms over foreign investments, tax advantages used by governments to support domestic industries. Trade barriers (tariffs) planned economy models, government-controlled investments, and nationalized procurement processes.

6. Discussion: Divergent Outcomes and Their Drivers

6.1 The Role of Political Structure in Shaping Decoupling Speed

The first important area of consideration is how political systems affect both the pace and completeness of the decoupling process. In the case of the U.S., the institutional characteristics of the political system include a) separate branches of government, b) federalism and c) an independent judiciary. As a result, there are many places in which policy decisions can be blocked or delayed. For example, in regard to the divestment from TikTok the U.S. started with a presidential Executive Order in 2020. After two years, and much additional legislative activity, an Act of Congress was passed in 2024, followed by almost another year when it went through Supreme Court Review in 2025. This process provided ample opportunity for blocking actions at each level of government, for litigation challenging those actions and for negotiating

terms of compromise among various interests. This type of friction is designed as part of the U.S. Constitution to protect against unwise or arbitrary policy making. However, this same friction may have serious negative consequences for the U.S. if it seeks to compete strategically with a nation-state that does not face similar constraints.

By comparison, China's single-party political system allows for relatively rapid changes to national policy. A new national development strategy called “dual circulation” was formally introduced by Chinese Communist Party leaders in October of 2020. That strategy was quickly incorporated into China's 14th five-year plan. At the same time, local authorities were instructed to develop related strategies (Grieger, 2020). Thus, unlike in the U.S. where Congressional Oversight, Judicial Review and Federalism create numerous barriers to rapid action on the part of the central government - in China the central government can rapidly shift focus to any strategic sector it chooses without needing to negotiate with other regional or local governments. The fundamental differences in these political systems will have substantial implications for how decoupling unfolds in each country. While the decoupling process undertaken by the U.S. will likely be limited in scope, contentious and subject to reversal based upon future election results - decoupling in China will likely be far completer and more enduring than would be possible under current conditions in the U.S.

6.2 The Paradox of American Industrial Policy

Beginning with the paradoxical elements of U.S. industrial policy, there is a difference in what can be considered an alternative form of industrial policy relative to the previous two decades of U.S. economic policy. Although the CHIPS Act and Inflation Reduction Act are examples of industrial policy, they utilize primarily market-based tools to achieve policy objectives rather than replacing existing markets. Therefore, the subsidies and tax credits provided to private companies under the CHIPS Act do not include the establishment of state owned semiconductor foundries (Vyas, 2025), and similarly, the IRA utilizes the tax code to provide financial incentives to encourage private sector investment into its supply chain restructuring efforts versus using regulatory mechanisms to impose specific supply chain requirements (Zhang & Shi, 2025).

This type of policy represents a reflection of America's historical institutional path dependence; however, this same aspect limits American industrial policy. Market based incentives rely upon the response of private businesses to incentives. However, if compliance with regulations does not reflect the intent or spirit of those regulations - as several automobile manufacturers have demonstrated in their implementation of Federal Energy Office Compliance (FEOC) rules - then the effectiveness of such policies will likely be significantly diminished (Evenett & Fritz, 2024). Additionally, market-based incentives may not be able to support and address the structural challenges to industries that require substantial, long-term investments across multiple sectors and stakeholders. For example, although the U.S. has offered numerous tax incentives for over three decades to stimulate development of domestic semiconductor manufacturing capability similar to East Asian countries', no such capability exists today. The paradox therefore presents itself as being both an enormous departure from prior forms of U.S. industrial policy and simultaneously, being limited by the institutional frameworks within which the new forms of U.S. industrial policy operate.

6.3 The Limits of Chinese State Capitalism

Chinese state capitalism has limitations. Although China's single-party political system allows for rapid government action, it creates principal-agent problems that can render the process ineffective. Regional governments are generally assessed using regional metrics (such as, Gross Domestic Product (GDP) growth, local taxes collected and total debt) rather than national metrics. This encourages regional officials to serve their own interests by maintaining regional capital, talent and companies within their area – even if these actions fragment the national economy (Naughton, 2021). The announcement of the Unified National Market Initiative in 2022 is an acknowledgment that while there have been many years of reforms to address regional protectionism barriers to domestic circulation remain a major obstacle.

The Chinese state-owned enterprise sector is facing significant challenges with regard to governance. State-owned commercial banks provide credit to favored sectors and firms through the state banking system which may create moral hazard and misallocation of resources. The crisis in China related to the housing/real estate development industry with respect to Evergrande and other developers demonstrated how state-directed allocation of credit for development purposes does not mitigate the risk of excessive reliance on growth based upon high levels of debt. Additionally, state-owned enterprises tend to be less innovative than private companies as they lack competitive pressure due to their monopolistic status as well as structural differences in incentives compared to private companies. The limitations of Chinese state capitalism indicate that decoupling will be costly for both the U.S. and China. China cannot rely solely on direction to achieve self-sufficiency in technology and instead needs to establish the institutional capacity necessary to support innovation, efficient allocation of capital and coordination of economic activities throughout a large and geographically dispersed country. These represent significant hurdles that will influence the course of Chinese decoupling.

7. Implications of Strategic Decoupling

7.1 The Emergence of Parallel Technological Ecosystems

The primary consequence of strategic decoupling is the development of parallel technological systems. In such systems the U.S. and China are creating separate foundational structures in critical emerging technologies. Examples include semiconductors, 5G telecommunications, artificial intelligence and quantum computing. A characteristic of these systems is a lack of compatibility among their components. Divergence exists regarding the technical standards used to define each system component. Separate Intellectual Property (IP) regimes govern each system's IP rights. A prime example of this trend can be seen in the Semiconductor Industry. Export restrictions imposed by the U.S. on advanced semiconductor products and manufacturing equipment restrict China's ability to acquire those same advanced chip and manufacturing tools. In response to U.S. export control actions, the CHIPS act was passed to restore America's semiconductor production capabilities (Miller, 2022). In turn, China accelerated its efforts to replace imports with domestically produced semiconductor products. However, due to reliance upon foreign sources for numerous types of chips, a significant amount of China's demand for semiconductor products continues to be met

through foreign sourced chips. As a result, there exist two distinct and partially independent semiconductor supply chains, and virtually no transfer of technology occurs between them. Fragmentation of the global semiconductor market has resulted in increased costs for both economies and reduced efficiencies resulting from globalization.

Consequences of Strategic Decoupling extend beyond Semiconductors into all aspects of the Digital Economy. Should the U.S. and China establish incompatible 5 G standards; create separate AI governance mechanisms; and develop divergent data Protection regimes then global digital trade will continue to fragment. Multinationals will incur greater Compliance Costs as they operate under two separate Regulatory Frameworks. Depending on the Ecosystem with which an individual is affiliated will determine what digital services that person has available to him/her. The Global Digital Economy established during the 1990 s and early 2000 s could potentially transition to a Bifurcated System. Developing Countries could suffer disproportionately from this fragmentation as they would likely need to choose whether to affiliate themselves with either the U.S./Western Ecosystem or the Chinese/Asian Ecosystem; thereby forcing them to abandon potential access to Technologies and Markets.

7.2 The Transformation of Global Supply Chains

For decades, multinationals have been optimizing their supply chains for efficiency and cost. They located manufacturing where it was cheapest and where they had the best talent. This logic has resulted in extensive interdependence between the U.S. and China. China became known as the "world's factory" and the U.S. became one of the largest markets for goods manufactured in China. The strategic de-coupling trend is reversing this logic. Companies in both the U.S. and China are being pressured into restructuring their supply chains to be more resilient and focused on national security as opposed to just efficiency. Provisions under the FEOC in the IRA require automotive manufacturers to leave Chinese supply chains for EV battery sourcing, regardless of increased costs (Zhang & Shi, 2025). Semiconductors in China are being encouraged to use domestic sources for component parts, even if foreign suppliers can provide higher quality products at lower price points.

This is leading to a less efficient and more expensive global economy. Estimating that complete decoupling would lead to a reduction of global GDP of 5% to 10%, long-term and that the majority of the costs would fall within industries that are highly interconnected across the two economies (Evenett & Fritz, 2024). While there will likely be winners and losers from de-coupling, some nations are expected to receive positive impacts due to changes in global supply chains including Vietnam, Mexico, and India as examples of possible beneficiaries. Decades of development, trade, and investment will be impacted by a new paradigm of global supply chains. Companies that can successfully navigate this transition could gain a competitive advantage, while those who cannot become obsolete. The role of government will also increase significantly as governments begin to take a much larger role in decision-making related to supply chain logistics, a marked departure from the market-driven model used for nearly thirty years.

Economic analysis based on modeling predicts a reduction in global GDP of about 7.9 percent by 2030 from an already decoupled scenario as compared to a scenario where no more economic decoupling occurs. The above figure is derived from a particular scenario where

there would be extra non-tariff barriers amounting to 100 percent tariffs among geopolitical blocs.

Table 2. Estimated Global GDP Losses Under Alternative Scenarios of U.S.–China Economic Decoupling by 2030

Source and scenario	Estimated economic effect	Interpretation
Kumagai (2023), moderate decoupling	2.3% reduction in global GDP by 2030	Trade barriers comparable to those imposed during the U.S.–China trade war.
Kumagai (2023), severe decoupling	7.9% reduction in global GDP by 2030	A modeled scenario imposing additional non-tariff barriers equivalent to 100% tariffs between the two blocs.
Cerdeiro et al. (2021), technological decoupling	Around 5% GDP losses for many economies	Country-level losses from technological fragmentation, not a global GDP estimate.
Bolhuis et al. (2023), broader trade fragmentation	2.3% long-run global output reduction; 4.8% short-run reduction	A scenario forcing countries into exclusive trade relationships and imposing barriers across sectors.

Sources: Kumagai (2023), Cerdeiro et al. (2021), and Bolhuis et al. (2023).

7.3 The Erosion of the Rules-Based International Order

The third consequence of the new cold war is that it erodes the rule-of-law based international order that the U.S. created post-WWII. The World Trade Organization's Dispute Settlement System - an integral part of international trade governance - has been severely undermined due to the U.S. obstruction of appellate body appointments. Both the U.S. and China have imposed tariffs and trade restrictions against each other without WTO authorization; this undermines the long-standing norm that trade disputes would be resolved through multilateral institutions versus unilaterally (Zirpoli et al., 2025). When the U.S. and China fail to work together economically, they will find it even more difficult to work cooperatively on global issues - including climate change, pandemics, and preventing the proliferation of weapons of mass destruction.

As noted above, the two largest economies in the world are also the two largest producers of greenhouse gas emissions. Therefore, if there can be no coordination on climate policy from these two countries - then it will become increasingly difficult to address global warming. If strategic competition between the U.S. and China continues to poison cooperation among them on every possible issue area, it will make it increasingly difficult for the international community to take coordinated action to solve "collective action" problems that require the cooperation of major powers. In addition, as the current norms and institutions continue to be challenged by revisionist powers - including Russia - a world where the U.S. and China are competing against one another solely through unilateral actions will be a far more perilous and uncertain world with a greater likelihood of miscalculations, escalations, and conflicts.

8. Policy Recommendations

8.1 Establish a Bilateral Technology Dialogue

The second part of this article has suggested that the U.S.- China relationship can be managed through a series of policies rather than being limited to two broad options: either competitive or cooperative. In addition to these policies, the authors suggest that in order to manage U.S. and Chinese relations effectively in the area of technological development, a formal bilateral technology dialogue should be created. This dialogue would provide both countries with a regular forum in which to discuss issues related to technology and commerce. These issues would include technology transfer, export control practices, and commercial practices such as the use of industrial subsidies.

In creating this dialogue, the critics are drawing upon the experience of the U.S.-China Strategic and Economic Dialogue, which was held during the Obama administration. Although there were some limitations to that process, it provided a model for how the two nations could have regular meetings at high levels of government to discuss key issues in their relations. I believe that the U.S.-China Technology Dialogue will allow for greater transparency concerning the actions taken by each country regarding technology and commerce. In particular, they recommend that each country agree to inform the other about changes in its export control regime prior to implementing those changes. They also recommend establishing procedures for resolving disputes arising out of differences over the interpretation of trade agreements.

8.2 Develop Allied Supply Chain Coordination

The next suggested policy is for the United States, along with allied countries, to create coordinated supply chain strategies. The U.S. alone cannot disengage from China; doing so would likely result in high costs to the U.S. economy as well as angering many important allies. Therefore, a more practical solution is for the United States to work with European allies such as Germany or France, Japanese allies like Toyota and Honda, and South Korean allies such as Hyundai and Kia, etc., to create aligned policies in terms of reducing reliance on Chinese supply chains within key industries. Coordination would come in three ways.

First, nations would need to align export control regulations and investment screening processes so as to limit the likelihood that restrictions imposed by one nation would cause businesses to transfer their operations to an ally nation. There are examples of this type of coordination already being done - for instance, there is ongoing collaboration between the United States, Japan, the Netherlands, and South Korea regarding semiconductor exports (Miller, 2022). Second, nations would collaborate on providing government subsidies to industry in order to prevent subsidy competition where all parties benefit at the expense of consumers around the world. For example, U.S. subsidies under the Chips Act, may be coordinated with equivalent subsidies provided by European governments and/or Japanese government(s) so as to ensure that resources are allocated efficiently. Third, nations would establish and agree upon a set of common criteria for evaluating whether a supply chain presents a national security risk and implement procedures to evaluate foreign investment. Coordination is crucial due to the fact that the U.S. can't accomplish decoupling independently. Many U.S.

allies in both Europe and Asia have business relationships with China and will not blindly follow U.S. policy absent discussion and agreement. Developing consensus across nations will be slow and burdensome; however, it is required if long-term strategic decoupling is desired.

8.3 Invest in Domestic Innovation Capacity

The third recommendation would include continued investments in U.S. innovation capabilities. It is necessary to create U.S. technology-based capabilities that allow the U.S. to reduce or eliminate reliance on Chinese sourced technologies and products. While the CHIPS Act was an initial investment, there is a need to invest in a wider array of emerging technologies. Investments should be focused on three areas. First, there needs to be a significant increase in funding for basic research focusing on the physical sciences, engineering, and computer science. The United States has allowed the basic research base to atrophy compared to China which currently outperforms the U.S. in many major metrics used to measure research productivity. Second, there should be expanded workforce development initiatives that provide training for scientists, engineers, and technicians required for both domestic semiconductor manufacturing and other high-technology sectors.

Third, investments in applied research and development should be designed to incentivize private sector investment with minimal opportunity for waste through the provision of government funded incentives. A competitive grant program as established by the CHIPS Act represents one example of how government provided financial incentives could be allocated on a basis consistent with commercial viability and national security objectives. Ultimately, the most effective means of sustaining competitiveness through strategic competition will require sustained investments in the generation of new technologies and new industry sectors. Export control measures and/or trade restrictions may be able to temporarily impede Chinese technology advancements; however, these types of measures cannot replace the necessity of U.S.-generated innovations. Therefore, to continue to maintain competitiveness within the global economy, it is critical that the U.S. sustainably invests in research, education, and development.

10. Conclusions

The regulatory mechanisms that operate through laws and market incentives would have been the approach used by the U.S. The administrative mechanisms operating through Party directives and State-Owned Enterprise mandates would have been the approach used by China. The separation of the U.S. and China at the level of strategy constitutes an extraordinary transition for the world political-economic environment. In this paper I have demonstrated that the path dependence of institutions explains how each nation responded to great power rivalry, thereby causing different approaches to separate - decouple based upon essentially equivalent objectives. Regulatory mechanisms which function through laws and market incentives represent the approach adopted by the U.S., whereas administrative mechanisms functioning via Party directives and State-Owned Enterprise mandates represent the approach adopted by China.

I discuss three primary arguments in the discussion: the role of political structure in determining the rate of decoupling, the paradox of American industrial policy, and the

limitations of Chinese state capitalism. I identify several implications of decoupling: the creation of alternative technological ecosystems, changes in global supply chains, and a weakening of the international rules-based order. Recommendations for policy also exist, including the establishment of a bilateral technology dialogue, the development of coordinated supply chains among allies, and investments in domestic R&D capabilities.

There are three general findings associated with this study. First, it will not result in one single model of techno-nationalism but instead create additional competing economic governance models, creating friction in global trade, investment and technological collaboration. The U.S. and China are constructing complementary ecosystems in critical technologies, with low levels of compatibility and increasingly diverging standards, regulations and IP regimes.

Secondly, success in decoupling is dependent on institutional capability. The U.S. regulatory state creates mechanisms for decoupling; however, its ability to implement decoupling is impacted by fragmentation, polarization and judicial review. China's unitary state allows for rapid implementation; however, its ability to do so is impacted by principal-agent problems, risk of misallocation and maintaining performance legitimacy. Neither system is unconditionally better than the other; each has relative strengths and weaknesses.

Lastly, the direction of travel of the future global economic order will be determined by how these two systems interact. Decoupling completely is unlikely because the cost will be too high for both countries. Instead, "managed competition" characterized by cooperation in some areas and confrontation in other areas is likely to describe the U.S.- China relationship for the foreseeable future. Managed competition will lead to a more fragmented and less predictable global economy with significant impacts on trade, investment, technology transfers and international cooperation on global issues.

This paper demonstrates that understanding the institutional basis of divergence is essential to predict the trajectory of decoupling. The U.S. and China are making decisions about differing sets of policy choices; they are operating under differing governance structures that dictate what policy options exist, how those options can be implemented and how those options evolve over time. Those governance differences will continue to define the great power competition that defines twenty-first century international relations.

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