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Tesla Goes to China

ERIC HARWIT

Asia Pacific

I S S U E S

Analysis from the East-West Center

No. 152

April 2022

About the Author

Eric Harwit is a professor of Asian Studies at the University of Hawai'i at Mānoa, and an adjunct senior fellow at the East-West Center. He thanks Chen Xinyi for research assistance with this article.

He can be reached at harwit@hawaii.edu.

Papers in the Asia Pacific Issues series feature topics of broad interest and significant impact relevant to current and emerging policy debates. The views expressed are those of the author and not necessarily those of the Center.

SUMMARY Over the past decade, Tesla has been one of the most successful American companies in the US's electric vehicle (EV) industry. Not satisfied with dominating the US market, the company turned in 2014 to China to expand its vehicle sales. There, Tesla entered a market with a mix of privately owned companies, joint ventures, and state-owned manufacturers, all operating since 2009 with government support. Indeed, in China, as it did in the United States, Tesla has benefitted greatly from both central and local government subsidies to EV manufacturers and customers. In 2020, China was reported to be the fastest growing market for Tesla, whose new manufacturing base in Shanghai made its vehicles more cost competitive. With China's government mandating that by 2030, 40 percent of all vehicle sales should be EVs, the future seems bright. But challenges include planned changes in government-supported incentives.

As early as 2009, the Chinese government offered incentives for manufacturers and consumers of electric vehicles

Over the past decade, Tesla has been one of the most successful American vehicle companies in the US's electric vehicle (EV) industry. This growth, however, has come along with significant assistance from the US government. From 2010, when the company received \$465 million from the federal Advanced Technology Vehicle Manufacturing loan program, which helped the company build out its California production factory,¹ to a \$7,500 tax credit for models made as early as 2008,² Tesla has benefited from US policies to advance the EV sector. Even state governments played a major role in assisting the company, as California's Zero Emission Vehicle credit selling system allowed Tesla to add \$428 million to the company's revenue in the second quarter of 2020.³ By mid-2021, Tesla held some 71 percent of the domestic American EV market.⁴

Not satisfied with dominating the US market, the company turned to China to expand its vehicle sales. The interest in China came naturally, because China's overall vehicle market has been larger than that of the United States since 2008. In 2020, total passenger car sales in China totaled 19.3 million vehicles; 1.1 million of those, or about 5.7 percent of the total, were electric passenger cars.

How China Built Its EV Market

In the first half of 2021, Chinese consumers demonstrated a growing appetite for EV passenger cars: to the end of July, 1.23 million EV had already sold, up more than 200 percent from 2020. In the second quarter of 2021, electric vehicles made up 12 percent of total passenger car sales in the country. China's government is mandating that by 2030, 40 percent of all vehicle sales should be EVs.⁹

China's strategy to develop its electric vehicle sector, in some ways like that of the US path, has been rooted in government financial support and consumer incentives. Unlike in the United States, however, the Chinese strategy has also depended on the growth of several state-invested manufacturers.

Incentives. As early as 2009, under the leadership of Minister of Science and Technology Wan Gang, who aspired to replace foreign energy technologies with domestic resources,¹⁰ the Chinese government offered incentives for manufacturers and consumers of electric vehicles. Taxi fleets and local government agencies in 13 cities could receive subsidies of as much as \$8,800 for each hybrid or all-electric vehicle purchased. The state electric grid was ordered to set up charging stations in the major cities of Beijing, Shanghai, and Tianjin. The government also offered research subsidies for electric car designs and began to plan for tax credits for consumers who purchased alternative energy vehicles.¹¹ In 2010, the same subsidy of \$8,800 was offered to buyers, initially in five cities, who purchased plug-in hybrids and pure electric vehicles.¹² And the following year, the government announced that pure electric, fuel-cell, and plug-in hybrid vehicles would be exempt from an annual vehicle tax.¹³

Policies to encourage manufacturing and purchases of electric vehicles varied over the following decade, but as of 2021, China continued to offer several incentives. For example, pure electric cars with a minimum driving range of 300 km received a subsidy of \$2,500-\$3,500, and a plug-in hybrid with minimum driving range of 50 km was offered a subsidy of about \$1,300.¹⁴ China also waived expensive license plate fees in some cities, which could cost up to \$15,000.¹⁵ In 2015, buyers of EVs in Beijing were given exemptions from odd-even license plate restrictions on driving on city roads during rush hours.¹⁶ In a society where many urban residents live in apartment buildings lacking access to home garages with electrical outlets, access to charging stations for electric vehicles was also key to the sector's growth. By 2019, China had 1.2 million charging stations, and had plans to build 600,000 more.¹⁷

Manufacturing. In line with government policies that emphasize the role of public sector corporations, several of the leading companies in China producing electric vehicles are fully state-owned enterprises (SOEs): for example, the Chery Auto-

Access to charging stations for EVs was a key to the sector's growth in China

mobile Co. Ltd. is owned by the Wuhu, Anhui municipal government; Guangzhou Auto and SAIC (formerly the Shanghai Automotive Industry Corporation) are owned by their eponymous cities.

However, it was a joint venture that produced the top selling electric vehicle in April 2021: the mass market-focused Hongguang Mini EV model, a two-door compact electric passenger car that sold for only about \$4,500.¹⁸ The car's manufacturer, SAIC-GM-Wuling, is a Sino-American SOE-foreign joint venture company, owned 44 percent by General Motors' GM China division.¹⁹

China's conventional car market has long been dominated by joint venture manufacturers. Starting from the late 1980s and into the 1990s, foreign companies such as Volkswagen, General

Motors, Toyota, Honda, Nissan, Hyundai, Ford and others have formed 50-50 joint ventures to produce cars in cities across the nation. A 1994 automotive industrial policy mandated that foreign car companies manufacturing in China that wanted to sell vehicles in the domestic market had to have a Chinese partner and could hold a maximum of 50 percent ownership in the joint company. Joint ventures have not dominated the EV market, however; the Hongguang Mini is the only one of the 15 top selling EVs to come out of a joint venture.

Private Chinese companies are also playing a growing role in the electric vehicle market. The number three selling model, the Han EV, is produced by privately owned BYD Auto, a divi-

Joint ventures dominate the conventional car market, but not the EV market

Table 1. Top 15 of China's New Energy Vehicle Sales, April 2021

Vehicle Model	Manufacturer	Ownership Type	Vehicles Sold
Hongguang Mini EV	SAIC-GM-Wuling	State-owned / Foreign Joint Venture	26,592
Model 3	Tesla	Foreign	6,262
Han EV	BYD Auto	Private	5,746
eQ	Chery	State-owned	5,617
Li Xiang One	Li Auto	Private	5,539
Model Y	Tesla	Foreign	5,407
Aion S	Guangzhou Auto	State-owned	5,077
Ola Black Cat	Great Wall	Private	4,613
Roewe Clever	SAIC	State-owned	4,130
Neta V	Hozon Auto	State-owned	3,846
Benben EV	Changan Auto	State-owned	3,826
Qin PLUS DM-i	BYD Auto	Private	3,603
Weilai ES6	Nio	Private	3,163
Xpeng P7	Xiaopeng Motors	Private	2,995
e2	BYD Auto	Private	2,918

Source: China Passenger Vehicle Federation, in Chinese, as cited at Beijing Dokrypton Information Technology Company website, online at <https://36kr.com/p/1236494582681985>

Table 1 illustrates the complexity of manufacturing company ownership in the Chinese electric vehicle market. Though a snapshot of sales only for the month of April 2021, the table gives information on the key EV producers, their various sales model production numbers, and their ownership structure.

sion of BYD Company Ltd., which itself is owned 8.25 percent by American billionaire Warren Buffett's Berkshire Hathaway company.²⁰ BYD has arguably the longest record of producing alternative energy vehicles, having introduced a plug-in hybrid model car as early as 2008. Though sales suffered in 2020, in 2021 BYD made a strong comeback, recording growth of 232 percent over the previous year's sales.²¹

In the Chinese domestic private manufacturing sector, BYD faces challenges from many new companies that have only recently become competitive. Startup electric auto manufacturers Xpeng Motors and Nio have recently opened large factories and have plans to open more.²² But production volume could be a problem for some of the new entrants to EV production—for example, Nio sold only 7,200 cars in January 2021, and by February had yet to make a profit.²³

In addition to the private start-up companies, established private corporations, ones that had focused mainly on conventional auto manufacturing or production of unrelated technologies, also began to eye the electric vehicle marketplace. For example, Zhejiang Geely, which was founded in 1986 and is now the owner of Volvo Cars, opened a new electric car factory in early 2021.²⁴ Even global telecommunications giant Huawei Technologies in April was reportedly considering taking control of a small domestic auto manufacturer's electric vehicle unit.²⁵

Foreign carmakers have also rushed to establish their own EV manufacturing base in China. By July of 2021, Volkswagen had built dedicated electric car factories in the cities of Shanghai and Foshan, with a combined annual capacity of 600,000 vehicles. By year's end, it had sold 70,625 of its ID series of electric vehicles.²⁶

However, EVs from other foreign carmakers, besides Volkswagen and Tesla, barely registered in these new energy vehicles sales lists. And Chinese government rules mandate that new foreign EV factories need a minimum production capacity of 100,000 electric passenger cars or 5,000 electric commercial vehicles, thereby presenting a high investment hurdle for new foreign entrants.²⁷

In sum, the fastest growing Chinese EV companies include a major Sino-foreign joint venture;

several purely private Chinese companies; one major foreign manufacturer, namely Tesla; and several state-owned enterprises. In every case, Chinese government policies to encourage the sector were important for spurring its rapid growth.

Tesla's Progress in China

Tesla has seen great success in China. It opened its wholly owned "Gigafactory" in Shanghai in 2019, making batteries and cars. By 2020, Tesla had captured a 13 percent share of the country's electric vehicle market. It faces challenges, however, from state-owned and private domestic manufacturers, as well as from planned changes in China's incentive structures.

Though successful now, the company got off to a rocky start in China, when it began selling vehicles in 2014. Through 2015, vehicle delivery delays and negative perception of charging options led to poor sales. Tesla, like all foreign auto manufacturers, also faced a 25 percent tariff on imported vehicles, one that added to the cost of the car.

However, the company worked to install hundreds of its "Superchargers" and thousands of "Destination" chargers to win over customers.²⁸ By 2016, more than 15 percent of Tesla's more than \$7 billion of total revenue came from its business in China,²⁹ where it sold some 11,000 vehicles.³⁰ At the time, imported luxury Teslas sold for \$104,000 to \$121,000.³¹

In June 2017, Tesla announced it was in talks to establish a factory in the automotive industrial city of Shanghai, a move meant to increase its sales volume in the country. However, as a foreign automaker wanting to manufacture and sell in China, Tesla was required to find a joint venture partner, a move that could have compromised its ability to protect its intellectual property.

Tesla was able to avoid the joint venture requirement by establishing its factory in Shanghai's Free Trade Zone (FTZ). In 2016, Shanghai's FTZ, from among China's 11 FTZs listed that year, had been selected to host foreign battery manufacturers. The next year, Chinese authorities moved to allow foreign electric vehicle companies to set up shop in the FTZ without a Chinese

Though successful now, Tesla got off to a rocky start in China

partner.³² As a wholly foreign-owned enterprise, in the FTZ Tesla could more carefully manage production methods and control for quality, while better protecting its intellectual property. Tesla further cemented ties to China when it revealed in 2017 that it had sold a 5 percent stake in the company to Chinese internet giant Tencent Holdings for \$1.8 billion.³³

Tesla's October 2018 official announcement that it would build its first overseas Gigafactory in Shanghai came the same year the Chinese government announced an end to the joint venture requirement for those making fully electric and plug-in hybrid vehicles. At the same time, the government announced the joint venture requirement for all vehicle makers would end by the year 2022.³⁴

Tesla worked quickly to build its Shanghai facility, and by 2020 production was up and running. That year, the company made 140,000 Model 3 vehicles, and began production of its Model Y cars in 2021. The factory size more than doubled to facilitate production of the Model Y autos.³⁵

With two models in its portfolio, early 2021 saw record sales for Tesla Shanghai. China's media promoted the success of the company's March sales, which reached 35,478 units in total, with 25,327 Model 3 cars and 10,151 of the recently launched Model Y's. Tesla finished 2021 with total vehicle production for the year at its Shanghai Gigafactory of 473,078 vehicles, with some 160,000 of those exported to markets outside of China. Production in China represented about half of all the 936,000 vehicles Tesla delivered globally that year.³⁶

The official *Global Times* newspaper noted that China had become the fastest growing market for Tesla, and that its base in Shanghai made the vehicles more cost competitive.³⁷ In late July, the least expensive Tesla vehicle in China sold for US\$36,500 (though its luxury cars, the largest part of its market, sold for much more). The starting price of the base Model 3 in the United States was \$39,990.³⁸

Tesla also moved quickly to expand its offering of charging stations. In February, the company began production at its dedicated supercharger factory in Shanghai of its V3 models.³⁹ These

superchargers took only 15 minutes to add 200 miles to a car's driving range.⁴⁰ By March, China hosted about 6,000 supercharger stalls,⁴¹ and in late May Tesla listed 692 supercharging stations on its website, with as many as 72 stalls each, and another 388 stations "coming soon."⁴² Tesla also aimed to appeal to long-distance drivers, as it created a "Silk Road" of charging stations connecting major cities up to the northwest Xinjiang region.⁴³

The company did hit some speed bumps in early 2021. In March, a security camera at one of Tesla's supplier factories in Henan province was hacked, indicating a possible attempt to steal intellectual property. The Shanghai factory itself, however, was unaffected.⁴⁴

A later spate of Tesla car accidents, ones widely broadcast in China's media, also threatened to dampen the company's product popularity. In April, a vehicle owner publicly protested at the Shanghai Auto Show by standing on top of a Tesla car; she blamed the company for an earlier accident involving her Tesla's braking system.⁴⁵ In the month of May alone, a Tesla knocked down and killed a traffic officer in Zhejiang province,⁴⁶ a Model 3 caught fire in Guangzhou,⁴⁷ and a Tesla in Guangxi province lost control and crashed into a store's glass front.⁴⁸ Tesla, likely recognizing the power of China's media to portray it as an irresponsible foreign manufacturer, specifically apologized to the Auto Show protester, writing on its social networking platform "We will try our best to learn the lessons of this experience."⁴⁹

At the end of 2021, the Chinese government announced it would cut subsidies on new energy vehicles, including EVs, by 30 percent in 2022, and withdraw them altogether at the end of the year.⁵⁰ This step could potentially hamper Tesla's future growth. However, provincial and municipal governments have continued to subsidize as much as 30 percent of charging station installation costs.⁵¹ And taking advantage of a policy similar to California's Zero Emission Vehicle mandate, Tesla could add to its revenue by selling credits under the second phase of the government's new energy vehicle credits policy that began on January 1, 2021.⁵²

The Chinese government is cutting subsidies on EVs, which could hamper Tesla's future growth

Tesla in China Going Forward

Despite what turned out to be short-term setbacks, by 2021 Tesla seemed well placed to maintain a dominant position in the luxury end of China's EV market. In addition to the prestige Chinese consumers receive by purchasing the American vehicle, the manufacturing capacity and supporting infrastructure Tesla has created in China should put it in good stead with both the nation's citizenry and the Chinese government. Moreover, Tesla CEO Elon Musk has likely accumulated goodwill from Chinese officials as he pursued his overseas investment even in the face of the Trump administration's calls for returning manufacturing enterprises to American soil.

In a move possibly meant to further ties with the Chinese authorities who want to promote domestic corporations, in November 2021 Tesla reportedly began receiving electric batteries from Chinese company CATL, the world's largest car battery manufacturer.⁵³

Unless Tesla faces more serious technical problems with its vehicles made in China, the company is in a good position to maintain and possibly expand its share of the world's largest EV market. At the same time, it puts an American company in prime position to take market share from Chinese competitors in their home market, and perhaps delay the day when Chinese EV makers may move to sell their vehicles in the global marketplace.

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ISSN: 1522-0966

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