

# THE IMPACT OF U.S. – CHINA POLITICAL AND TRADE TENSIONS ON U.S. LISTED CHINESE FIRMS: AN EVENT STUDY APPROACH

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## ABSTRACT

*We investigate whether major U.S.–China political events impact U.S.-listed Chinese firms stock prices. We find that the cumulative average abnormal returns of these firms are mixed, but upon the Inauguration of President Joseph Biden, the U.S. listed Chinese firms experienced a cumulative abnormal return (CAR) of 6% over an event window of -2/+5 days. Further, upon a major decision from the WTO (Dec. 9, 2022) that ruled President Trump breached global trade rules in 2018, U.S.-listed Chinese firms experienced a CAR of 8% over a window of -2/+5 days. Finally, Speaker of the House Nancy Pelosi’s visit to Taiwan in August of 2022 had significant negative impacts on U.S.-listed Chinese firms (-40 % loss in value during a window of -20/+10 days). Our results provide evidence that certain but not all U.S.-China events impact Chinese listed firms and investors need to be aware of potential risks and future foreign policy changes.*

## INTRODUCTION

U.S. President Joe Biden’s May, 14, 2024 announcement of tariffs of over 100% on Chinese electric vehicles was a stunning indication of the persistent and intensifying trade tension between the two countries.<sup>15</sup> The range of other products also covered by this announcement (semiconductors, solar cells, and critical minerals) signals the multifaceted, geopolitical nature of the issue.

Since 2017, the relationship between the United States and China has been marked by a complex interplay of cooperation, competition, and tension. The early years of this period saw efforts by both nations to address common global challenges, such as climate change and North Korean denuclearization. However, underlying economic and geopolitical differences began to surface, leading to increased trade tensions. The Trump administration in the United States

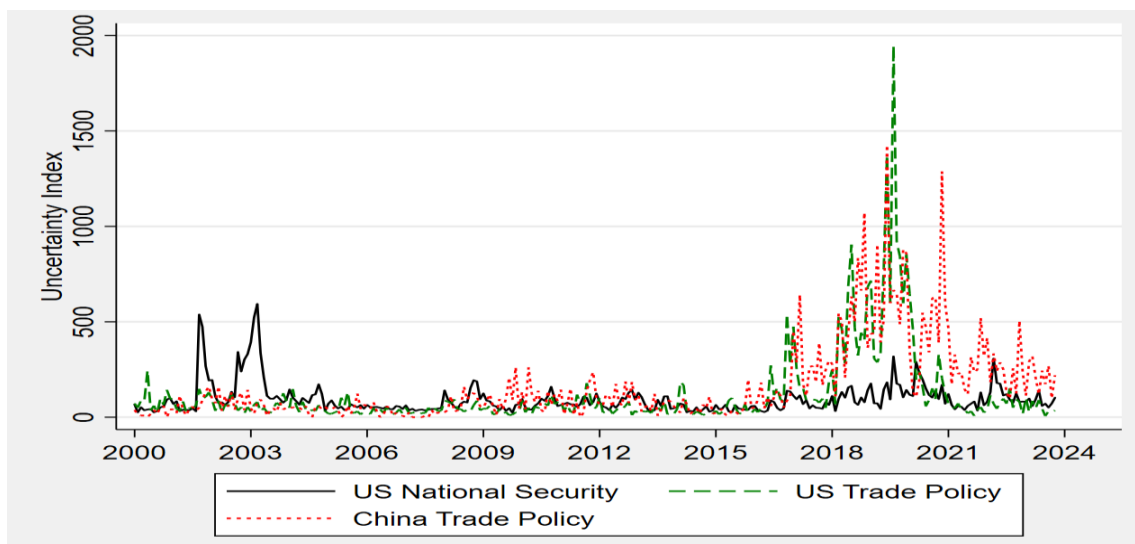
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<sup>15</sup> Biden sharply hikes US tariffs on an array of Chinese imports, Trevor Unnicutt and Steve Holland, May, 14, 2024, Reuters, <https://www.reuters.com/markets/us/biden-sharply-hikes-us-tariffs-billions-chinese-chips-cars-2024-05-14/>

pursued a more confrontational approach, implementing tariffs on Chinese goods and labeling China a currency manipulator. These actions triggered a trade war that escalated over the following years, impacting global markets and straining diplomatic ties.

In 2021, the Biden administration assumed office with a commitment to recalibrating U.S.-China relations. While acknowledging the need for competition, the new administration sought avenues for cooperation on issues like climate change and pandemic response. Nevertheless, challenges persisted, including human rights concerns, cybersecurity issues, and territorial disputes in the South China Sea. The relationship remained characterized by a delicate balance between areas of collaboration and competition, reflecting the complex interdependence of the world's two largest economies.

**Figure 1: Trade and Security Policy Uncertainty Measures** (<https://policyuncertainty.com/>)



The evolving dynamics between the U.S. and China continue to shape global geopolitics, with implications for trade, technology, and international security. Figure 1 provides a visual of how U.S. and China's trade policy uncertainty measures have changed over time. It is evident that since 2017 trade policy in both countries have been evolving rapidly as well as the policy uncertainty surrounding U.S. national security.

Recent literature has shed some light on how the evolving relationship between U.S. and China has impacted the economy and equity prices. In general, these studies find the following: 1) Chinese industries exhibit more exposure to trade tensions compared to their U.S. counterparts (Chen and Pantelous, 2022), 2) trade policy uncertainty (TPU) has heterogeneous effects on U.S. and China stock markets. U.S. TPU has a stronger impact on both U.S. and Chinese stock markets. Time-varying characteristics show that U.S. - China trade conflicts have a positive effect on U.S. stock market but a negative effect on the Chinese stock market (He et al. 2021), 3) The escalation of the recent trade war reduces gross domestic product (GDP) in China and the U.S. by  $-1.41\%$  and  $-1.35\%$ , respectively (Itakura, 2020). The trade war reduces nearly all sectoral imports and outputs in both countries. Chen, Fang, and Liu (2023) examine the

composite firms in the S&P 500 index and show that firms with high exposure in exporting their products to Chinese consumers suffer more in valuation than those with high exposure in importing goods from Chinese producers.

To this point, most literature that focuses on the impact of U.S.–China tensions on equity prices has only used market and industry indices to capture the impact. This paper adds to the literature by focusing on U.S.-listed Chinese firms and employing an event study methodology with individual U.S.-listed Chinese firm's data. This is an important contribution as U.S.-listed Chinese firms have become a significant and controversial component of the global financial landscape. Many Chinese companies, particularly in the technology and e-commerce sectors, have sought listings on U.S. stock exchanges to access international capital markets and broaden their investor base. U.S. investors have been attracted to these firms' growth potential and diversification benefits, contributing to their substantial market capitalizations.

Over 55 percent of Americans own stocks and rely on managed pension funds, mutual funds, exchange-traded funds, and direct investing to gain exposure to equities. A substantial percentage (+20%) is generally allocated to international equities. In 2019, nearly \$400 billion of new foreign investment into Chinese equities was driven by changes in allocations within benchmark indexes, with American investors accounting for more than a third of these massive portfolio flows.<sup>16</sup> The dichotomy of U.S. market participants investing more in Chinese companies, even as some U.S. policies aim to discipline China for its trade practices, poses significant risks. Not only will U.S. investors' portfolios become potentially too exposed to a single equity class, but they will also be allocated to one that could be subject to U.S. sanctions or Chinese government controls. To manage these and other inherent risks, U.S. investors need to understand and monitor the foreign policy decisions and geopolitical risks related to China. This research provides evidence of how U.S.-listed Chinese firms react to major U.S.–China political events.

## **THE U.S. EQUITY MARKET LANDSCAPE FOR CHINESE FIRMS**

### **The Holding Foreign Companies Accountable Act (HFCAA)**

The Holding Foreign Companies Accountable Act (HFCAA) was a piece of legislation passed by the U.S. Congress in December 2020. The primary purpose of the HFCAA is to enhance transparency and accountability for foreign companies listed on U.S. stock exchanges. HFCAA specifically targets companies from countries with restrictions on U.S. oversight, such as China. One of the key provisions of the HFCAA requires foreign companies to provide access to their audit work papers for inspection by the Public Company Accounting Oversight Board (PCAOB), which is a non-profit corporation that oversees audits of public companies.

Under the HFCAA, if a foreign company fails to comply with the PCAOB audit inspection requirements for three consecutive years, it faces delisting from U.S. stock exchanges. The legislation aims to protect American investors by ensuring that they have access to accurate and reliable financial information from foreign companies. By holding these companies

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<sup>16</sup> See for further information related to institutional and managed funds exposure to Chinese equities - <https://www.reuters.com/markets/asia/us-institutional-investors-could-face-restrictions-chinese-stock-ownership-2023-08-04/>

accountable and subjecting them to the same audit standards as U.S. companies, the HFCAA seeks to strengthen the integrity of U.S. financial markets and protect investors from potentially fraudulent activities or financial irregularities.

In its 2022 HFCAA Determination Report, the PCAOB retracted its determination that Chinese authorities prevented inspections of auditors based in mainland China and Hong Kong as mandated under the Sarbanes-Oxley Act of 2002. This reconsideration by the PCAOB means that Chinese companies do not currently face the risk of delisting from U.S. exchanges by retaining the service of these auditors.<sup>17</sup> The PCAOB's report followed an agreement reached on August 26, 2022 with the China Securities Regulatory Commission (CSRC) and China's Ministry of Finance allowing the PCAOB to inspect Chinese and Hong Kong-based auditors of U.S.-listed firms. Under the provisions of the 2022 audit agreement, Chinese authorities must allow PCAOB investigators complete access to unredacted audit work papers and the ability to interview personnel of audit firms located in the People's Republic of China (PRC) and Hong Kong.

The PCAOB's 2022 determination does not guarantee it will be able to inspect and investigate auditors headquartered in China and Hong Kong in the future. Chinese regulators could abrogate the audit agreement and impede or obstruct future inspections. The CSRC emphasized in a statement in August 2022 that the agreement "complies with the laws and regulations and regulatory requirements of both parties." As Chinese law requires documents and interview requests to be arranged by the CSRC on behalf of U.S. investigators, Chinese regulators could restrict the level of access provided to the PCAOB.

### **Variable Interest Entity**

Based on 2023 annual report filings, 161 Chinese companies listed on the three major U.S. exchanges use a Variable Interest Entity (VIE). These companies account for a market capitalization of \$910 billion as of January 9, 2023—89 percent of the total market capitalization of Chinese firms listed on U.S. exchanges. The VIE structure is a legal and financial arrangement commonly employed by Chinese firms, particularly those in the technology and internet sectors, to facilitate foreign investment and overseas listings. Due to regulatory restrictions on foreign ownership in certain industries in China, the VIE structure allows Chinese companies to establish an offshore entity, typically in a tax-friendly jurisdiction, which holds the licenses and permits required to operate the restricted business. This offshore entity, often structured as a VIE, enters into contractual arrangements with the Chinese operating company, giving the offshore investors economic interests and control rights without direct ownership.

In a VIE structure, investors in the foreign entity essentially hold contractual rights to the profits and assets of the Chinese company rather than direct equity ownership. This structure raises legal and regulatory concerns, as it involves a level of financial and operational risk. The Chinese government has periodically expressed concerns about the potential legal challenges and regulatory uncertainties associated with VIE structures. Despite these concerns, many Chinese firms have successfully utilized the VIE structure to attract foreign investment and access global

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<sup>17</sup> Under the HFCAA, the SEC must impose a trading prohibition on issuers that it has identified for two consecutive years as retaining an auditor from a noncompliant jurisdiction. With the PCAOB vacating its HFCAA determination on mainland China and Hong Kong, issuers that were notified by the SEC for using noncompliant auditors in their fiscal year 2021 financial statements may regain compliance with the HFCAA after filing their fiscal year 2022 annual reports

capital markets, enabling them to expand their operations and enhance their competitiveness on the international stage. As regulations and policies evolve, it is essential for investors and companies alike to stay informed about potential changes that may impact the use of the VIE structure for Chinese firms. Since July 2021, the SEC has imposed additional disclosure requirements for Chinese companies using a VIE to sell shares in the U.S.<sup>18</sup>

### **Other Risks/Issues**

Since the end of the first quarter of 2022, the NYSE and the NASDAQ delisted 13 companies for violating the standards for continued listing on their respective exchanges, while another 61 Chinese issuers with a combined market capitalization of \$3.0 billion have received notice from the NYSE or NASDAQ as of January 9, 2023 that their listed securities are non-compliant. Most of these companies failed to comply with the requirement to keep the bid price for their shares above a specified minimum, a reflection of the dramatic decline in the value of Chinese issuers over the past few years. If these notified companies fail to regain compliance, they may face removal from the exchange.

On July 6, 2021, the General Offices of the Chinese Communist Party (CCP) Central Committee and State Council jointly issued the *Opinions on Strictly Cracking Down on Illegal Securities Activity in Accordance with Law*, which pledge to strengthen supervision of Chinese companies issuing securities overseas by, among other things, enhancing data security protection and oversight of cross-border data flows. The Chinese government's focus on data security for overseas-listed firms is underlined in rules from the Cyberspace Administration of China (CAC), co-issued with CSRC and several other agencies. Effective February 2022, the rules require mandatory review for any company collecting personal information of more than one million users before new overseas listings.

Investors in Chinese companies may support activities that are contrary to U.S. national interests, including the development of technology used for censorship and surveillance and in support of the military. China's 2017 National Intelligence Law states that "any organization or citizen shall support, assist, and cooperate with state intelligence work," and the 2017 Cybersecurity Law requires companies to "provide technical support and assistance to public security organs."

## **DATA AND METHODOLOGY**

As of January 2023, there were 252 Chinese companies listed on these U.S. exchanges with a total market capitalization of \$1.03 trillion.<sup>19</sup> We obtained a list of all 252 firms from a report by the U.S.–China Economic and Security Review Commission (<https://www.uscc.gov/research/chinese-companies-listed-major-us-stock-exchanges>). We limit our sample to firms with a market capitalization of at least \$100 million and have their

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<sup>18</sup> For further details of VIE structures please see <https://www.sec.gov/oiea/investor-alerts-and-bulletins/investor-bulletin-us-listed-companies-operating-chinese>

<sup>19</sup> Please see <https://www.uscc.gov/research/chinese-companies-listed-major-us-stock-exchanges> for further details and information about U.S. listed Chinese firms.

equity data available via the Center for Research in Security Prices (CRSP) database, which yields a sample of 110 firms. Table 1 provides a breakdown of these firms by industry and average market capitalization. We then select eight major U.S.–China events, beginning with the Inauguration of President Donald Trump on January 20, 2017, and ending with the World Trade Organization (WTO) ruling that the U.S. was in breach of global trade rules on December 9, 2022.

The eight events selected for this study were chosen because they represent critical turning points in the evolution of China–U.S. relations from 2017 to 2022. Each event had the potential to significantly influence investor sentiment, policy expectations, and market behavior due to its economic, political, or diplomatic implications.

1. **Policy Shifts and Trade Actions:** Events such as President Trump's inauguration, the Section 301 investigation, the announcement of tariffs, and the currency manipulator designation marked key moments in the escalation of the U.S.–China trade war. These announcements had direct implications for trade volumes, corporate earnings, and global supply chains.
2. **Market-Influencing Agreements:** The signing of the Phase One trade deal represented a temporary de-escalation and a shift toward negotiation, with immediate consequences for sectors like agriculture, manufacturing, and finance.
3. **Financial Market Restrictions:** The executive order banning investments in Chinese military-linked firms and its downstream effects on U.S. capital markets exemplify the intersection of national security concerns and financial regulation.
4. **Leadership Transitions and Strategic Signaling:** The inaugurations of Biden and Trump, serve as signals of potential policy continuity or change, influencing expectations around trade, tariffs, and diplomacy.
5. **Legal and Institutional Developments:** The 2022 WTO ruling challenges the legitimacy of past U.S. tariffs, which may impact future trade negotiations and compliance with global norms.

Together, these events span a range of trade, investment, currency, and diplomatic dimensions. They were chosen for their clear documentation, public visibility, and likelihood of triggering measurable market reactions, making them highly suitable for an event study focused on assessing the impact of geopolitical developments on economic and financial variables. Table 2 provides a full list of dates and events that we use in our study. While we recognize that many events have shaped the China–U.S. relationship, the authors have identified these eight events as the most significant based on their economic and geopolitical impact; a more comprehensive timeline of key events can be found at: <https://www.cfr.org/timeline/us-china-relations>.

**Table 1: Firms by Industry and Average Market Capitalization**

Sector	# of Firms	Average Market Cap (US\$ mil)
Technology	39	12637
Finance & Real Estate	19	2112
Consumer Services	17	11453
Health Care	16	4796
Business Services	12	7845
Other	7	5212
Total	110	9160

**Table 2: Major U.S.–China Related Events**

Date	Event
2017-01-20	President Donald Trump Inauguration Day
2017-08-18	Trump directed the Office of the United States Trade Representative (USTR) to investigate Chinese economic practices
2018-03-22	Trump asked the United States Trade Representative (USTR) to investigate applying tariffs on US\$50–60 billion worth of Chinese goods. He relied on Section 301 of the Trade Act of 1974 for doing so, stating that the proposed tariffs were "a response to the unfair trade practices of China over the years", including theft of U.S. intellectual property. Over 1,300 categories of Chinese imports were listed for tariffs, including aircraft parts, batteries, flat-panel televisions, medical devices, satellites, and various weapons.
2019-08-05	The U.S. Department of Treasury officially declared China as a Currency Manipulator after the People's Bank of China allowed its yuan to depreciate that, according to CNN, was seen as retaliation to Trump's August 1 tariff announcement. According to an article in <i>The Washington Post</i> , Trump reportedly pressured the Treasury Department Steven Mnuchin to authorize the designation. Both the IMF and the Chinese government have rejected the designation, with the IMF saying that the valuation of the yuan is in line with China's economic fundamentals. Also, on August 5: China ordered state-owned enterprises to stop buying U.S. agricultural products.
2020-01-15	U.S. President Donald Trump and China's Vice Premier Liu He signed the U.S.–China Phase One trade deal in Washington DC. The "Economic and Trade Agreement between the United States of America and the People's Republic of China" is set to take effect from February 14, 2020, and focuses on intellectual property rights (Chapter 1), technology transfer (Chapter 2), food and agricultural products (Chapter 3), financial services (Chapter 4), exchange rate matters and transparency (Chapter 5), and expanding trade (Chapter 6), with reference also being made to bilateral evaluation and dispute resolution procedures in Chapter 7.

2020-11-08	President Donald Trump signed an executive order prohibiting Americans from investing in shares of companies with ties to the Chinese military. New transactions would be barred from 11 January 2021, while investors that already held such stocks would have until November 2021 to divest them. On 6 January 2021, the New York Stock Exchange announced that it would delist stocks related to China Mobile, China Telecom and China Unicom. Index provider MSCI also announced it would stop including China Mobile, China Telecom and China Unicom in its benchmarks.
2021-01-20	Trump left office and Joe Biden was inaugurated as president of the United States. Biden said that he did not have immediate plans to remove the tariffs and planned to review the phase one trade deal and discuss the matter with allies first.
2022-12-09	The WTO ruled that former U.S. President Donald Trump was in breach of global trade rules in 2018 with his administration's tariffs on steel and aluminum. The Biden administration however disputed the panel's rulings and instead stated that they will not take away the duties that Trump had earlier established
2023-07-06	The US Treasury Secretary Janet Yellen visited Beijing, During her four-day visit, Yellen met several top Chinese officials, including Premier Li Qiang, Vice Premier He Lifeng, Minister of Finance Liu Kun, and the Deputy Governor of the People's Bank of China Pan Gongsheng. Yellen stated that the objective of her trip was to "establish and deepen relationships with the new economic leadership team in place in Beijing"
2023-11-15	Chinese President Xi Jinping and US President Joe Biden held their first face-to-face meeting in a year in San Francisco. This is only the second time the two leaders have met during Biden's term as president. According to Biden, the meeting was "among the most constructive and productive we've had", and resulted in the establishment of several areas of cooperation, including artificial intelligence governance, counternarcotics, and defense, as well as commitments to improving transport links and expanding educational and cultural exchanges between the two countries.

The objective of an event study is to assess the extent to which investors earn excess or abnormal stock returns from an event that carries new informational content, where an abnormal return is the difference between the observed return and the return expected in the absence of the event. Underlying this methodology is a semi-strong form of market efficiency, which makes two assumptions. First, stock prices reflect all publicly available information. Second, stock prices instantly change to reflect new information when it becomes available (Fama 1991). Under these assumptions, investors use the new information contained in an announcement to instantly adjust their expectations of the firm's future cash flows. As a result, the price of the firm's stock changes to account for these new expectations; the change captures the value-added associated with the new information contained in the announcement.

The seminal reference for short-term event studies is Brown and Warner (1985), who examine the statistical properties of abnormal returns computed using daily data. We apply a standard event study with the following parameters: The event is defined as the dates outlined in Table 2. Our estimation period of 100 daily returns ends 50 trading days before the event day. Our event window ranges from -2 to +5 days around the event day (Day 0). We estimate daily abnormal stock returns for each firm during the event period using the Fama and French (1993) three-factor model supplemented with the momentum factor (Carhart, 1997). We follow the

common event study approach and define average abnormal returns (AR) of a specific day of a portfolio of stocks as the average of the abnormal stock returns on this day. The cumulative average abnormal return (CAR) is the sum of the AR over a certain period of time. We show the statistical significance of the results using t-tests.<sup>20</sup> We consider a firm's current stock price as the value investors attribute to the future profitability of a firm. A positive (negative) CAR indicates that the firm's stock price increased (decreased) more than the stock price of a comparable firm. According to the price-building mechanisms in capital markets, a higher (lower) stock price indicates that more (less) investors show demand for the firm, possibly due to the belief that the firm's profitability has increased (decreased).

## EMPIRICAL RESULTS AND DISCUSSION

Figure 2 provides the CARs graphs for the ten events outlined in Table 2. The figures suggested that Chinese firms listed on U.S. exchanges experienced significant positive outperformance during the week of President Biden's Inauguration and when the WTO ruled that the U.S. was in breach of global trade laws. The tables associated with these figures (available in the online appendix) indicated that the CARs (-2/+5) for the period surrounding the WTO ruling were 8.8%. The majority of positive performance was on day t-1 (5.01%) and day 0 (2.85%). This suggests that the ruling was likely leaked in the days prior to the public announcement and that investors absorbed this information as positive news for these firms' future profitability and cash flows. The CARs for the period surrounding President Biden's Inauguration (-2/+5) were 5.96%, perhaps reflecting an expectation that President Biden will take a different approach toward China from the one taken by President Trump. Similar to the WTO ruling, the majority of these returns were on days t-1 (3.77%) and t+1 (1.89%). It is important to note that these two events are the two events in our study when President Donald Trump was no longer in office.

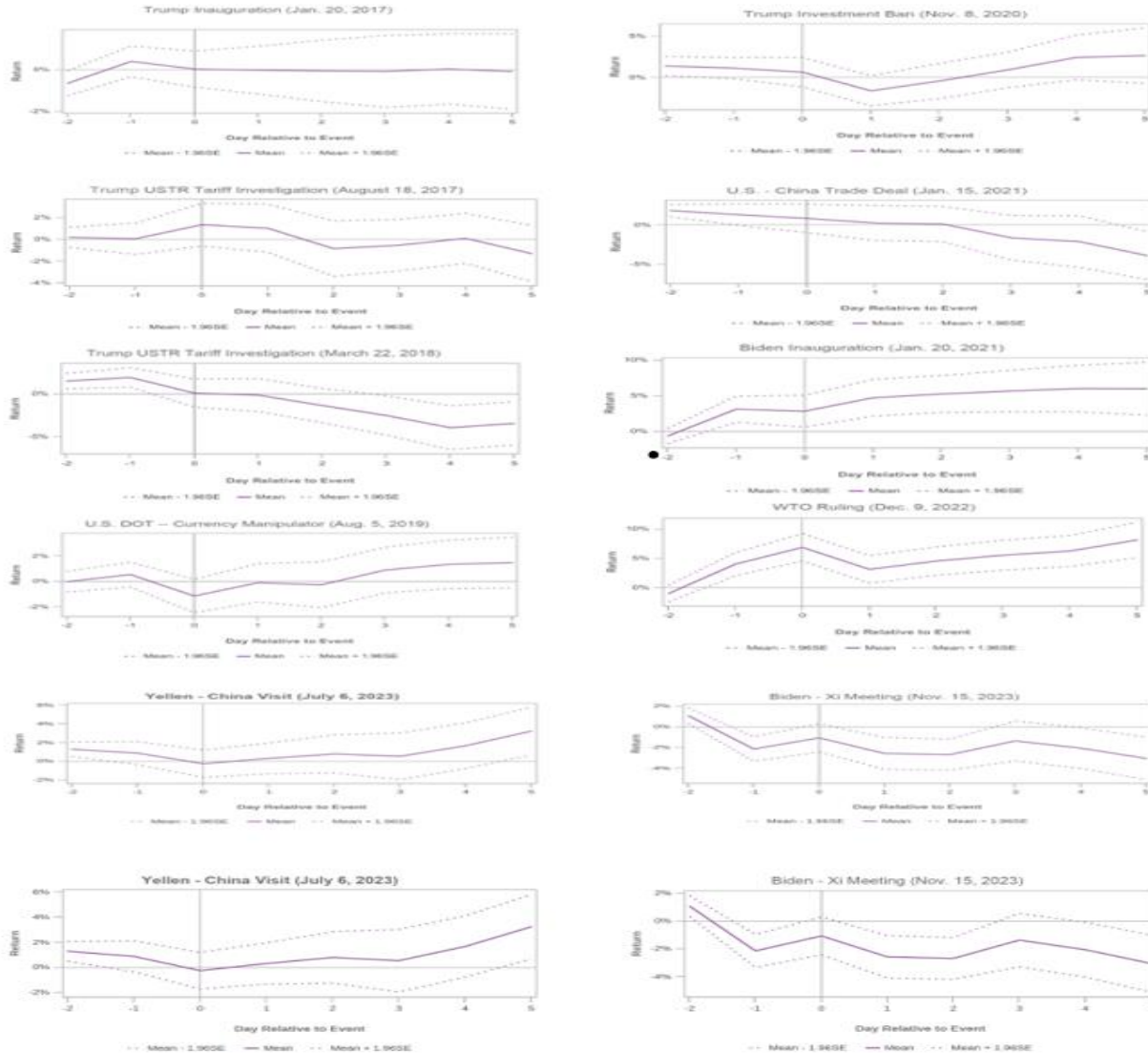
The first USTR event (directive from President Trump to begin an investigation) shows little impact on our sample of firms. The second USTR event/announcement on March 3, 2018, resulted in a negative price movement for U.S.-listed Chinese companies. The majority of these negative downward movements happened on days t+2 (-1.22%), t+3 (-1.15%), and t+4 (1.42%). The CARs for the -2/+5 window was -3.47%. The day the U.S. Department of Treasury officially declared China as a currency manipulator (August 5, 2019) resulted in a day 0 abnormal return of -1.69%, but over the next week of trading, this significant reaction was reversed in a CAR (-2/+5) of 1.46% (not statistically significant). Finally, the U.S. – China Trade Deal announcement had little impact on days t-1 to t+2, but overall the CAR was negative in the -2/+5 day window with significant negative returns on days t+3 and t+5. The executive order issued by President Trump prohibiting Americans from investing in shares of companies

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<sup>20</sup> Please see Corrado (2011) for a full review of event study methodology. Due to space considerations we limit the discussion of the methodology. Please note we run several other models (e.g., market, market-adjusted, Fama-French Three Factor) and the results do not significantly change. Further additional unreported results show that our findings are robust to test statistics such as the Patell test (Patell, 1976), the Adjusted Patell test (Kolari and Pynnonen, 2010), and the Wilcoxon signed-ranks test (Wilcoxon, 1992). We also conduct analysis with varying time windows. These results are available upon request.

with ties to the Chinese military had an immediate negative impact ( $t+1 = -2.26\%$ ), but investors quickly reversed this sell-off in the following days.

**Figure 2: Fama-French Plus Momentum Model**



The results of this study suggest that investors in U.S.-listed Chinese stocks often exhibit an “overreaction” that quickly is reversed in the following week of trading. This is particularly true for the events initiated by President Trump (USTR events and executive order). Bessembinder, et al. (2021), Assess, et al. (2023), and Cotter and Kobor (2023) all provide evidence of the strong performance and benefits of international equity diversification for investors. The results of our study supplement these studies and suggest that U.S. market participants absorb information quickly but sometimes overreact. Investors in U.S.-listed Chinese shares must understand these firms' increased risk and ensure that proper diversification techniques are employed to reduce single-event risks.

### Additional Analysis -- U.S. Firms with Exposure to China

We extend our study to explore whether U.S. firms with significant exposure to China experience significant impacts during some of these major U.S.–China political and trade announcements. Table 3 provides a list of 10 U.S. firms with the most exposure to China (based on revenue percentage). As shown in Chen, Fang, and Liu (2023), it is the exposure to exporting to the Chinese market that matter the most. It is important to note that disclosure of U.S. firms to China is limited in many cases. In 2023, Jay Clayton, former chairman of the Securities and Exchange Commission, proposed that large U.S. companies with significant exposure to China should be required to disclose to investors the extent of their exposure to China and the expected effects on operations and business of a substantial disruption to U.S.-China relations. Mr. Clayton proposed establishing a disclosure program that would apply to companies with a market capitalization greater than \$50 billion or \$100 billion, with at least \$10 billion in revenue or costs in China, or would have material impacts if their China business ceased.<sup>21</sup>

**Table 3: S&P 500 Companies with the most Revenue Exposure to China**

Ticker	Name	China % of Revenue	Sector	Market Cap. (US\$ mil)
QCOM	Qualcomm	63.6	Information Technology	174,001
MPWR	Monolithic Power Systems	52.3	Information Technology	27615
TXN	Texas Instruments	49.2	Information Technology	170887
NXPI	NXP Semiconductors	35.6	Information Technology	51845
AVGO	Broadcom	35.0	Information Technology	854235
VTRS	Viatis	33.1	Healthcare	1245
ALB	Albemarle	33.0	Materials	9124
GLW	Corning	30.0	Information Technology	40121
AMAT	Applied Materials	28.1	Information Technology	132457
ON	ON Semiconductor	27.8	Information Technology	19774

Figure 3 provides a visual of the impact that two events have on these firms.<sup>22</sup> In both of these events, little statistical significance is shown in either the A.R. or CAR during the -2/+5 day window. These suggest that U.S. firms with significant exposure to China are likely “insulated” from these events. This may be because many investors may not be aware of the

<sup>21</sup> See <https://www.wsj.com/articles/big-businesses-should-disclose-china-risks-ex-sec-chairman-says-68e67fb6> for further details.

<sup>22</sup> Please note we produce only figures for the event on August 5, 2019 (currency manipulator), which also corresponds with China ordering state-owned enterprises to stop buying US agricultural products, and January 15, 2020 (U.S. – China Trade Deal), as these are theoretically two events that would have more impact on U.S. based firms. We conduct tests on all the events but due to space considerations and little statistical significance we do produce these results in the manuscript but are available upon request.

significant exposure that some of these firms have to China, which may change if a new regulation is brought forward to require firms to disclose their Chinese exposure.

### **Additional Event – Nancy Pelosi’s Visit to Taiwan**

Visits by U.S. officials to Taiwan have been a point of contention between the U.S. and China due to the "One China" policy, which recognizes the People's Republic of China as the sole legitimate government of China. Any high-profile visit by a U.S. leader to Taiwan strains U.S.-China relations. Nancy Pelosi, the former Speaker of the U.S. House of Representatives, visited Taiwan on August 2, 2022. A delegation of five [Democratic Party](#) members of the House accompanied Pelosi on the visit. President Joe Biden initially cautioned against the reported trip on July 20, 2022, saying the US military had assessed "it is not a good idea right now". However, on August 1, White House national security spokesman John Kirby said that Pelosi had the right to visit Taiwan, adding that the United States would not be intimidated by China's expected escalation in response to the potential trip. The People's Republic of China had strongly condemned the visit and called the visit a "provocation" by the US that "seriously infringes upon China's sovereignty". In a telephone meeting between US President [Joe Biden](#) and PRC leader [Xi Jinping](#) the week before, the [PRC government](#) warned the US to abide by the [One China](#) principle, that "those who play with fire will perish by it", and that the US would be "playing with fire" if Biden were to allow Pelosi to visit Taiwan.

From the statements above, we can see tensions were high between the two countries during this time. Figure 4 provides a visual of U.S. listed Chinese firms' reaction during the -2/+5 day window. As the figure shows, this event caused investors to sell off these Chinese-domiciled securities significantly. The CAR from day -2 to day +4 reached close to -15%. This evidence suggests that investors in U.S.-listed Chinese stocks need to be aware of the potential asset pricing risk these equities are exposed to and closely monitor the China-Taiwan relationship.

Figure 3: U.S. Firms Reactions with Fama-French Plus Momentum Model

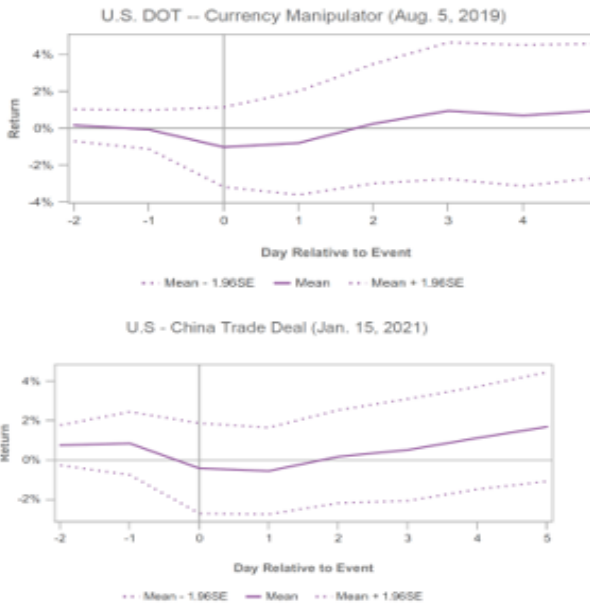
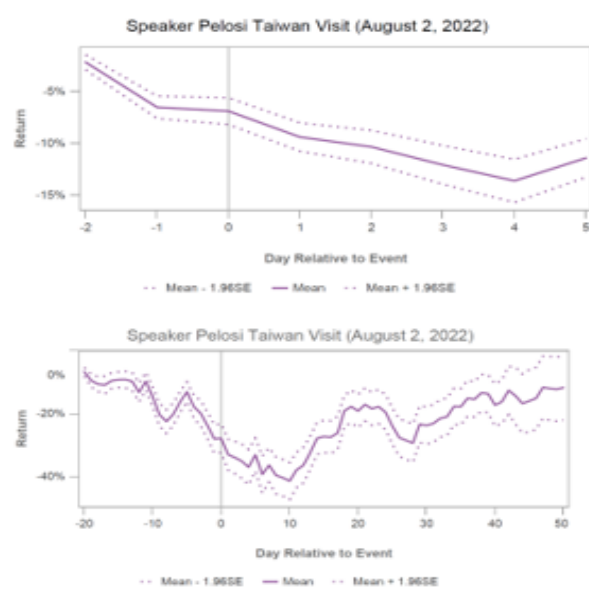


Figure 4: Speaker Pelosi's Taiwan Visit with Fama-French Plus Momentum Model



In addition to the -2/+5 event study, we provide a longer-term view of the behavior of U.S.-listed Chinese equities in and around Speaker Pelosi’s visit to Taiwan in August 2022. The second visual in Figure 4 provides evidence that up to 40% of the value of U.S.-listed Chinese shares was lost in the -20 to +10 window surrounding the event. A significant portion of this value was recovered in the weeks following this window, but portfolio managers and investors need to be aware of the significant impacts that U.S. policy decisions (and the approach) related to Taiwan could have on the asset prices of Chinese firms. A recent publication by Forbes suggested that in 2018, U.S. investors purchased more than a \$17 billion new investment in Chinese stocks and bonds. This net flow rose to \$36 billion in 2020 and steadied at \$20 billion in 2021. In 2022, new portfolio investment slowed and through October 2023, there has been a net outflow of \$31 billion dollars.<sup>23</sup>

### CONCLUSION

With high trade policy uncertainty, trade conflicts, and political posturing between U.S. and China, investors need to understand the impact these events have on asset prices – both short-run and long-run. Further, demand for Chinese financial assets continues to grow even in times of U.S. – China trade disputes due to the positive diversification effects for U.S. investors. Work by He et al. (2021), Yu et al (2023) and others have provided some evidence of trade

<sup>23</sup> <https://www.forbes.com/sites/miltonezrati/2024/01/01/american-investors-say-no-to-china/?sh=4f7088cc1741>

uncertainty's impact on U.S. and Chinese stock markets using a trade policy uncertainty index. Generally, the results suggest that U.S. and China trade conflicts positively affect the U.S. stock market while negatively affecting the Chinese stock market. This study extends this research using an event study methodology utilizing individual data of equity prices of U.S.-listed Chinese firms.

This research finds that particular political and trade events result in significant short-run abnormal returns in and around the event date. Our results indicate that U.S. market often exhibit an overreaction to the announcements or events, in which a sell-off is quickly reversed and losses recovered in a short window of -2/+5 days. Thus,

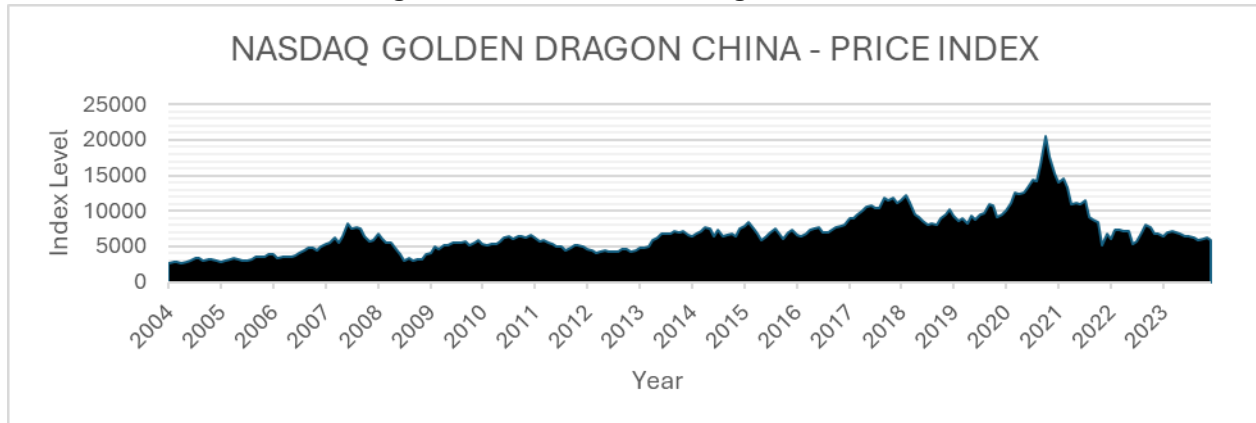
On the other hand, for the long-run scenario, investors may want to be conscious about how they diversify with Chinese equities and make sure they don't have an outside position in any particular name. It is important to note that several U.S.-listed Chinese companies are in danger of being removed from U.S. stock exchanges starting in 2024 under the Holding Foreign Companies Accountable Act of 2020.<sup>24</sup>

U.S. investors face several risks when investing in Chinese stocks, primarily due to differences in regulatory environments, accounting practices, and legal frameworks between the two countries. One notable concern is the lack of transparency and oversight in certain Chinese companies, as regulatory constraints may hinder U.S. regulators' access to audit records and financial information. The VIE structure, commonly employed by Chinese firms, adds another layer of complexity and legal ambiguity, as it relies on contractual arrangements rather than direct ownership. Additionally, geopolitical tensions and trade disputes between the U.S. and China can introduce uncertainties that impact the performance of Chinese stocks. Changes in Chinese government policies, currency fluctuations, and the potential for fraud or corporate governance issues are additional risks that investors need to consider carefully. While investing in Chinese stocks can offer diversification and growth opportunities, U.S. investors must conduct thorough due diligence, stay informed about regulatory developments, and be aware of the unique risks associated with investments in Chinese domiciled stocks. As an illustration of the overall U.S. based investor appetite for Chinese equities, Figure 5 provides a visual of the NASDAQ Golden Dragon China Index is a modified market capitalization weighted index comprised of companies whose common stock is publicly traded in the United States and the majority of whose business is conducted within the People's Republic of China.<sup>25</sup> It is evident that since 2021, there has been a remarkable decline in the asset prices of these Chinese firms which has a strong correlation with the trade and investment policy uncertainty between the two countries.

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<sup>24</sup> See <https://www.sec.gov/hfcaa> for further details

<sup>25</sup> The Index is designed to provide insight and access to the unique economic opportunities taking place in China while still providing the transparency offered with U.S. listed securities.

**Figure 5: NASDAQ Golden Dragon China Price Index**

Finally, investors need to weigh the outcome of political events on the relationship between the U.S. and China. On January 13, 2024, Taiwan held elections for its presidency and 113-seat legislature, the Legislative Yuan. The run-up to the election drew global attention because of the growing tensions in the Taiwan Strait. Since current president Tsai Ing-wen was elected in 2016, official cross-strait dialogue has been suspended, and there is deep concern about China's growing use of "gray zone" tactics and the rising possibility of actual hostilities. With the elections now concluded and Democratic Progressive Party (DPP) candidate William Lai winning, all eyes are on the ongoing transition, which will culminate in Lai's inauguration on May 20, 2024. In addition to the election in Taiwan, the 2024 United States presidential election is scheduled for November 5, 2024. Incumbent President [Joe Biden](#), is running for re-election and his predecessor, [Donald Trump](#), re-election to a second nonconsecutive term will likely alter foreign policy stances related to the Asia-Pacific region. Global investors need to be aware of the foreign policy and regulatory-related risks that Chinese domiciled equities have. Future research on U.S. firms listed in China and Chinese firms listed in the U.S. will likely examine the impact of evolving regulatory frameworks, such as China's tightened data security laws and the U.S. Holding Foreign Companies Accountable Act. Additionally, scholars may focus on the financial performance, investor sentiment, and geopolitical risks influencing cross-border listings, particularly in light of U.S.-China tensions and delisting threats. Additional granular evaluation on an industry level is also an area in which future research can be explored, particularly in the technology sector with focused regulatory/foreign relations changes related to technology and ownership of foreign firms.

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## APPENDIX

**Table 3: Fama – French + Momentum Model**

	Days	Abnormal Return	T-Stat (A.R.)	Cumulative Abnormal Return	T-Stat (CAR)
Trump Inauguration (Jan. 20, 2017)	-2	-0.0066	-2.1896**	-0.0066	-2.1896**
	-1	0.0105	4.1278***	0.0039	1.0293
	0	-0.0037	-1.4676	0.0002	0.0441
	1	-0.0005	-0.1225	-0.0003	-0.0534
	2	-0.0004	-0.0999	-0.0007	-0.0917
	3	-0.0003	-0.0614	-0.0009	-0.1070
	4	0.0012	0.3984	0.0002	0.0279
	5	-0.0012	-0.3418	-0.0010	-0.1067
Trump USTR Investigation Announcement (Aug. 18, 2017)	-2	0.0017	0.3554	0.0017	0.3554
	-1	-0.0012	-0.2266	0.0005	0.0640
	0	0.0129	2.3389**	0.0134	1.3354
	1	-0.0032	-0.5630	0.0101	0.8900
	2	-0.0188	-1.8802*	-0.0087	-0.6671
	3	0.0032	0.6928	-0.0055	-0.4510
	4	0.0063	1.2635	0.0008	0.0684
	5	-0.0141	-3.1050***	-0.0133	-1.0061
Trump USTR Tariff	-2	0.0146	3.1869***	0.0146	3.1869***

Investigation 22, 2018)	(Mar.	-1	0.0041	0.8812	0.0187	3.2079***
		0	-0.0181	-3.0249***	0.0006	0.0660
		1	-0.0023	-0.5980	-0.0018	-0.1800
		2	-0.0122	-1.7105*	-0.0139	-1.3738
		3	-0.0115	-2.1194**	-0.0255	-2.1872**
		4	-0.0142	-3.3133***	-0.0397	-3.0510***
		5	0.0050	1.1100	-0.0347	-2.7149**
		-2	-0.0004	-0.1011	-0.0004	-0.1011
		-1	0.0056	1.6445	0.0051	1.0300
U.S. Department of Treasury officially declared China as a Currency Manipulator (Aug. 5, 2019)		0	-0.0169	-3.2140***	-0.0117	-1.7586*
		1	0.0104	2.7201**	-0.0013	-0.1662
		2	-0.0016	-0.3461	-0.0029	-0.3120
		3	0.0116	3.0450***	0.0087	0.9492
		4	0.0045	1.6430	0.0132	1.3564
		5	0.0013	0.3714	0.0146	1.4280
			-2	0.0179	4.4931***	0.0179
		-1	-0.0053	-0.9968	0.0127	1.8327
U.S. - China Trade Deal Announcement 15, 2020)	(Jan.	0	-0.0047	-1.0253	0.0080	0.8636
		1	-0.0059	-0.9570	0.0021	0.1890
		2	-0.0013	-0.4132	0.0008	0.0717
		3	-0.0175	-2.9564**	-0.0167	-1.1520
		4	-0.0048	-0.8546	-0.0215	-1.2859
		5	-0.0178	-3.8874***	-0.0393	-2.5403**
			-2	0.0134	2.2557**	0.0134
		-1	-0.0026	-0.5879	0.0108	1.6310
Trump Investment Ban Announcement (Nov. 8, 2020)		0	-0.0049	-0.6415	0.0059	0.6452
		1	-0.0226	-4.1080***	-0.0168	-1.7982
		2	0.0119	2.6526**	-0.0048	-0.4413
		3	0.0135	2.4793**	0.0087	0.7860
		4	0.0152	2.6701**	0.0239	1.7224*
		5	0.0022	0.3209	0.0260	1.5115
			-2	-0.0069	-1.2775	-0.0069
		-1	0.0377	4.3886***	0.0308	3.2960***
Biden Inauguration (Jan. 20, 2021)		0	-0.0028	-0.5444	0.0279	2.4593**
		1	0.0189	2.9080**	0.0468	3.5631***
		2	0.0053	1.1744	0.0521	3.9531***
		3	0.0040	0.7753	0.0562	3.7830***
		4	0.0035	0.5138	0.0597	3.5796***
		5	-0.0001	-0.0170	0.0596	3.1422***
			-2	-0.0104	-1.4421	-0.0104
WTO Ruling	(Dec.					

9, 2022)	-1	0.0501	8.0543***	0.0397	3.9290***
	0	0.0285	4.1585***	0.0682	5.7579***
	1	-0.0374	-5.9462***	0.0308	2.5808**
	2	0.0140	3.3066***	0.0449	3.6590***
	3	0.0100	2.4431**	0.0549	4.2244***
	4	0.0071	1.4409	0.0620	4.6039***
	5	0.0188	2.7325***	0.0808	5.2653***

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\*10% significance, \*\*5% significance, \*\*\*1% significance.