CHAPTER 2

BEIJING’S INTERNAL AND EXTERNAL CHALLENGES

Key Findings

• The Chinese Communist Party (CCP) is facing internal and external challenges as it attempts to maintain power at home and increase its influence abroad. China’s leadership is acutely aware of these challenges and is making a concerted effort to overcome them.

• The CCP perceives Western values and democracy as weakening the ideological commitment to China’s socialist system of Party cadres and the broader populace, which the Party views as a fundamental threat to its rule. General Secretary Xi Jinping has attempted to restore the CCP’s belief in its founding values to further consolidate control over nearly all of China’s government, economy, and society. His personal ascendancy within the CCP is in contrast to the previous consensus-based model established by his predecessors. Meanwhile, his signature anticorruption campaign has contributed to bureaucratic confusion and paralysis while failing to resolve the endemic corruption plaguing China’s governing system.

• China’s current economic challenges include slowing economic growth, a struggling private sector, rising debt levels, and a rapidly-aging population. Beijing’s deleveraging campaign has been a major drag on growth and disproportionately affects the private sector. Rather than attempt to energize China’s economy through market reforms, the policy emphasis under General Secretary Xi has shifted markedly toward state control.

• Beijing views its dependence on foreign intellectual property as undermining its ambition to become a global power and a threat to its technological independence. China has accelerated its efforts to develop advanced technologies to move up the economic value chain and reduce its dependence on foreign technology, which it views as both a critical economic and security vulnerability.

• China’s senior leaders are concerned over perceived shortfalls in the People’s Liberation Army’s (PLA) warfighting experience and capabilities and its failure to produce an officer corps that can plan and lead. These concerns undermine Chinese leaders’ confidence in the PLA’s ability to prevail against a highly-capable adversary. The CCP has also long harbored concerns over the loyalty and responsiveness of the PLA and internal security
forces to Beijing and the potential for provincial officials to co-opt these forces to promote their own political ambitions.

- China’s Belt and Road Initiative (BRI) faces growing skepticism due to concerns regarding corruption, opaque lending practices, and security threats. However, this criticism has not been followed by an outright rejection of BRI because significant infrastructure gaps persist globally and China has few competitors in infrastructure financing.

- Beijing’s military modernization efforts, coercion of its neighbors, and interference in other countries’ internal affairs have generated resistance to its geopolitical ambitions. Countries in the Indo-Pacific and outside the region are accelerating their military modernization programs, deepening cooperation, and increasing their military presence in the region in an attempt to deter Beijing from continuing its assertive behavior.

**Recommendations**

The Commission recommends:

- Congress provide resources for programs that support independent media and the free flow of information to prioritize Indo-Pacific countries in their efforts to counter China’s influence and propaganda efforts.

- Congress require the relevant departments and agencies of jurisdiction—including the U.S. Department of the Treasury, the U.S. Department of Commerce, and the U.S. Securities and Exchange Commission—to prepare a report to Congress on the holdings of U.S. investors in Chinese bonds and other debt instruments. Such a report shall include information on the direct, indirect, and derivative ownership of any of these instruments.

- Congress require the U.S. Department of the Treasury to prepare a report to Congress on the operation of China’s Cross-Border International Payment System. As part of such a report, the department shall include information on the extent to which the Cross-Border International Payment System could be used to bypass international sanctions regimes.

**Introduction**

In his address to the 19th National Congress of the CCP in October 2017, General Secretary Xi announced that China was approaching the “world’s center stage” and was closer than at any point in its modern history to realizing the “great rejuvenation of the Chinese nation.” He declared China would no longer tolerate opposition to its rise, warning that “no one should have the fantasy of forcing China to swallow the bitter fruit of damaging its own interests.” General Secretary Xi also pointed to China’s uncertain domestic and international situation, noting that China is in the midst of “profound and complex changes [and] an important period of strategic opportunity for development” in which “the prospects are bright, but the challenges are severe.” He went on to describe a litany of challenges affecting nearly every aspect of Chinese governance and society, from cadre corruption to slowing economic growth, weak in-
novative capacity, environmental degradation, ethnic tensions, and insufficient military capability and preparedness.\(^4\)

As tensions have risen in the U.S.-China relationship and between China and countries from the Indo-Pacific to Europe, the challenges facing Beijing have become only more acute and the pressure on the CCP to resolve them even greater. Increasingly negative perceptions of Beijing in Taiwan and Hong Kong have lent these challenges an even greater sense of urgency. (For more on Taiwan and Hong Kong developments, see Chapter 5, “Taiwan” and Chapter 6, “Hong Kong.”)

This chapter examines the many challenges facing the CCP in its efforts to maintain its hold on power, develop China's economy, and promote its influence in the region and in global affairs. It also notes the determined efforts and some of the notable progress the CCP has made in addressing these challenges. The chapter begins by assessing the CCP's internal challenges that have driven General Secretary Xi to consolidate his power over the Party and the CCP's control over the Chinese state. It then reviews the economic, technological, and innovation challenges that continue to plague China. Finally, the chapter surveys the limitations Beijing faces in extending its political, economic, and military influence abroad, and concludes with a discussion of the implications of these vulnerabilities for the United States. This chapter is based on the Commission’s February 2019 hearing on the topic, the Commission’s May trip to the Indo-Pacific, and open source research and analysis.

**Internal Challenges to CCP Rule**

In the years leading up to General Secretary Xi’s elevation to power in 2012, CCP leadership had grown increasingly concerned over mounting internal dilemmas directly threatening one-party rule, including ideological decay, weakened control and cohesion, widespread corruption, and flagging economic growth.\(^5\) General Secretary Xi came to power with a mandate to address these concerns and proceeded to consolidate his power over the CCP, extend further CCP control over nearly every aspect of the Chinese state and society, and launch a campaign to address corruption and revive the ideological nature of CCP leadership.\(^6\) Despite nearly seven years of efforts, however, significant challenges remain. In some cases, the CCP’s efforts to address its shortcomings have created new vulnerabilities. The CCP continues to focus on what it views as issues of ideology and legitimacy, political cohesion and leadership decision making, and control over the PLA and internal security forces.

**Ideological Decay and the Crisis of CCP Legitimacy**

The CCP perceives Western values and democracy as weakening the commitment of Party cadres and the broader populace to China’s socialist governing system and as a fundamental threat to its rule.\(^7\) General Secretary Xi, whose outlook is profoundly shaped by the fall of the Soviet Union, has made restoring the CCP's belief in its founding values a focus of his leadership.\(^8\) He has repeatedly stated the CCP faces a legitimacy crisis from a loosening of ideological control that has allowed “subversive Western values” to penetrate Chinese politics and society.\(^9\) According to General Secretary Xi, reviving ideological fervor in the CCP and in Chinese society
has become a defining challenge concerning “the life and death of the party, the long-term stability of the country, and the cohesion of the nation.”

Central to this concern is a potential crisis of confidence in Chinese socialism, Marxism, and the CCP’s leadership over China’s political system. General Secretary Xi has argued this crisis was in part brought about by Deng Xiaoping’s move toward market-oriented economic reform. The CCP issued its “Document 9” in April 2013, which ordered officials to guard against seven “false ideological trends, positions, and activities”: Western constitutional democracy; “universal values” of Western freedom, democracy, and human rights; Western-inspired notions of media independence and civil society; pro-market neoliberalism; “nihilistic” views of the CCP’s history; and the “questioning [of] reform and opening and the socialist nature of socialism with Chinese characteristics.”

In its campaign to combat Western influence and restore belief in Chinese socialism, the CCP has increasingly combined nationalism with its socialist message to rally the population around its political leadership. In testimony before the Commission, Jude Blanchette, then a senior advisor to the Crumpton Group, noted that the CCP’s compact with the Chinese population could be described as a “legitimacy meter” with different dials, including economic growth, nationalism, international prestige, and management of U.S.-China relations, which the Party adjusts according to the circumstances. Mr. Blanchette cited the response to the 1989 Tiananmen Square massacre to illustrate the CCP’s use of its legitimacy meter. He said Beijing “dialed up” the message of nationalism under the Patriotic Education Campaign, which stressed the CCP’s role in the struggle for independence from Western influence to redirect the attention of the Chinese population.

Struggles with Intractable Corruption

An active anticorruption campaign has become a hallmark of General Secretary Xi’s administration and is a key component of the CCP’s effort to restore faith in its legitimacy and preserve its one-party rule. General Secretary Xi has also used the campaign to remove potential rivals and silence dissent over his increasingly repressive policies. Few checks on CCP power, combined with wealth-creating opportunities in an increasingly capitalist economy, led to widespread corruption and the weakening of the CCP’s governing legitimacy throughout China’s reform and opening era. Although the CCP has long acknowledged endemic corruption as a central challenge to its legitimacy and periodically launched anticorruption campaigns, the campaign carried out since 2012 has been the most far-reaching.

Despite top leaders’ recent claims that the anticorruption campaign had “built into a crushing tide,” indicators suggest the campaign has failed to overcome the endemic nature of CCP corruption, and may have even worsened the functioning of China’s already cumbersome bureaucracy. The anticorruption campaign has targeted both powerful officials at the top levels of government and lower-level cadres, with the number of targeted officials continuing to climb. From 2013 to 2018, over 2.3 million officials were subjected
to disciplinary action, ranging from dismissals to prosecution and imprisonment. In 2018, 621,000 officials were subjected to disciplinary action, up from 182,000 officials in 2013. Out of those punished in 2018, 51 were “tigers”—officials at or above the provincial or ministerial level.*

Nevertheless, according to Transparency International’s Corruption Perceptions Index, China ranked as corrupt in 2018 as it did in 2012.† In a speech before the 13th National People’s Congress in March 2018, Premier Li Keqiang praised the anticorruption efforts, but also lamented the corruption and formalistic bureaucracy that continued to plague CCP governance. In language suggesting some of these problems had actually worsened in recent years, Premier Li criticized cadres who were “neglectful of their duties,” decried burdensome inspections where “formalities were prioritized over practical results,” and implored the CCP to promote a government that “dares not, cannot, and does not want to be corrupt.” In a July 2019 speech, General Secretary Xi warned that officials should not use the anticorruption campaign as “an excuse for shirking responsibilities or refusing to perform duties.” According to Andrew Wedeman, professor of political science at Georgia State University, the campaign has “also reportedly led to a degree of bureaucratic paralysis because officials fear being accused of corruption,” with ordinary citizens viewing Chinese “officialdom as inherently corrupt and [believing] those who get caught and punished [are] . . . the poor saps who lacked the friends in high places who could have protected them.”

Statements from China’s top leadership criticizing officials for inaction, coupled with media reports of delayed projects and officials avoiding meetings with companies, suggest the anticorruption campaign has led to bureaucratic inertia. According to Yuen Yuen Ang, professor of political science at the University of Michigan, government officials “would rather do nothing and avoid blame than to sign off on initiatives.” For example, in 2015 China’s top auditor found that local officials dragged their feet on implementing $45 billion worth of investment projects, about one-sixth of the total value approved by the National Development and Reform Commission that year.

Beyond targeting corruption, General Secretary Xi has also used the anticorruption campaign to consolidate his power within the CCP by removing potential political threats and controlling dissent. According to Kerry Brown of King’s College London, the campaign has “probably been very useful as a means of clearing away potential, or real, opponents to Xi’s mission,” such as Ling Jihua—the

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*The CCP’s Central Committee, which is typically composed of Party members of provincial or ministerial rank and above, has 205 full members and 171 alternate members. The 51 “tigers” caught in the anticorruption dragnet represent close to one in seven officials at this level. Yu Jie, “The Chinese Communist Party Congress: An Essential Guide,” October 2017, 4.

†Transparency International ranks 180 countries and territories by their perceived levels of public sector corruption according to experts and businesspeople from a scale of 0 to 100, where 0 is highly corrupt and 100 is very clean. China’s 2018 score of 39 placed it 87th out of 180 countries, down from a score of 41 in 2017. When it was ranked 77th out of 180 countries, China received a score of 39 in 2012, placing it 80th out of 174 countries. For comparison, in 2018 the United States received a score of 71, placing it 22nd out of 180 countries. Transparency International, “Corruptions Perceptions Index 2018,” January 2019; Transparency International, “Corruption Perceptions Index 2017,” February 2018; Transparency International, Corruption Perceptions Index 2012,” 2013.
protégé of former CCP leader Hu Jintao—and Bo Xilai, the charismatic and ambitious former Politburo member and CCP chief of the western municipality of Chongqing. A recent working paper by scholars from the University of San Francisco and National University of Singapore concludes that although the campaign’s primary target appears to have been “individuals, networks and geographic regions that departed sharply from meritocratic governance practices,” individuals with personal ties to General Secretary Xi “appear to be exempt from investigation, while individuals with ties to the other six members of the Politburo Standing Committee had no special protection.” These findings suggest the campaign “served both its stated goal of strengthening the party and the unstated goal of consolidating [General Secretary] Xi’s power.”

Centralization of Control and a Weakening of Collective Leadership

General Secretary Xi’s efforts to root out opposition to his leadership are reflective of the CCP’s broader concern over the deterioration of elite cohesion and its control over the state apparatus. Both the Tiananmen Square massacre and the collapse of the Soviet Union caused the CCP to explore the potential causes of regime collapse and determine that an “ossified party-state with a dogmatic ideology, entrenched elites, dormant party organizations, and a stagnant economy would lead to failure.” More recent events, such as the “color revolutions” in Eastern Europe and the Caucasus in the early 2000s, the Arab Spring (2010–2011), Hong Kong’s 2014 “Umbrella Movement,” and Hong Kong’s 2019 anti-extradition bill protests have reinforced these fears.

According to Mr. Blanchette, despite determined efforts to fend off these threats to its own rule, the CCP perceived in recent years that the economic development and collective leadership model it had adopted during the reform and opening era had resulted in rampant corruption, flagging internal discipline, and a breakdown of elite-level cohesion in a Party “replete with competing factions and differing centers of authority.” In particular, the events leading to the rise and eventual purge of Bo Xilai represented “one of the most significant political schisms in the post-Mao period” and a powerful reminder of the potential for a return to that era’s instability or even for a breakdown in CCP rule.
The CCP also judged itself to have ceded too much authority to the State Council in the post-Mao era, hurting its ability to lead domestically and navigate rapidly unfolding changes in the international environment.\textsuperscript{35} To address this perceived challenge, the CCP has launched a sweeping effort to achieve the “Party-ification” of Chinese society and the Chinese state to—in the words of Vice President Wang Qishan—“fundamentally [change] the situation of a weakened Party leadership.”\textsuperscript{36} While attempting to combat what it viewed as powerful and unresponsive interests in China’s bureaucracy, the CCP's efforts have effectively sidelined the State Council and weakened China’s government institutions, centralizing vast new bureaucratic powers in the hands of General Secretary Xi and the CCP.\textsuperscript{37}

A key component of the CCP’s centralization of power has been the expansion of the role of “leading small groups”—coordinating bodies covering important policy areas—and the elevation of some of these bodies into central commissions.\textsuperscript{38} General Secretary Xi chairs many of these groups, which have assumed more of the government bureaucracy’s traditional policymaking role.\textsuperscript{39} State Council ministries are increasingly relegated to implementing leading small group-decided policies.\textsuperscript{40} For example, two CCP commissions (upgraded from leading small groups in 2018)—the Central Commission for Comprehensively Deepening Reforms and the Central Commission for Financial and Economic Affairs—have taken over top-level economic policy design and decision making from the State Council.\textsuperscript{41} Additionally, General Secretary Xi has weakened the role of Premier Li, who occupies what has long been China’s top economic policymaking position, and entrusted economic management to close allies.\textsuperscript{42}

The CCP’s concentration of power is creating new governance challenges as decision making becomes dependent on the personal direction of General Secretary Xi and the demands of CCP ideology. In a 1980 speech on reforming China’s leadership system, then Chinese top leader Deng Xiaoping warned that “overconcentration of power is liable to give rise to arbitrary rule by individuals at the expense of collective leadership.”\textsuperscript{43} Deng—who had emerged as China’s paramount leader following the death of Mao Zedong—viewed the collective leadership system as key to preventing the return of Mao-style despotic rule.\textsuperscript{44}

In contrast, General Secretary Xi’s termination of presidential term limits suggests an intent to remain in power for life. Mr. Blanchette testified to the Commission that as General Secretary Xi prolongs his term in office, “China’s political system is becoming increasingly rigid, restrictive, and thus brittle,” further noting that “institutions governing China will atrophy as they grow increasingly dependent on the will of the top leader.”\textsuperscript{45} He concluded that, with these changes, China was “moving ... toward a garbage in, garbage out model of governance” while increased CCP control over government administration would result “in more ideological policy.”\textsuperscript{46}

\textsuperscript{35} For more information on China’s efforts to promote “Party-ification,” see U.S.-China Economic and Security Review Commission, Chapter 2, Section 1, “Year in Review: Security and Foreign Affairs,” in 2018 Annual Report to Congress, November 2018.
Xi Jinping’s Trusted Personnel

General Secretary Xi has surrounded himself with a group of loyalists who ensure his guidance is faithfully implemented and help guard against factional challenges. Although China’s leadership structure is often opaque, it appears General Secretary Xi has improved his ability to control the country’s top decision making bodies by stacking them with allies he has gathered throughout his career. Those serving in the Politburo and its Standing Committee with longstanding personal loyalties to General Secretary Xi include the two vice chairmen of the Central Military Commission (CMC)—China’s highest military decision making body—and the leaders of a number of consequential Party administration, propaganda, and discipline inspection organizations. General Secretary Xi’s key loyalists include:

- **Wang Qishan:** Wang is China’s vice president and believed to be a close confidant of General Secretary Xi. From 2012 to 2017, Wang served on the Politburo Standing Committee and led the Central Commission for Discipline Inspection, where he was instrumental to implementing General Secretary Xi’s anticorruption campaign. Wang briefly retired after reaching the CCP’s informal retirement age in 2017, but was brought back by General Secretary Xi to serve as vice president. While the role of vice president has traditionally been a ceremonial one, Wang wields considerable power as General Secretary Xi’s right-hand man. According to media reports, Wang and General Secretary Xi share a decades-long friendship, beginning when the two were “sent-down youths” during the Cultural Revolution.

- **Li Zhanshu:** Li is the party secretary of the National People’s Congress, China’s rubber stamp legislative body responsible for carrying out CCP policy. Li met General Secretary Xi when both served as county-level party secretaries in Hebei Province in central China in the early 1980s. He is ranked third in protocol order on the Politburo Standing Committee.

- **Wang Huning:** Wang leads the CCP’s Secretariat and is in charge of Party ideology. A former academic and long-time Party ideologist, Wang is widely credited for developing the ideological platforms of General Secretary Xi as well as those of his two predecessors, Hu Jintao and Jiang Zemin. While Wang does not appear to have close personal ties to

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*The Politburo of the CCP is a group of China’s 25 highest-ranked officials who oversee all decisions relating to the affairs of Party and state. The Politburo is managed by the Politburo Standing Committee, which consists of seven members and is effectively given standing authority to make all decisions on behalf of the Politburo. Of the 25 members on the Politburo, 14 were appointed by or had political ties to General Secretary Xi. Of the Politburo Standing Committee members under General Secretary Xi, only two, Li Keqiang and Wang Yang, lack clear connections to him. Li Keqiang, the premier, was promoted to the Standing Committee at the 17th Party Congress held in October 2007. Wang Yang, head of the Chinese People’s Political Consultative Conference, was promoted to the Standing Committee during the 19th Party Congress, but lacks a clear prior connection to General Secretary Xi. Katsuji Nakazawa, “The Power Relationships that Govern China,” *Nikkei Asian Review*, 2019; Cheng Li, “China’s New Politburo and Politburo Standing Committee,” *Brookings Institution*, October 26, 2017.*
Xi Jinping’s Trusted Personnel—Continued

Xi, the two are ideologically aligned, with Wang associated with crafting Xi’s signature “China dream” ideology.\(^{51}\) He is ranked fifth on the Politburo Standing Committee and was elevated to the committee in 2017 as a reward for his efforts as a theoretician for the CCP.\(^{52}\)

- **Zhao Leji:** Zhao is secretary of the Central Commission for Discipline Inspection, China’s top anticorruption body, and is responsible for enforcing internal CCP rules and combating corruption. He was the party secretary of Shaanxi Province from 2007 to 2012 where he developed ties with General Secretary Xi’s family and friends. The two men’s fathers were also reportedly close friends. Zhao is ranked sixth on the Politburo Standing Committee.\(^{53}\)

- **Han Zheng:** Han is the vice premier of China’s State Council, which is responsible for developing and implementing policies that conform with CCP directives. Han was General Secretary Xi’s deputy when the latter served as party secretary of Shanghai for seven months in 2007. He is ranked seventh on the Politburo Standing Committee.\(^{54}\)

- **Zhang Youxia:** General Zhang is a vice chairman of the CMC, and in 2017 became the first vice chairman directly appointed by General Secretary Xi. General Zhang and General Secretary Xi are childhood friends, and their fathers fought together during the Communist Revolution.\(^{55}\)

- **Xu Qiliang:** General Xu is a vice chairman of the CMC and the first CMC vice chairman and Politburo member from the PLA Air Force. He was the commander of the air force’s Eighth Corps when General Secretary Xi was the party secretary of Fuzhou from 1990 to 1996, making Xu his direct subordinate for provincial mobilization and recruitment issues. Xu became a vice chairman of the CMC in October 2012 immediately prior to General Secretary Xi becoming CMC chairman in November 2012.\(^{56}\)

- **Chen Xi:** Chen is the head of the CCP’s Organization Department, which is responsible for staffing key positions within the Party. Chen and General Secretary Xi were classmates at Tsinghua University from 1975 to 1979.\(^{57}\)

- **Huang Kunming:** Huang is the head of the CCP’s Propaganda Department and is responsible for information dissemination and enforcing media censorship. Huang previously worked with General Secretary Xi when he was the deputy party secretary of Huzhou City in Zhejiang Province from 1999 to 2003 and Xi was the party secretary of Zhejiang Province from 2002 to 2007. Huang was also the party secretary in Yongding County, Fujian Province, between 1996 and 1998 when General Secretary Xi was the Fujian party secretary.\(^{58}\)
Concerns over PLA Loyalty

Another component of the CCP’s campaign to tighten control over all levers of governmental power has been its redoubled efforts to ensure the absolute loyalty of China’s security forces to the CCP’s central leadership in general and General Secretary Xi in particular. Before General Secretary Xi’s 2012 rise to power, longstanding concerns had heightened in Beijing that elements within the PLA and China’s domestic security forces were resisting the authority of the CCP’s central leadership, with some even being used as a tool by provincial leaders to pursue their own political ambitions without regard for central authorities. The reported support for Bo Xilai’s bid for power in 2012 from key elements within the PLA and People’s Armed Police, a key component of China’s internal security system, raised serious concerns within the Party leadership about the reliability of China’s security forces.*

The arrest of former Politburo Standing Committee member Zhou Yongkang, a key ally of Mr. Bo and the first member of the Standing Committee to be prosecuted † since the Cultural Revolution, was an additional example of the factionalism and unresponsiveness spurring these concerns. 60 Tim Heath, senior international defense researcher at the RAND Corporation, highlighted in testimony before the Commission that symptomatic of the concerns over the loyalty of Chinese security forces are “numerous media reports of unverified rumors of coup plots against [General Secretary] Xi—something virtually unheard of in either Jiang Zemin or Hu [Jintao]’s eras.” 61 There have also been numerous incidents reported where corrupt local officials have used People’s Armed Police units to collect debts, seize land, disrupt protests against misrule, and carry out political retribution.62

Bureaucratic resistance by high-ranking PLA leaders further contributed to a loss of CCP confidence in the military top brass. In his testimony before the Commission, Mr. Heath pointed to the 2012 arrest of Gu Junshan, a senior general in the PLA’s logistics headquarters, as “alarming evidence of the military’s resistance to civilian oversight.” 63 According to Mr. Heath, then General Secretary Hu reportedly ordered an inquiry into corruption charges against Gu, and ultimately had to direct the military’s top disciplinary inspection unit to carry out the inquiry after senior officers on the CMC ignored Hu’s instructions. 64 This and other similar incidents underscored longstanding CCP concerns over the PLA becoming a “nationalized” force that viewed itself as a professional, national military rather than as an instrument of the Party.‡

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* In February 2012, Bo Xilai sent the People’s Armed Police after former Chongqing police chief Wang Lijun, who sought refuge in the U.S. consulate in Chengdu after the two men argued over the involvement of Bo’s wife in the murder of a British businessman, Viola Zhou, “Why China’s Armed Police Will Now Only Take Orders from Xi and His Generals,” South China Morning Post, December 28, 2017.

† In 2015, Zhou Yongkang was found guilty on charges of bribery, abuse of power, and disclosing national secrets and given a life sentence. BBC News, “China Corruption: Life Term for Ex-Security Chief Zhou,” June 11, 2015.

‡ Concerns among CCP leaders have grown over what they view as trends within the PLA toward becoming a fully professional, autonomous force outside the political control of the Party. A prominent example of this concern occurred during the mass protests leading up to the 1989 Tiananmen Square massacre, when some PLA units refused to obey orders to disperse the student protesters. Part of the blame for PLA units failing to comply with CCP orders was directed at then CCP General Secretary Zhao Ziyang, who some senior CCP leaders associated with support for a nationalized army and blamed for the weakening of Party control over the military. Phillip
of CCP leaders, this development would inevitably weaken Party control over the PLA, increase bureaucratic resistance to CCP oversight, and increase the chances that PLA leaders might refuse to follow Party directives to forcibly suppress dissent within China in the event of future large-scale unrest.65

In part to address concerns over PLA loyalty, General Secretary Xi—who also serves as chairman of the CMC—has targeted a number of high-ranking generals in the anticorruption campaign, embarked on a propaganda campaign to reinvigorate PLA loyalty to the CCP, and pushed through major changes to the PLA command system.* According to Dr. Wedeman’s calculations, whereas only one PLA officer holding the rank of major general or above was convicted of corruption between 2000 and 2011, 78 officers at this rank were “either … charged with corruption or were reportedly sidelined after allegation[s] of corruption were leveled against them” between 2012 and January 2019.66 Included in this purge have been two sitting CMC members and the two CMC vice chairmen—the PLA’s two top-ranking military officers Guo Boxiong and Xu Caihou—who served under former General Secretary Hu. Since the prosecution of the latter two, the CCP has launched an extensive propaganda campaign to rebuild military discipline under the slogans of “eliminate the baneful influence of Guo Boxiong and Xu Caihou” and “scraping poison off the bone.” 67

In his CMC leadership role, General Secretary Xi has also taken a series of steps to tighten his personal control over the PLA and People’s Armed Police. In 2017, he reduced the number of positions on the CMC, and has taken a more active role in selecting senior military officers for promotion than his predecessor.†68 Meanwhile, he has also replaced more top PLA and People’s Armed Police leaders than his predecessor and placed the People’s Armed Police directly under the command of the CMC, removing the force from the influence and control of provincial authorities.‡69

A further step to ensure General Secretary Xi’s unquestioned authority over military affairs has been the resuscitation of the “CMC Chairman Responsibility System,” a formulation that aims to centralize decision making over all important military matters in the office of the CMC chairman and curtail the independence of uni-

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* For more on China’s military reorganization, see U.S.-China Economic and Security Review Commission, Chapter 2, Section 2, “China’s Military Reorganization and Modernization, Implications for the United States,” in 2018 Annual Report to Congress, November 2018, 211.

† According to Phillip C. Saunders and Joel Wuthnow, Hu Jintao was not actively involved in the senior military officer selection and promotion process, effectively rubber-stamping decisions made by his two CMC vice chairmen. Conversely, General Secretary Xi has been much more personally engaged in the promotion process, reportedly even conducting personal interviews with candidates for senior positions. This level of personal involvement has allowed him to place supporters of his agenda in key positions and reward officers who display personal loyalty. Phillip C. Saunders and Joel Wuthnow, “Large and in Charge” in Phillip Saunders, ed., Chairman Xi Remakes the PLA: Assessing Chinese Military Reforms, National Defense University, February 22, 2019, 543–544.

formed PLA leaders. An earlier arrangement instituted by Deng Xiaoping had delegated significant authority over administration of the PLA to the CMC vice chairmen in an attempt to improve the efficiency and professionalism of PLA management.

Beyond the inefficiencies that could attend an overcentralization of power in the hands of General Secretary Xi, according to Mr. Heath, the CCP’s renewed focus on loyalty and political indoctrination could also “result in a military that prioritizes compliance and sloganeering over professional competence.” This concentration of power could also create bottlenecks in military command decisions. In his testimony, Mr. Heath argued that “elevating too many decisions to elite supraministerial leading small groups raises the risks that important decisions will be delayed or grow unpredictable. The lack of institutionalization of authority between new and old command structures also causes friction and could cause problems with coordination, deconfliction, and decision making in a crisis.”

China’s Economic and Innovation Challenges

Beijing Strengthens State Control

In a speech commemorating the 40th anniversary of Deng Xiaoping’s reform and opening in December 2018, General Secretary Xi declared 40 years of reform had demonstrated the need to maintain CCP leadership “over all tasks,” but did not offer any new commitments to economic reform. The speech indicated a continuation of General Secretary Xi’s vision of “reform,” which features limited market liberalization, reasserts government control over the economy, and favors the inefficient state sector at the expense of the private sector. At the annual Central Economic Work Conference in December 2018, Chinese leaders acknowledged “new and worrisome developments” and a “complicated and severe” external environment—an oblique reference to trade tensions with the United States.

According to official Chinese statistics, China’s gross domestic product (GDP) growth slowed to 6.3 percent in the first half of 2019—a near 30-year low. General Secretary Xi continued to centralize economic governance to strengthen the state sector. In testimony before the Commission, Michael Hirson, China and Northeast Asia practice head at Eurasia Group, described CCP decision making bodies, such as leading small groups, supplanting technocrats and regulators to guide economic policy, and “a wave of party building” taking place across both state-owned enterprises (SOEs) and private firms. (For a discussion of China’s economic slowdown, including analysis of key growth drivers, see Chapter 1, Section 1, “Year in Review: Economics and Trade.”)

In the face of economic headwinds, Chinese policymakers are leaning on stimulus measures to stabilize growth. Beijing understands that China’s long-term economic stability is threatened by the resurgence of the state sector at the expense of the private sector,

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There are longstanding doubts about the reliability of China’s official data. Of note, Xiang Songzuo, a professor at Renmin University’s School of Finance and former chief economist of the Agricultural Bank of China, made a splash in December 2018 when he suggested the real rate of economic growth in 2018 could be 1.67 percent, or even lower. Chris Buckley and Steven Lee Myers, “China’s Leader Says Party Must Control ‘All Tasks,’ and Asian Markets Slump,” New York Times, December 18, 2018.
rising debt levels, and a rapidly-aging population, but its response has been constrained by overriding political objectives.

The State Advances

Since General Secretary Xi assumed power in 2012, China’s state sector has become newly ascendant. Despite being significantly less productive than the private sector, SOEs receive the lion’s share of bank credit: in 2016, SOEs received 83 percent of all new loans versus 11 percent for private companies.* As China’s economic growth slows, SOEs have fared better than the private sector. According to Chinese statistics, SOEs’ revenue grew by 10 percent and profits grew by 12.9 percent during 2018, compared to revenue growth of 13.6 percent and profit growth of 23.5 percent during 2017.† The decrease from 2017 suggests SOEs were impacted by the slowdown, but not nearly to the extent of the private sector. Revenue for private industrial enterprises decreased 29.6 percent year-on-year, while profit decreased 27.9 percent.‡

Meanwhile, China’s private sector, which contributes around 66 percent of China’s GDP and 90 percent of new jobs, is under severe stress due to a credit crunch and the country’s weakest economic expansion since 1990. The Chinese government’s ongoing efforts to reduce overall debt levels have choked off financing to the private sector to the benefit of the state sector. Previously, China’s banks used off-balance-sheet channels to lend to private firms, which are regarded as more risky because they do not have implicit state support. The deleveraging campaign has forced banks to bring these loans back on their books, requiring them to set aside more capital to cover for potential losses and consequently lend at a higher rate to private borrowers.

Following the launch of the deleveraging campaign in 2016, financing costs decreased for SOEs, but jumped for private enterprises. In 2018, bond defaults by private companies reached an all-time high and a wave of de facto nationalizations hit the private sector as capital-starved private companies sold large stakes to SOEs. With financing drying up, a growing number of Chinese companies are issuing commercial acceptance bills—essentially, documents promising payment in the future—to their suppliers. According to Chinese government data, companies owed $211 billion in commer-

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† China’s National Bureau of Statistics defines “industry” to encompass extraction industries, electricity and water provision, manufacturing, processing of agricultural products (e.g., leather making), and repair of industrial products. It does not encompass construction or energy. Statistics are compiled for “enterprises above a designated size,” which China’s National Bureau of Statistics defines as enterprises having revenues of at least $2.9 million (20 million renminbi [RMB]) from primary business activities. China’s National Bureau of Statistics, Industry, October 29, 2019. Translation; China’s National Bureau of Statistics, Profits for China’s Industrial Enterprises above a Designated Size Grew 10.3 Percent in 2018 (2018年规模以上工业企业利润增长10.3%), January 28, 2019. Translation.

‡ Private companies accounted for 45 of the 52 defaulting issuers in 2018. In 2017 and 2016, the numbers of defaulting issuers were about 20 and 35, respectively, and the majority of them were private. Many economists argue that the rise in corporate bond defaults is a positive sign of a maturing financial market after years of routine government bailouts, but the fact that private firms continue to account for the vast majority of defaults suggests SOEs are not held to the same standards. Edward White, “Chinese Corporate Bond Defaults Hit Record High, Fitch Says,” Financial Times, January 20, 2019; Shen Hong, “Default Fears Add Fresh Stress to Chinese Private Sector,” Wall Street Journal, January 11, 2019.
cial acceptance bills at the end of February 2019, an increase of more than a third from the previous year.\textsuperscript{85}

General Secretary Xi met with a group of China’s top private executives in November 2018 to reassure them of the state’s support, promising a range of measures including tax cuts, increased lending to private borrowers, and equal treatment for the private sector.\textsuperscript{86} Nicholas Borst, director of China research at Seafarer Capital Partners, argued in his testimony to the Commission that while such policies might ease the pressure felt by private firms, “in order to truly level the playing field between private firms and SOEs, difficult reforms are needed. This includes ending the implicit guarantee of government support enjoyed by many SOEs that lower their credit risk relative to private firms.”\textsuperscript{87}

\textit{Rising Debt Burden Threatens Long-Term Economic Stability}

According to the Bank for International Settlements,\textsuperscript{†} at the end of 2018 (the latest data available) China’s total nonfinancial debt\textsuperscript{‡} reached $33.2 trillion, or 254 percent of GDP, up from 142 percent at the end of 2008.\textsuperscript{88} This is comparable to debt levels in advanced economies like the United States but high relative to emerging markets.\textsuperscript{§} Equally important as the absolute size of China’s debt burden is its rapid growth, coupled with the increasing complexity and opacity of China’s financial system, which makes accounting for exact levels of indebtedness problematic.

The size of China’s total internally held debt increases further when local government borrowing is factored in, including credit guarantees by local government financing vehicles (LGFVs).\textsuperscript{¶} In an October 2018 report, S&P Global Ratings estimated China’s local government debt could be as high as $6 trillion—“a debt iceberg with titanic credit risks”—with most of these debts held by LGFVs.\textsuperscript{89} The International Monetary Fund (IMF) assesses that while China’s official budgetary government debt remains “low and sustainable,” its “augmented” debt (e.g., off-budget liabilities borrowed by LGFVs) is “high and on an upward trajectory,” suggesting “risks of debt stress.”\textsuperscript{90} (For further discussion of China’s debt and deleveraging, see Chapter 1, Section 1, “Year in Review: Economics and Trade.”)

\textsuperscript{*} The presumption of government support creates a moral hazard by incentivizing SOEs to undertake riskier investments and accumulate debt in excess of their repayment capacity. Moral hazard is a situation where a party to an agreement engages in risky behavior because it knows the other party bears the consequence of that behavior.

\textsuperscript{†} The Bank for International Settlements is an international financial institution owned by 60 central banks, representing countries from around the world. The bank’s mission is “to serve central banks in their pursuit of monetary and financial stability, to foster international cooperation in those areas and to act as a bank for central banks.” Bank for International Settlements, “About BIS—Overview.” \url{https://www.bis.org/about/index.htm}.

\textsuperscript{‡} Nonfinancial debt comprises the outstanding debt of the private nonfinancial sector (which is broken down into household and corporate debt) and the government. The largest category of nonfinancial debt is held by corporations, which account for about 60 percent of China’s total debt, while government and households each hold another 20 percent. Bank for International Settlements, “Changes to the Data Set on Credit to the Non-Financial Sector.”

\textsuperscript{§} At the end of 2018, the United States’ total nonfinancial debt reached 249 percent of GDP and the total nonfinancial debt of emerging economies averaged 183 percent of GDP. Bank for International Settlements, “Credit to the Non-Financial Sector,” June 4, 2019.

\textsuperscript{¶} LGFVs are economic entities established by Chinese local governments to finance government-invested projects, typically infrastructure and real estate development projects. Because local governments are barred from borrowing directly from banks, they use LGFVs to borrow money to finance projects. These debts are not included in official Chinese debt statistics.
Aging Population Dims China’s Future Prospects

China is experiencing major demographic challenges, including a shrinking workforce and a rapidly-aging population, which will impose an additional burden on its economy. In testimony to the Commission, Andrew Polk, cofounder of research firm Trivium China, argued that China’s “demographic dynamics only further challenge China’s ability to successfully move up the economic ladder over the longer term, not least because one of China’s perennial economic advantages—a large, improving, and relatively cheap labor force—will increasingly dissipate.”

In 2018, China’s working age population—people between the ages of 16 and 59—accounted for 64.3 percent of China’s total population, and people over 60 made up 17.9 percent of the population (see Figure 1). According to UN forecasts, by 2045 China’s working age population will drop to 54.4 percent of China’s total population, while the country’s population over 60 will grow to 31.4 percent of the total population. China’s declining labor force will detract an average of 0.3 percentage points from GDP growth annually for the next ten years, according to estimates from the Conference Board.

Figure 1: China’s Population Distribution by Age Group

![Figure 1: China’s Population Distribution by Age Group](source)

In addition, China’s aging population is straining its social insurance system, whose outlays exceeded payroll tax revenues by $68 billion in 2017. Chinese Academy of Social Sciences social insur-

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ance expert Bingwen Zheng remarked in November 2018 that the budget shortfall for pensions, administered by local governments, poses increasing fiscal risks. China’s public pension system is dependent on government subsidies to cover the shortfalls, but the country’s slowing economic growth may limit Beijing’s ability to bridge the gap. An April 2019 Chinese Academy of Social Sciences report warned China’s main state pension fund—the urban worker pension fund—could become insolvent by 2035. Signs of stress have begun to emerge, with some provinces already struggling to make pension payments. The Chinese government has sought to address the pension shortfalls through measures such as creating a fund in July 2018 to shift funds from regions with pension surpluses to those with shortfalls. However, in March 2019 Beijing announced cuts to the corporate contributions rate to help companies weather the economic slowdown, a move that will reduce contributions to government pension funds.

**China’s Science and Technology Goals and Shortfalls**

China seeks to acquire and develop advanced technologies to move up the value added chain and reduce its dependence on foreign-controlled technology, which it views as both an economic and security vulnerability. In support of this effort, the Chinese government has marshaled vast resources toward encouraging domestic innovation, financing industrial upgrading, and supporting the acquisition of foreign technology. The U.S. Department of Commerce’s ban on U.S. companies selling technology and services to Chinese telecom equipment giant ZTE—imposed in April 2018 but subsequently lifted—and the Department of Commerce’s May 2019 decision to add Huawei and its affiliates to its Entity List controlling U.S. technology exports are reminders of the continued dependency of many Chinese companies on foreign technology despite recent gains.

General Secretary Xi has been a vocal champion of China’s indigenous innovation drive, repeatedly emphasizing the importance of mastering what he has termed “core technologies” and technological “self-reliance.” In an April 2016 speech, General Secretary Xi declared that “core technology is our biggest lifeline and the fact that core technology is controlled by others is our greatest hidden danger.” Although there is no official list of core technologies, technology experts believe they include advanced semiconductors, operating systems, cloud systems, and the hardware and algorithms behind artificial intelligence (AI) systems. China’s drive for technological self-reliance has taken on new urgency as U.S.-China trade tensions drag on. In May 2019, General Secretary Xi said, “Only if we own our own intellectual property and core technologies … can we pro-

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† For Beijing, technological self-reliance means developing technology free of foreign control or dependency and based on homegrown intellectual property. General Secretary Xi has invoked the phrase as a rallying cry in face of escalating trade tensions with the United States. Kinling Lo, “Xi Jinping Urges China to Go All In on Scientific Self-Reliance after ZTE Exposes Hi-Tech Gaps,” South China Morning Post, May 28, 2019.
duce products with core competitiveness, and [we] won’t be beaten in intensifying competition.”

China’s technology push under General Secretary Xi builds upon earlier efforts but differs in at least three key aspects: a greater emphasis on the strategic importance of reducing reliance on foreign core technologies, the critical role of private companies, and the mobilization of new funding channels. According to Mr. Hirson, China’s private technology companies "rather than state-owned behemoths like China Telecom, represent China’s ‘national champions’ in next generation areas.” China’s major technology giants, including Baidu, Alibaba, and Tencent, have made large investments in AI and consumer internet and fintech industries. Following the ZTE sanctions, Baidu, Alibaba, and Tencent each responded to Beijing’s call for self-reliance by taking steps to support the development of the semiconductor industry in China.

In recent months, China’s technology sector has faced stepped-up government scrutiny and increased pressure to align with Party edicts after years of thriving under light regulation—a trend some analysts caution may undermine Beijing’s national strategy for innovation driven development.

Addressing Shortfalls in Defense Technology

Beijing is deeply concerned about its defense industry’s capacity to independently innovate and develop the cutting-edge technologies it views as critical to what the CCP terms China’s “core national power.” China has made great strides in key defense technologies related to cyber, space, advanced computing, and AI, and is a world leader in hypersonic weapons. Nevertheless, Beijing believes China is still lagging behind the United States, noting in its most recent defense white paper that China’s military is “confronted by risks from technology surprise and a growing technological generation gap.” General Secretary Xi has demonstrated particular concern over shortfalls in China’s technological capabilities, which he has described as the “root cause of [China’s] backwardness.” China’s defense industry continues to struggle to produce some high-end military components—such as advanced aircraft engines, guidance and control systems, and microprocessors—forcing Beijing to remain reliant on foreign technologies in these areas. China continues to rely in particular on foreign innovation systems from the United States and Japan for the core technologies and talent it views as necessary to its national security.

*In China, direct ownership is not the primary determinant of the government’s ability to control a company’s decision making; in other words, private companies can also be directed to carry out government objectives. As described by Curtis J. Milhaupt and Wentong Zheng, “Large, successful [Chinese] firms—regardless of ownership—exhibit substantial similarities in areas commonly thought to distinguish SOEs from [private companies]: market dominance, receipt of state subsidies, proximity to state power, and execution of the state’s policy objectives.” Curtis J. Milhaupt and Wentong Zheng, “Beyond Ownership: State Capitalism and the Chinese Firm,” Georgetown Law Journal 103 (2015): 665.

†For instance, in July 2018 Baidu unveiled its self-developed, high-end AI chip designed for autonomous vehicles and data centers. In September 2018, Alibaba established a semiconductor subsidiary to produce AI chips made for autonomous vehicles, smart cities, and smart logistics. Paul Triolo and Graham Webster, “China’s Efforts to Build the Semiconductors at AI’s Core,” New America, December 7, 2018.

‡For example, in September 2019 Chinese state media reported that Hangzhou, a major technology hub in China, plans on assigning government officials to work with 100 local private companies, including Alibaba. Josh Horwitz, “China to Send State Officials to 100 Private Firms Including Alibaba,” Reuters, September 23, 2019.
One of General Secretary Xi’s top priorities is military-civil fusion, a strategy that seeks to enable transfers between the civilian and defense sectors to support defense-related science and technology advancements. Military-civil fusion is also a vehicle for creating cohesion in China’s military and civilian research efforts, so that the entire system can be effectively mobilized to support the military and sustain economic growth. The strategy is intended to lessen China’s dependence on foreign expertise while positioning China to become a global leader in key emerging technologies, which General Secretary Xi has identified as “a national heavy weapon.”

To this end, China has sought to penetrate innovation hubs in the United States like Silicon Valley and to develop research partnerships with U.S. and other foreign universities to facilitate the transfer of defense-related technology and knowledge. In testimony before the Commission, Greg Levesque, then managing director at Pointe Bello, argued that this strategy is “critical to strategic competition and securing China’s future as not only an economic, but also a military superpower.” Jiang Luming, a leading expert on military-civil fusion at the PLA National Defense University, views the success of this strategy in similar terms. According to Major General Jiang, should China fail to fully implement military-civil fusion, its “national security development will lose its most central supporting power; if we are defeated in this particular competition, an entire era will be lost.” (For more on military-civil fusion, see Chapter 3, Section 2, “Emerging Technologies and Military-Civil Fusion: Artificial Intelligence, New Materials, and New Energy.”)

While General Secretary Xi has placed significant emphasis on military-civil fusion, there are areas where China’s defense industries continue to fall well short of Beijing’s expectations. Continued shortfalls stem largely from the military-civil fusion system being still in the early stages of development and hampered by high barriers to entry in the defense industry and a lack of information-sharing between the PLA and civilian entities. For example, Chinese defense conglomerates remain bloated, inefficient, and vertically integrated in contrast to the horizontal structure of many U.S. and other foreign enterprises capable of making quicker innovations. Furthermore, China’s defense sector is closed to outside entrants and is dominated by a limited number of state-owned defense corporations, resulting in contracts being awarded through single-sourcing mechanisms that limit competition and innovation. There is also likely lingering corruption in China’s research, design, and acquisition processes which could hamper China’s ability to innovate. Ultimately, China’s embrace of military-civil fusion to tap into the technical skills that exist inside the civilian economy is a reflection of the ongoing capability shortfalls within the defense sector.

Resistance to Beijing’s Ambitions Abroad: Economic, Military, and Political Challenges

Despite its growing ambition to shape the regional and even global order, Beijing faces a number of challenges to its economic statecraft, military modernization, and political influence efforts that may constrain its ability to achieve its foreign policy aims. While Beijing seeks to use economic statecraft in the areas of trade, currency, and infrastructure investment to shift Asia’s center of gravity away from
the United States, it is running into challenges because of a lack of transparency and accountability in its approach as well as its inexperience. In the military domain, China has embarked on an ambitious modernization program to build what it terms a “world-class” military by the middle of the 21st century, but General Secretary Xi harbors serious reservations over China’s ability to prevail in a conflict against a highly capable adversary. Beijing has used the PLA with increasing frequency in recent years to coerce and intimidate China’s neighbors into accepting the CCP’s expansive sovereignty claims and bid for leadership in the region. Nevertheless, top leaders’ concerns over the PLA’s warfighting prowess may lessen their appetite to provoke a military conflict that could draw in the direct intervention of the United States, at least in the near term. (For more information on China’s military modernization efforts, see Chapter 4, Section 1, “Beijing’s ‘World-Class’ Military Goal.”)

Finally, as China has grown more assertive abroad, countries in the Indo-Pacific and outside the region have begun pushing back against what many view as Beijing’s unwarranted interference and intimidation efforts. Over the last several years, these countries have accelerated their own military modernization programs, enhanced security ties and intelligence-sharing with the United States and each other, and increased their military deployments in the region in an attempt to deter further Chinese adventurism.

Challenges with Beijing’s Economic Statecraft

Beijing’s first external challenge stems from criticism of its economic statecraft efforts. During the 19th Party Congress, General Secretary Xi stated that China’s experience “offered a new option for countries that want to speed up their development while preserving their independence.” In Beijing’s view, China’s economic model combines a market economy’s efficient resource allocation with a state’s ability to provide macroeconomic stability and equitable socio-economic outcomes. In practice, China’s economic model promotes authoritarianism, resource misallocation, and global economic distortions.

In an article for the Texas National Security Review, China specialist Liza Tobin argues Beijing sees economic opening as a process of “integration with the global economy that is necessary for China’s rise—initially to acquire advanced technology and expertise and, later, to shape global norms, standards, and institutions in line with Chinese strategic requirements.” Beijing seeks to reshape global economic governance

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* Beijing has used the PLA, China Coast Guard, and maritime militia paramilitary forces to coerce or intimidate China’s neighbors with increasing frequency in recent years. In 2012, China deployed its coast guard to occupy the Philippine-claimed Scarborough Shoal, and has prevented Filipino fisherman from accessing the rich fishing waters around the shoal since that time. In 2014, Beijing deployed the PLA Navy and PLA Air Force to support China’s coast guard and maritime militia, preventing Vietnam from expelling a Chinese hydrocarbon rig from Vietnam’s claimed exclusive economic zone. In 2019, the PLA Air Force and PLA Navy continued Beijing’s multi-year campaign to intimidate Taipei by conducting exercises and other provocative activities near Taiwan. Martin Banks, “Taiwan Official Pledges Boost in Defense Capabilities Won’t Be Deterred by Chinese ‘Coercion,’” Defense News, May 3, 2019; Yimou Lee, “Taiwan President Says Chinese Drills a Threat but Not Intimidated,” Reuters, April 15, 2019; U.S. Department of Defense, Annual Report to Congress: Military and Security Developments Involving the People’s Republic of China 2014, April 24, 2014, 3–4.

† A notable exception to the trend of increased intelligence-sharing among countries in the region is the friction between Japan and South Korea that recently led Seoul to announce its intention to terminate a key intelligence-sharing arrangement between the two countries. Choe Sang-Hun, Motoko Rich and Edward Wong, “South Korea Says It Will End Intelligence-Sharing Deal with Japan, Adding to Tensions,” New York Times, August 22, 2019.
through its participation in existing international institutions like the IMF and World Bank while at the same time creating and funding China-led regional organizations (e.g., the Asian Infrastructure Investment Bank and Forum on China-Africa Cooperation) that provide venues for Chinese leadership. Beijing also wants a larger role for itself in setting global rules, particularly in “emerging domains such as cyberspace, deep seas, polar regions, and outer space.”

Promotion of a “China Model” through BRI

China’s growing economic clout and assertive foreign policy is drawing increased attention to Beijing’s economic statecraft, of which BRI—General Secretary Xi’s signature economic and foreign policy project—is perhaps the most visible example. In addition to seeking economic benefits, Beijing views the project as a vehicle for revising the global political and economic order to better align with its interests. Six years after BRI’s inception, the global response has been mixed. Many countries welcome BRI in light of China’s sizable financial commitments, but some are increasingly concerned about the transparency, debt sustainability, and environmental impacts of BRI projects, as well as the strategic implications of the initiative for their political, economic, and security interests. Notably, over the past year leaders in Malaysia, the Maldives, and Pakistan swept into power by capitalizing on public unease about Chinese-funded investment projects, and since taking office have suspended or canceled several high-profile BRI projects. Nonetheless, these setbacks have not led to wholesale rejection of the initiative. In many cases, host countries are moving forward with projects that were suspended or even canceled after renegotiating deals with Beijing.

The United States, the EU, India, and Japan have also voiced their concerns about BRI. For example, India’s main objections to BRI center on the China-Pakistan Economic Corridor, which runs through the disputed region of Kashmir. In a speech at the Shanghai Cooperation Summit held in June 2019, Indian President Narendra Modi said India only supported connectivity projects that are based on the “respect for sovereignty, regional integrity, good governance, transparency ... and reliability.” German business newspaper *Handelsblatt* reported in April 2018 that 27 out of 28 EU ambassadors to Beijing signed an internal EU report stating BRI “runs counter to the EU agenda for liberalizing trade and pushes the balance of power in favor of subsidized Chinese companies.”

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* For example, China’s 2017 strategy on international cyberspace cooperation declared “China will push for institutional reform of the UN Internet Governance Forum to enable it to play a greater role in Internet governance.” State Council Information Office of the People’s Republic of China, *International Strategy of Cooperation in Cyberspace*, March 2, 2017.

† Beyond expanding China’s export markets and promoting the use of the RMB as an international currency, BRI provides an opportunity for China to export some of the country’s massive industrial overcapacity. In a September 2019 interview, the director of strategic planning and technology at Baosteel, China’s largest steel producer, said, “For the steel industry, the Belt and Road Initiative will generate direct demand for steel products.” Nick Schifrin and Dan Sagalyn, “China’s Massive Belt and Road Initiative Builds Global Infrastructure—and Influence,” *PBS*, September 27, 2019.

‡ For more on views and responses from the United States, Japan, and India, see U.S.-China Economic and Security Review Commission, Chapter 3, Section 1, “Belt and Road Initiative,” in 2018 Annual Report to Congress, November 2018, 282–286.

§ Only Hungary’s ambassador to Beijing did not sign the report. For more on China’s efforts to influence the policies of individual EU countries, see U.S.-China Economic and Security Review Commission, Chapter 3, Section 1, “Belt and Road Initiative,” in 2018 Annual Report to Congress, November 2018, 282–286.
An EU-wide policy response is emerging: in September 2018, the EU unveiled a new strategy to improve transport, energy, and digital links between Europe and Asia. While the EU’s strategy seeks to distinguish its approach from BRI through its emphasis on sustainability and respect for the rules-based international system, it also preserves engagement with China by highlighting possible synergies between BRI and European connectivity projects, reflecting European countries’ varying levels of support for BRI.

Concerns about China’s growing international economic engagement extend beyond BRI. The EU’s connectivity strategy comes on top of a separate push to adopt an EU framework for screening foreign investment in response to concerns surrounding Chinese investment in Europe’s strategic sectors. In March 2019, the European Commission released a landmark paper on EU-China relations that declared China an “economic competitor in the pursuit of technological leadership” and a “systemic rival promoting alternative models of governance.” The paper called on European leaders to seek “a more balanced and reciprocal economic relationship” with China by taking a tougher stance in key areas of bilateral trade while noting potential areas of cooperation.

An area of emerging concern is the potential for BRI projects to saddle participating countries with unsustainable debt. Many countries receiving loans from China also receive concessional financing from the World Bank’s International Development Association (IDA) and some have received debt relief through the IMF and World Bank’s Heavily Indebted Poor Country initiative and related Multilateral Debt Relief Initiative programs (see Table 1). At the time debt relief was negotiated, concern was raised by IDA executive directors regarding the risk of “free riding,” defined as “situations in which IDA’s debt relief or grants could potentially cross-subsidize lenders that offer non-concessional loans to recipient countries,” particularly in “resource-rich grant-recipient countries that could rely on non-concessional borrowing collateralized with future export receipts.” China’s lack of transparency in its lending raises concerns regarding not only China’s free riding on previous international debt relief efforts, but also the potential for increased risk of debt distress in low-income countries, compromising the impact and
contribution of IDA’s concessional lending to meet poverty reduction and growth goals in the poorest nations.

Table 1: BRI Signatories: Debt Relief, Debt Sustainability, Chinese Investment, and Loans

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<tbody>
<tr>
<td>Afghanistan</td>
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<td>Congo, Republic of</td>
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In response to pushback against BRI, Beijing has been rethinking how it selects and implements projects and presents BRI to overseas audiences. China’s economic slowdown, ongoing trade tensions with the United States, and the decline of its foreign reserves in recent years are constraining Beijing’s ability to finance BRI. Beijing recognizes it cannot afford to continue to make investments that are financially nonviable and incur reputational costs. As a result, Beijing has begun an interagency review to take stock of the number and terms of BRI deals, according to media reports in June 2018.

During the second Belt and Road Forum in April 2019, General Secretary Xi sought to rebuild BRI’s tarnished global image in the wake of high-profile scandals by promising “open, green, and clean” projects. Official pronouncements at the forum echoed the tone and fanfare of the first forum in 2017, but tailored the messaging and deliverables to address international concerns. The second forum announced multiple initiatives to improve environmental sustainability of BRI projects, including a program to train environmental officials in BRI countries, the creation of a debt sustainability assessment framework, and seminars on anticorruption and business integrity. Chinese agencies also signed a number of bilateral agreements to improve transparency, such as auditing cooperation between China’s Ministry of Finance and regulators in Malaysia and Japan.

At the second BRI forum, People’s Bank of China Governor Yi Gang sought to address concerns about the financial risks of BRI lending, saying China needs to “objectively assess developing countries’ debt problems” and “consider a country’s complete debt-servicing capabilities.” Over the past year, Beijing has provided debt relief for some BRI countries, including debt write-offs, deferments, and refinancing.

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*a* China’s foreign exchange reserves are an important source of capital for China’s policy banks, which—along with China’s major state-owned commercial banks—have been the main financiers of BRI. When BRI was launched in 2013, China’s foreign exchange reserves were valued at $3.66 trillion, peaking at nearly $4 trillion in June 2014. As of April 2019, China’s foreign exchange reserves stood at $3.1 trillion.


‡ According to China’s Ministry of Finance, the debt sustainability framework is a “non-mandatory policy tool” for BRI participants “to conduct debt sustainability analysis and manage debt risks according to the risk rating results, as an important reference for lending decisions.” The framework is largely modeled after the World Bank and IMF’s debt sustainability framework for low-income countries governing lending operations for multilateral institutions; however, as a voluntary framework, China’s debt sustainability framework is not binding on Chinese financial institutions. Scott Morris and Mark Plant, “China’s New Debt Sustainability Framework Is Largely Borrowed from the World Bank and IMF. Here’s Why That Could Be a Problem,” Center for Global Development, July 19, 2019; China’s Ministry of Finance, Debt Sustainability Framework for Participating Countries of the Belt and Road Initiative, April 25, 2019.

§ A March 2018 study from the Center for Global Development examining the debt vulnerabilities of countries identified as potential BRI borrowers found that out of 23 countries determined to be significantly or highly vulnerable to debt distress, there are eight countries—Djibouti, Kyrgyzstan, Laos, Maldives, Mongolia, Montenegro, Pakistan, and Tajikistan— “where BRI appears to create the potential for debt sustainability problems, and where China is a dominant creditor in the key position to address those problems.” John Hurley, Scott Morris, and Gailyn Portelance, “Examining the Debt Implications of the Belt and Road Initiative from a Policy Perspective,” Center for Global Development Policy Paper, March 2018, 11.
ca Research Initiative at the Johns Hopkins University School of Advanced International Studies, notes that China’s debt write-offs have been “limited to interest-free Chinese government loans maturing at the end of the year,” which comprise a “relatively modest part of Chinese finance in Africa.” In January 2019, China agreed to waive $78.4 million worth of interest-free debt owed to it by Cameroon. In April 2019, the Ethiopian government announced China canceled interest-free loans that had matured at the end of 2018, without specifying the amount; the cancelation was on top of China agreeing in 2018 to extend the repayment period of Ethiopia’s loans for a major railway project.

In an attempt to counter corruption in BRI projects, in July 2019 China’s Central Commission for Discipline Inspection announced plans to embed its officers in countries with major BRI projects to monitor the activity of Chinese companies abroad. This follows the rollout of notices from China’s state-owned asset regulator in July 2018 and June 2019 requiring SOEs to increase supervision of overseas units and personnel. It remains to be seen whether Chinese officials’ new emphasis on transparency, debt sustainability, and environmental sustainability leads to a substantive course correction. Given its strategic interests in BRI, however, Beijing is unlikely to go beyond tactical adjustments to the initiative.

Myanmar Renegotiates BRI Project over Debt Concerns

Driven by concerns over excessive debt, in 2018 Myanmar renegotiated the cost and scope of the Kyaukpyu deep-water port—a major BRI project—from $7.2 billion to $1.3 billion. The initial plan for the project—approved under the previous military-backed government in 2015—consisted of a major deep-water port and industrial park. Under the new deal finalized in November 2018, Myanmar scaled down the size of the port and increased the stake held by the Myanmar government and local companies from 15 percent to 30 percent; a Chinese consortium led by state-owned investment company CITIC holds the remaining 70 percent stake.

For Myanmar officials, Sri Lanka’s experience—where in 2017, the Sri Lankan government granted a Chinese company a 99-year lease to operate Hambantota port after struggling to repay Chinese loans—raised concerns that the Kyaukpyu port project could leave Myanmar heavily indebted to China. In a July 2018 interview, Myanmar’s Planning and Finance Minister Soe Win emphasized the importance of paying attention to “lessons that we learned from our neighboring countries, that overinvestment is not good sometimes.”

The plans will build on a pilot program launched in Laos in 2017, where the Central Commission for Discipline Inspection embedded its officers in a railway project built by Chinese SOE China Railway Group and established a joint inspection team with its Laotian counterpart. Don Weinland, “China to Tackle Corruption in Belt and Road Projects,” Financial Times, July 18, 2019; Deng Hao, “Belt and Road a Path to Clean Governance,” China Daily, June 15, 2019.

The July 2018 notice outlines standards and required responses for cases of illegal management and investment of state assets by SOEs. The June 2019 notice requires SOEs to develop plans for holding individual employees accountable for their involvement in business operations that violate rules or incur major losses. Bai Yujie and Mo Yelin, “China Urges State Firms to Punish Rule Violations in Overseas Operations,” Caixin, June 15, 2019; Xinhua, “China Details Regulation on Central SOEs’ Asset Management,” July 30, 2018.
visor to State Counsellor Aung San Suu Kyi, said the new deal “reduces the financial risk dramatically” and demonstrates that “concerns about indebtedness and sovereignty have been and can be addressed…. This really could become a constructive model for countries that don’t have much leverage over a giant like China.”

According to media reports, the U.S. Agency for International Development (USAID) provided a team of technical experts to assist Myanmar in renegotiating the deal, at the request of the Myanmar government. USAID described the assistance as the “public investment planning” part of its broader economic growth programming for Myanmar, noting in a statement, “This is part of our consistent position to help governments throughout the region interested in developing the technical capacity to do the due diligence needed to assess possible investments and projects—regardless of the source of financing.” Other Western countries, including the United Kingdom and Australia, reportedly provided Myanmar with similar assistance.

**Limitations to Shaping Multilateral Trade Rules and Promoting the Renminbi**

Beyond infrastructure investment, Beijing seeks to leverage its economic clout in the areas of trade, currency, and payments to challenge the primacy of U.S.-dominated financial systems. In the trade arena, Beijing has sought to shape multilateral trade rules, but other countries’ participation in multilateral fora has diluted China’s ability to establish its trade preferences. In his testimony to the Commission, Rush Doshi, director of the Brookings Institution’s China Strategy Initiative, described how the Regional Comprehensive Economic Partnership (RCEP) illustrates “both … Chinese-order building ambitions and … Asian resistance, as well as … how China’s agenda can stall when it is multilateralized.” China’s “lofty leadership ambitions” for RCEP have run into obstacles from regional countries, particularly Australia, India, and Japan. For example, Japan is reportedly pushing for RCEP to incorporate Comprehensive and Progressive Agreement for Trans-Pacific Partnership provisions on cross-border data flows and digital trade, something China is unlikely to agree to. Meanwhile, India has been reluctant to grant China the same import terms as Association of Southeast Asian Nations countries, fearing an influx of Chinese goods widening its already significant trade deficit with China.

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*RCEP is a multilateral free trade agreement under negotiation between Australia, China, India, Japan, New Zealand, South Korea, and the ten member states of the Association of Southeast Asian Nations. RCEP represents half of the world’s population and 32 percent of global GDP. Takashi Terada, “RCEP Negotiations and the Implications for the United States,” *National Bureau of Asian Research*, December 20, 2018.

†The Comprehensive and Progressive Agreement for Trans-Pacific Partnership is a free trade agreement between Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, and Vietnam signed in March 2018. Matthew Goodman, “From TPP to CPTPP,” *Center for Strategic and International Studies*, March 8, 2018.
The Chinese government continues to promote renminbi (RMB) internationalization to reduce its reliance on the U.S. dollar while enhancing its economic influence, but efforts to date have been limited by Beijing’s unwillingness to liberalize the country’s capital accounts. Despite becoming a world reserve currency in 2016, the RMB’s international use remains limited; as of April 2019 the RMB accounted for less than 2 percent of all global payments,* according to global interbank communications network SWIFT.† Beijing has made greater inroads regionally—by 2017, 40 percent of payments between China and countries in the Asia Pacific were conducted using the RMB, up from just 7 percent in 2012.174

China has sought to increase RMB internationalization through BRI, bilateral currency swaps, agreements with foreign central banks, and the use of Hong Kong as an RMB hub.175 To facilitate RMB internationalization and create an alternative to SWIFT, in 2015 Beijing launched the Cross-Border International Payments System (CIPS), its own interbank messaging and payments system.176 While CIPS transactions are growing rapidly (an 80 percent year-on-year increase to $3.77 trillion for 2018), it is nowhere close to rivaling SWIFT, which processes $5 trillion to $6 trillion in settlements daily.177 Nonetheless, Dr. Doshi assesses CIPS “not only insulates China from financial pressure but also increases its autonomy, giving the country control over all information that passes through its network, the power to help others bypass sanctions, and the ability to one day cut others off from the RMB-denominated system.”178 CIPS has been attractive for banks in countries targeted by U.S. sanctions, such as Russia and Turkey, which have sought to reduce their reliance on the U.S. dollar.‡

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**Global 5G Backlash**

Huawei is positioning itself as a global leader in 5G, the next generation of wireless communications.§ However, Huawei faces growing international scrutiny as some countries rethink their relationship with the company over the national security concerns posed by its close ties to the Chinese government. Huawei has largely been blocked from the U.S. telecommunications equipment market due to concerns the company could build backdoors in its products to provide the Chinese government access into U.S. networks.179 At the same time, the U.S. government is trying to persuade its allies and partners not to allow Huawei

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* In comparison, the U.S. dollar was used in about 41 percent of transactions processed during the same period. SWIFT, “RMB Tracker: Monthly Reporting and Statistics on Renminbi (RMB) Progress towards Becoming an International Currency,” May 29, 2019.

† SWIFT is a global financial messaging network used by banks and other financial institutions to securely send and receive information. SWIFT, “SWIFT History.” [https://www.swift.com/about-us/history](https://www.swift.com/about-us/history)

‡ As of April 2019, Russia had the second-highest number of banks outside of China participating in CIPS at 23 banks, after Japan (at 30 banks), while Turkey had 11 banks participating in CIPS. Kazuhiro Kida, Masayuki Kubota, and Yusho Cho, “Rise of the Yuan: China-Based Payment Settlements Jump 80 Percent,” Nikkei Asian Review, May 20, 2019; Karen Yeung, “Why China and Russia Are Struggling to Abandon the U.S. Dollar and Forge a Yuan-Ruble Deal,” South China Morning Post, January 15, 2019.

Global 5G Backlash—Continued

to build their 5G networks. In February 2019, U.S. Secretary of State Mike Pompeo warned the United States would not be able to partner with or share intelligence information with countries that use Huawei technology in their information technology systems, stating, “We’re not going to put American information at risk.”

U.S. allies and partners differ as to whether to impose a ban on the use of Huawei’s 5G equipment or work to mitigate the risks. Australia and Japan have effectively blocked Huawei from providing 5G technology, but other U.S. allies and partners, despite sharing U.S. concerns about Huawei’s security risks, believe they can mitigate the risks through rigorous security standards and testing. For example, in April 2019 Germany’s telecommunications regulator announced its position “is that no equipment supplier, including Huawei, should, or may, be specifically excluded.” A spokesperson for Germany’s Federal Interior Ministry said in February 2019 that the ministry’s “focus is on adapting the necessary security requirements so that the security of these networks will be guaranteed even if there are potentially untrustworthy manufacturers on the market.”

Like Germany, France is against an outright ban on Huawei, preferring instead to focus on tightening the rules governing the security of its 5G network. In July 2019, the French parliament passed a new law requiring telecommunications operators and service providers to obtain approval from the French prime minister for their 5G network projects; the prime minister can block such activities if they pose a “serious risk” to national defense and security. A March 2019 report from the North Atlantic Treaty Organization Cooperative Cyber Defense Center of Excellence argues “the issue of Huawei 5G deployment must be assessed in a broader geopolitical context,” warning “the fear remains that adopting 5G technology from Huawei would introduce a reliance on equipment which can be controlled by the Chinese intelligence services and the military in both peacetime and crisis.”

For many countries, Huawei’s price and quality remain a significant draw. In April 2019, Huawei won a contract to supply 5G equipment to the Netherlands’ leading wireless carrier by underbidding the existing vendor, Ericsson, by 60 percent. South Korea is letting individual carriers make their own decisions on selecting network equipment vendors; LG Uplus, the smallest of South Korea’s three mobile carriers, uses Huawei equipment in its 5G network.

Fears of an Untested Military

A second major challenge Beijing faces in achieving its foreign policy aims stems from senior leaders’ concerns about the competency of China’s untested military. China has not engaged in large-scale military operations since its 1979 invasion of Vietnam, and Chinese leaders since that time have expressed concerns over the PLA’s ability to prevail against an adversary in a modern military
Four decades of PLA modernization efforts have produced an impressive inventory of advanced ships, aircraft, missiles, and space and cyber capabilities that in some cases rival those of the United States.

Nevertheless, successive generations of Chinese leaders have noted a number of deficiencies in the PLA's operational abilities, many of which do not appear to have improved significantly relative to the United States or even China's regional competitors. General Secretary Xi has been the most critical of the PLA's warfighting competence of any recent Chinese leader, publicly excoriating military leaders for a range of shortcomings that undermine the PLA's ability to fight and win a modern war. While the PLA has appeared to redouble efforts to improve its capabilities and competence, after six years many of the same shortcomings remain, with some potentially exacerbated by General Secretary Xi's restructuring of the PLA. In particular, these problems center on weaknesses in the PLA's joint warfighting capabilities and ability to produce a competent officer corps through its military education and training system.

Concerns over PLA Competence

CCP leaders' concerns over the PLA's warfighting competence center on the force's lack of recent combat experience. In 2009, shortly before he was elevated to the CMC, now CMC Vice Chairman General Zhang Youxia—himself a veteran of China's Vietnam war—noted the PLA's lack of combat experience and the potential that it had fallen behind its competitors, warning that “the gap between the PLA and foreign militaries is growing day by day.” In testimony before the Commission, Dennis Blasko, a former U.S. military attaché in Beijing, argued that in recent years the frequency of criticism of the PLA's lack of operational experience and combat mindset has increased. For instance, while the term “peace disease” was used in Chinese media as early as the late 1980s, references to this and related terms such as “peacetime [bad] habits” have spiked in recent years, with the terms appearing roughly 565 times in the PLA Daily from 2012 to mid-2018. In 2018, likely in part to emphasize his seriousness in ridding the PLA of these practices, General Secretary Xi personally issued the PLA's annual order directing the start of that year's military training cycle—the first time since the founding of the People's Republic of China that a CMC chairman had done so directly. Using similar language to his 2018 address, General Secretary Xi instructed the PLA in 2019 to “rectify … peacetime malpractices” in its training efforts, indicating the persistent nature of the problems six years into his tenure as CMC chairman.

Beijing's concerns over the PLA's competence have also manifested in the scathing critiques General Secretary Xi and senior military leaders have leveled against the PLA's combat readiness and the command ability of its officer corps. Chinese leaders since Deng Xiaoping have criticized the PLA for its inadequate preparations to fight a modern war, with top leaders disapproving of the force's “Two

*The PLA's invasion of Vietnam in 1979 and the cross-border incursions that followed it into the mid to late-1980s were China's last experiences with large-scale combat operations. Many Chinese and foreign observers view the PLA's invasion as an operational failure that continues to cast a shadow over the PLA. Charlie Gao, “This Is the War That Made China’s Military What It Is Today,” National Interest, November 14, 2018.
Inabilities,” which identify the PLA as having insufficient ability to fight and its officers as having insufficient ability to command a modern war. Since General Secretary Xi assumed the CMC chairmanship, several new formulas have been used to augment earlier criticism of the PLA that question the PLA’s ability to fight and win a conflict against a capable, modern adversary. Primary among these are the so-called “Five Incapables”—referring to the inability of too many PLA officers to effectively judge the military situation, understand their orders, make operational decisions, direct troops in combat, and handle unforeseen battlefield developments.

Dedicated efforts by the PLA to improve the content and realism of exercises and officer training do not appear to have resolved these issues. In the most recent version of its official training guidelines, issued in 2018, the PLA emphasized realistic combat and joint training across all warfare domains while highlighting the command shortcomings characterized by the “peace disease” and Five Incapables. Following the rollout of the new guidelines, each of the services held training events focused on overcoming these shortfalls and tested senior officers’ knowledge of missions, operational scenarios, and understanding superiors’ intentions.

Despite these efforts, according to calculations by Alastair Iain Johnston, professor of government at Harvard University, references to the Five Incapables in PLA press have spiked since they were first introduced in 2015, doubling from 40 mentions in the PLA Daily in 2016 to nearly 80 in 2018. Overall mention of terms critiquing PLA capabilities jumped from less than 20 in 2012 to nearly 150 in 2018. According to Mr. Blasko, an important function of the PLA’s self-criticism is to identify problems as part of the force’s long-term modernization efforts. Nevertheless, he notes, the increasing scope and frequency of these critiques under General Secretary Xi effectively “casts doubt over the senior party and military leadership’s confidence in the PLA’s ability to prevail in battle against a modern enemy.”

Shortfalls in the Military Education and Training System

Central to the shortfalls Chinese leaders perceive in the PLA’s operational and operational command capabilities is the longstanding and systemic failure of China’s military education system to produce a competent officer corps. To resolve this issue, the PLA has overhauled its military academies and training standards in an attempt to improve the quality of joint and service-level education. However, educational reforms have yet to produce the quality military leaders sought by Beijing. In a September 2018 address, General Secretary Xi recognized the PLA’s educational system had seen some improvement, but concluded the present “system of personnel training … does not match the mission of fulfilling the new era, and it does not match the new organizational form of [China’s] military…. [M]ilitary vocational education is still in the initial explo-

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*I In his testimony before the Commission, Mr. Blasko argued that the “shortcomings in today’s PLA commanders and staffs represent multiple systemic failures to execute Jiang Zemin’s guidance from two decades ago that ‘we must train qualified personnel first, for we would rather let qualified personnel wait for equipment than equipment wait for qualified personnel.’” U.S.-China Economic and Security Review Commission, Hearing on What Keeps Xi Up at Night: Beijing’s Internal and External Challenges, written testimony of Dennis J. Blasko, February 7, 2019, 14.
ration stage.” In 2019, he reiterated these concerns, stating that “the development of joint command officers is an urgent priority for addressing the shortage of qualified personnel.208

**Pushback against Chinese Interference Activities**

A third challenge to China’s ambitions abroad comes from the growing international pushback against China’s influence and interference activities. In recent years, a number of countries from Asia to Europe and the Western Hemisphere have recognized the coercive nature of China’s influence operations and other “sharp power” efforts and have begun taking steps to counter what they perceive as the threatening elements of these activities.† EU and UN members have likewise taken steps to limit CCP efforts to change international norms on human rights, sovereignty, and freedom of expression. (For more information on Chinese influence operations in Oceania and Singapore, see Chapter 4, Section 4, “Changing Regional Dynamics: Oceania and Singapore.”)

**Coordination Grows among U.S. Allies**

In the last several years, U.S. allies and partners around the globe have taken significant steps to expose and counteract Chinese influence operations. Lindsey Ford, director of political-security affairs at the Asia Society Policy Institute, testified to the Commission that “democracies such as Australia and New Zealand have raised concerns that China has leveraged ties to elite policy, expert, and business communities to exert political pressure and shape domestic policy debates.”209 A major component of these countries’ response has been action by the Five Eyes intelligence-sharing countries—the United States, Australia, Canada, the United Kingdom, and New Zealand—to counter Chinese influence efforts through enhancing intelligence-sharing, improving communication with their citizens on the subject of Chinese influence activities, and expanding information-sharing with non-Five Eyes partners. In August 2018, in a reference clearly including China, Five Eyes countries issued a statement condemning “the coercive, deceptive, and clandestine activities of foreign governments, actors, and their proxies to sow discord, manipulate public discourse, bias the development of policy, or disrupt markets for the purpose of undermining our nations and our

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*The term “sharp power” describes how authoritarian regimes like China seek to undermine democratic institutions in other countries. Many of these activities rely on neither coercive nor persuasive power—hard and soft power, respectively—because they aim not to influence the policies of states directly but rather to “pierce, penetrate, or perforate” their information environments. This differs from soft power, which focuses specifically on a country’s "ability to affect others by attraction and persuasion rather than through the hard power of coercion and payment." Some examples of the CCP using sharp power include encouraging self-censorship by Western academics, use of Chinese language media outlets abroad to shape narratives, and use of donations to gain political influence. For more on China’s application of sharp power see U.S.-China Economic and Security Review Commission, Chapter 3, Section 2, “China’s Relations with U.S. Allies and Partners” in 2018 Annual Report to Congress, November 2018, 315; Juan Pablo Cardenal et al., “Sharp Power: Rising Authoritarian Influence,” National Endowment for Democracy, December 2017, 6.

† In addition to the United States, countries including Australia, Canada, France, Germany, Japan, New Zealand, Singapore, and the United Kingdom have publicly warned that China is engaging in influence operations that have interfered with and otherwise adversely affected their domestic politics, economy, and societal wellbeing. Larry Diamond et al., “Chinese Influence and American Interests: Promoting Constructive Vigilance,” Hoover Institution, November 2018, 163; Noah Barkin, “Exclusive: Five Eyes Intelligence Alliance Builds Coalition to Counter China,” Reuters, October 12, 2018.
allies.” In early 2018, Five Eyes countries began sharing information about Chinese influence operations with Japan, Germany, and France to foster greater cooperation. EU countries have also begun to demonstrate their concerns over China’s efforts to suppress freedom of speech, encourage censorship in film and academia, and spread propaganda.

**Pushback in the UN to Chinese Amendment Language**

Resistance has also emerged within the UN to Chinese efforts to insert the CCP’s preferred language into UN documents to alter international norms. The CCP has sought to revise language and downplay the importance of human rights and development norms to better align with its emphasis on state sovereignty. For example, the CCP has tried to shift the UN’s focus on human rights from emphasizing “political and individual rights” of people to a focus on “economic and social rights.”

Although Beijing has had a few notable successes, such as inserting “Xi Jinping Thought” into a 2017 resolution that called for “promoting development over human rights,” many European governments—along with countries as diverse as Afghanistan, Australia, Japan, Mexico, Morocco, Peru, and Paraguay—have consistently opposed Chinese-sponsored resolutions and amendments at the UN Human Rights Council. For example, in March 2016, Chinese efforts to water down internationally accepted language on “human rights defenders” was voted down, and a 2017 amendment that would weaken state obligations to cooperate with UN Human Rights Council mechanisms was similarly defeated. In 2018, several amendments pushed by China dealing with civil society and territorial sovereignty, to include how nongovernmental organizations should operate and respect host country sovereignty, also failed to pass after meeting firm opposition.

**Countering Hard Power**

Finally, assertive Chinese military activities in the East and South China seas have prompted mounting regional pushback. Many Indo-Pacific countries have undertaken efforts to counter China’s activities in the region through enhanced partnership building, military modernization, and increased military cooperation with countries outside the Indo-Pacific.

**Enhanced Partnership Building**

In a November 2018 speech, Commander of U.S. Indo-Pacific Command Admiral Philip Davidson identified maritime partnership building as a way to ensure a free and open Indo-Pacific and help countries counter China’s malign activities and influence in the region. Australia, Singapore, Japan, Vietnam, and India are a few of the countries in the region that have taken steps to expand partnerships and counterbalance China’s expanding presence. (For more information on pushback from Australia and Singapore on China’s growing regional influence, see Chapter 4, Section 4, “Changing Regional Dynamics: Oceania and Singapore.”)

- **Australia**: To counter China’s growing regional presence, particularly in Oceania, Australia has sought to strengthen its se-
curity relationships. In July 2019, Australia’s Defense Minister Linda Reynolds indicated Canberra would accelerate its plans to counter Chinese influence in the region by creating a military unit that would strengthen capacity, resilience, and interoperability with Australia’s Pacific Island partners. The unit will focus on conducting security operations, humanitarian assistance, disaster relief, and peacekeeping in the region. In addition to creating this unit, Australia is also pursuing and maintaining security relationships with a number of its Pacific Island neighbors, including Vanuatu, Fiji, and the Solomon Islands. Furthermore, Canberra has partnered with Washington to construct a naval base in Papua New Guinea in part as an effort to curb China’s growing influence in the country and as a response to Beijing’s pursuit of a base in Vanuatu.

• Singapore: Singapore seeks stability in the South China Sea and supports the U.S. Free and Open Indo-Pacific strategy. While Singapore maintains a balanced relationship with China and has conducted training with the PLA, it allows the United States, Australia, and New Zealand to maintain a routine naval presence in the country. Singapore also has a strong security relationship with India and supports Indian engagement in Southeast Asia, particularly concerning India’s support for a Free and Open Indo-Pacific and its commitment to maintaining secure sea lines of communication between the Indian Ocean and the South China Sea. Recent agreements between Singapore and India aimed at strengthening this relationship include the 2017 renewal of a five-year training pact allowing Singapore’s air force to train in India, and a 2018 agreement concerning mutual naval coordination, logistics, and services support during port calls and military exercises.

• Japan: While Japan maintains a strong alliance with the United States, Tokyo has also increased its regional influence by enhancing its outreach abroad through the provision of diplomatic, economic, and security assistance. Japan has sought in particular to strengthen its military ties with many Southeast Asian countries, donating patrol boats, maritime surveillance aircraft, and spare helicopter parts to the Philippines, patrol boats to Vietnam, and retired P-3 Orion anti-submarine aircraft to Malaysia.

• Vietnam: While seeking to stabilize its relationship with Beijing, Hanoi is strengthening its partnerships with the United States, Australia, India, Japan, and New Zealand. In 2018, Vietnam and India pledged to continue defense collaboration to include senior dialogues, arms procurement, and port calls for navy and coast guard ships, and reaffirmed the importance of upholding freedom of navigation and overflight in the South China Sea. Also in 2018, Vietnam and the United States worked to strengthen security ties through a series of exchanges between their coast guards, the first port call by a U.S. aircraft carrier since the end of the Vietnam War, and Vietnam’s participation in the U.S.-hosted biennial Rim of the Pacific exercise.
India: New Delhi’s concerns over China’s growing presence in the Indian Ocean region have spurred its interest in deepening security partnerships with Japan and the United States.\textsuperscript{229} India and the United States established a direct hotline and signed a Communications Compatibility and Security Agreement in 2018, allowing the two countries to quickly and securely exchange sensitive information.\textsuperscript{230} India and Japan continue to strengthen their economic and security relationship, with Japan becoming a permanent member of the annual U.S.-India Malabar naval exercise in 2015.\textsuperscript{231} The two have also agreed to create a new Foreign and Defense Ministerial Dialogue to strengthen bilateral security cooperation and will conduct exercises in 2019 between their air and ground forces.\textsuperscript{232} India has also increased its naval presence in the South China Sea, conducting several exercises in the area in 2019 that included its second bilateral naval exercise with Vietnam; a six-day exercise with the United States, Japan, and the Philippines; and a separate exercise with France.\textsuperscript{233}

Regional Military Modernization as a Response to China’s Growing Assertiveness

China’s more than four-decades-long effort to modernize its military has spurred other regional countries to accelerate their own modernization efforts. Japan has taken steps to acquire expeditionary capabilities it has not possessed since World War II, and Vietnam has acquired high-end Russian military equipment to develop its own anti-access deterrent in the South China Sea. Finally, India has stepped up efforts to build a military capable of fighting both Pakistan and China.

Japan’s emerging expeditionary capabilities: Japan is modernizing its military to counter increasing pressure from China in the air and maritime domains, as well as to improve the defensive capabilities of its southwest islands.\textsuperscript{234} Tokyo is specifically focused on establishing an amphibious rapid deployment brigade to improve the expeditionary capability of its Ground Self-Defense Force, acquiring large numbers of F-35B fighters, modifying its Izumo-class helicopter destroyer to support F-35B flight operations, and improving the defensive capabilities of its southwest islands by deploying shore-based antiship cruise missiles to several key locations in the Ryukyu island chain.\textsuperscript{235} Since legislation was passed in 2015 allowing Japan’s military to participate in collective self-defense, Tokyo has deployed its ships to participate in escort operations of U.S. ships and aircraft in the East and South China seas, and has participated in bilateral exercises in the South China Sea.\textsuperscript{236} The administration of Prime Minister Shinzo Abe may seek to hold a vote in 2020 to amend “Article 9” of the Japanese constitution to allow for the development of offensive capabilities, despite having failed to retain enough support to pass the measure after the July 2019 Diet election.\textsuperscript{237}
• **Vietnam building its own area denial capabilities:** To address its current disadvantages vis-à-vis Beijing in the maritime domain, Hanoi has sought to enhance its area denial capabilities by purchasing advanced military equipment from Russia, including 36 Su-30MKK attack aircraft, 6 KILO-class attack submarines, and two S-300 surface-to-air missile (SAM) systems. In 2019, Vietnam also registered its interest in purchasing Russia’s advanced S-400 SAM systems.

• **India recapitalizing air and maritime capabilities:** Since 2015, India’s Defense Ministry has signed 188 defense acquisition contracts, including an October 2018 contract with Russia for S-400 SAM systems and a deal for advanced Israeli SAM systems to be installed on Indian warships. In 2019, India is scheduled to receive the first half of the 36 French-built fighter-bombers New Delhi ordered in 2015, and has already begun receiving the first of 22 AH-64E Apache attack helicopters and 15 Chinook heavy-lift helicopters built by Boeing. The Indian Navy anticipates commissioning six new Scorpene-class submarines and a new indigenously-built aircraft carrier between 2020 and 2021.

**Global Powers Increasing Military Presence in the Indo-Pacific**

A number of U.S. allies and partners, including European allies, have also demonstrated their willingness to more publicly broadcast their military presence in the Indo-Pacific as their willingness to stand up to Beijing has increased.

• **International military presence increasing in the South China Sea:** Several countries have conducted patrols in the South China Sea in tandem with or in addition to U.S. freedom of navigation operations in the region—although no other country has yet joined the United States in navigating within 12 nautical miles of disputed features. Australia’s navy regularly conducts presence patrols in the South China Sea, and in August 2018 the United Kingdom conducted a South China Sea transit with an amphibious assault ship near the Paracel Islands. Japan, France, and Canada have also increased their military activities in the South China Sea.

• **Increasingly complex multilateral exercises:** In May 2019, the U.S. Navy, Japan Maritime Self-Defense Force, Philippines Navy, and Indian Navy conducted joint naval drills in the South China Sea for the first time in a four-day event demonstrating military presence and cooperation. Also in May 2019, the U.S. Navy dispatched a guided-missile destroyer to the Indian Ocean to participate in a large-scale exercise—alongside ships from France, Japan, and Australia—focused on live-fire and other combat drills. The U.S. Army has also announced plans to carry out in 2020 a new exercise known as Defender Pacific, focusing on a South China Sea scenario and including the Philippines, Thailand, Malaysia, Indonesia, and Brunei.
Implications for the United States

In recent years, China has promoted itself abroad as an alternative, authoritarian-led model for other countries to emulate on an inexorable drive toward achieving regional and even global leadership. In reality, the prospects for Beijing’s ability to achieve its goals are far more uncertain than they might appear. The CCP faces significant internal and external challenges that constrain its ability to sustain economic growth, project power, and spread its influence globally. China’s leadership is acutely aware of these challenges and is making a concerted effort to overcome them. Ultimately, the extent to which Beijing can address these vulnerabilities—partially, successfully, or ineffectively—affects its ability to contest U.S. leadership and interests.

In the economic realm, Chinese policymakers credit their state-led economic model for the country’s rapid growth and view it as critical to China’s continued prosperity. Beijing’s doubling down on its economic model likely will prolong U.S.-China trade frictions. As trade tensions drag on, U.S. companies may need to reassess their positions.

Moves by the United States and its allies and partners to block China’s access to critical technologies may have the unintended effect of accelerating China’s innovation drive, due to Beijing’s assessment that technological self-reliance and dominance are fundamental to China’s future economic and military competitiveness. China’s military-civil fusion strategy, which blends military, civilian, and academic research and development, could put U.S. industries at risk. U.S. and foreign companies collaborating with Chinese entities may be participants in China’s military-civil fusion system.

While Beijing’s economic statecraft has had limited success, China is learning and progressing along what Dr. Doshi has described as a “superpower learning curve.” Notably, amid criticism of BRI, Beijing is rethinking how it selects and implements projects and presents the initiative to overseas audiences. BRI’s roster continues to grow because significant infrastructure gaps persist globally and Beijing faces few competitors in infrastructure financing. China’s lack of transparency in its lending raises concerns regarding not only Beijing’s free riding on previous international debt relief efforts, but also the potential for increased risks of debt distress in low-income countries. As a geopolitical strategy, BRI’s breadth and ambiguity means it does not need to succeed everywhere to undermine the rules-based international order. BRI continues to make China a major creditor in regions that are strategically important to the United States, giving Beijing increased political influence.

Finally, China’s frequent deployments of the PLA and paramilitary forces to support its regional sovereignty claims could reflect an increased willingness to employ military force—especially against a less-capable opponent in a limited conflict—if Beijing were confident Washington would not intervene. Nevertheless, Beijing’s concerns over the PLA’s warfighting capabilities may lessen senior Chinese leaders’ willingness to initiate a conflict that could prompt the intervention of a modern, capable adversary such as the United States, at least in the near term. Instead, Beijing likely will continue to rely on coercive actions below the threshold of armed conflict by its
coast guard, maritime militia, and naval forces to avoid risking an outright military confrontation. Beijing’s calculus regarding the use of force may change as the PLA continues its modernization drive. For the foreseeable future, however, the uncomfortable status quo of low-level Chinese coercion and its attendant risk of accidents and miscalculation may rank among the most pressing challenges for the United States and its allies.
ENDNOTES FOR CHAPTER 2


17. Peter Lorentzen and Xi Lu, “Personal Ties, Meritocracy, and China’s Anti-Corruption Campaign,” November 21, 2018, 4.


162


164


