January 27th, 2022

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Testimony before the U.S. -China Economic and Security Review Commission:

Hearing on "CCP Decision-Making and the 20th Party Congress"

Please describe the economic policy decision-making apparatus in China. What kinds of institutions are used to formulate, debate, and communicate economic policy? What kind of information does the political leadership use in making these decisions, and how reliable is that information?

China's economic policy and decision-making structure has developed into an advanced and complex one-party-state, featuring various bureaucratic-administrative systems e.g., ministries, regulatory bodies e.g., China Banking and Insurance Regulatory Commission, and financial institutions e.g., state banks. On top of this, the CCP (from now on used interchangeably with "party") is systematically integrated at all levels of decision-making. Party leaders occupy both the "commanding heights" of national strategic policymaking and agenda-setting, as well as the leading posts in each and every administrative organization. The authoritarian, party-dominated structure of the political system therefore defines economic policymaking. This hierarchical division of labor (put somewhat simplistically) between strategic leadership and coordination by the CCP, and administration and implementation by state bureaucracies, is reflected in the decision-making structure. The scope of the party's authority is perhaps best put by Xi himself: "In party, government, military, society and education, in the East, West, South, North, and Center, the party rules all." For economic policy, some of the most important institutions are the following (organized approximately by authority in the system):

The Central Commission for Comprehensively Deepening Reform (CCDR) has become the powerhouse for Xi Jinping's "top-level design" policymaking, issuing policy on a broad array of topics, including economic issues. Crucially, the CCDR is a party organization. It was established by and is chaired by Xi who conducts every meeting, while Wang Huning acts as a Managing Director. It has convened 63 times since its first meeting in January 2014, issuing more than 500 policy documents. The full list of members is unknown but at least 40 of the most senior officials from key central-level state and party organizations are members. It is organized into six sub-groups, each with their own policy focus. Relevant for economic issues is the "Work group on economic and ecological civilization system reform," managed by Politburo member and chief economic planner Liu He. In terms of authority, it outranks ministries, and because its led by Xi Jinping and senior leaders oversee the work groups, its political clout effectively surpasses China's cabinet, the State Council. The CCDR's mission is to steer and accelerate structural reforms under guidance by the central leadership. Pertaining to economic policymaking, this includes but is not limited to structural reforms in the financial sector, market regulation, and trade policy. The CCDR's work groups are known to actively engage in the policy formulation process by advising ministries charged with drafting specific policies. Some policies are also deliberated and even passed during the CCDR meetings before they are officially legislated by the State Council or ministries later on.

The **Central Commission for Economy and Finance** (CCEF) is somewhat similar to the CCDR, although more specialized in its policy scope. Like the CCDR, it is chaired by Xi Jinping, while Liu He acts as Managing Director. Reliable information about the CCEF is sparse, but it is known to be used as the top-level committee for deliberation of economic policy, albeit not as involved in the concrete policy formulation as the CCDR. It is a party organization, reporting directly to Xi Jinping, with attendance from most, if not all, relevant central-level officials.

The **National Development and Reform Commission** (NDRC) remains one of the most important organizations for macroeconomic planning, pricing policy, market regulation, and industrial/sectoral development issues. Despite its name, it is a ministry-rank unit under the State Council and it enjoys significant authority compared to other ministries because of its broad policy mandate and large group of leaders (He Lifeng as director and 8 vice-directors). Under Xi, the authorities formerly vested in the NDRC have been dismantled in favor of other central party and state agencies (notably the CCDR), and it has lost its (informal) status as the "small State Council." The NDRC helps formulate China's industrial policies and sectoral planning e.g., energy and infrastructure, and strategic planning such as the five-year plans and China's decarbonization policy. As key party officials of the central party-state, the most senior NDRC leaders are also members in the CCDR and CCEF. Together with the Ministry of Finance, the NDRC is one of the most influential ministries. It regularly receives input and normative guidance from the CCDR. An example that reflects the hierarchy of decision-making authority between central party organs and state administration.

The **People's Bank of China** (PBoC) serves as China's central bank in charge of monetary policy, formally organized under the State Council. Its dual leadership team in comprised of Governor Yi Gang, and Party Secretary Guo Shuqing. Guo is also in charge of the China Banking and Insurance Regulatory Commission. While the PBoC enjoys some degree of independence, it is required to implement CCP policy. Guo Shuqing has established himself as a capable and skilled leader and a key official for fighting financial risks and implementing tighter financial regulation.

The **Ministry of Finance** (MoF) handles annual budgets, public finance, and other economic regulations, but shares (or contests) macroeconomic responsibilities with the NDRC. The MoF also serves as controlling shareholder of several large sovereign wealth funds. On several occasions, the MoF has received guidance from the CCDR, and its Minister Liu Kun also serves as its Party Secretary and is a member of the CCDR and CCEF.

The **National Bureau of Statistics** (NBS) is not a policymaking organ, but relevant here because it oversees collecting and compiling data, both at central and local levels. China has long had issues with data reliability, and it is generally acknowledged that the misreporting of growth, fiscal deficits, expenditures etc. remain a problem. Corruption and poor supervision in the NBS have exacerbated this problem. One response to this problem has been the establishment of a central audit commission (a party organ), which is supposed to add another level of check to prevent fudged numbers in fiscal expenditure and distorted economic reporting.

Information asymmetry has been identified as a problem for sound policymaking even by top leaders, such as Li Keqiang who reportedly has his own measure of estimating economic growth (the so-called Li Keqiang index). More recently, former Minister of Finance Lou Jiwei warned that officials report distorted numbers to the center and “accentuate the positive, and play down the negatives,” leading to serious issues in China’s ability to react to and prevent economic risks. The problem often lies with the career incentives local officials face, which remain tied to a list of performance indicators. Generating growth and stability has long been the most important KPI for leading cadres, and although this is meant to change with Xi Jinping’s intention to shift from quantitative to qualitative growth (meaning more inclusive and sustainable growth), for most parts it will likely take some time before the long-established focus on growth as a key selector for promotion can change. The party-state has other systems of obtaining information, such as the CCP’s own information system, and internal reports compiled by state media. These channels are secret, and it is unknown how systematic and reliable these sources are i.e., not affected by the same incentive issue. The vastly increased number and scope of auditing and inspection tours by CCP’s Central Audit Commission, CCP discipline inspection officers, and more specialized audits e.g., for environmental policy, setting up camp for weeks to go through the books of local governments, state-owned enterprises, and even ministries, suggest that the data problem is pretty serious, and that the central government does not trust data unless trusted personnel verify it.

> Who are the key individual players in formulating economic policy in China’s political leadership? What is the role of Xi Jinping in deliberating economic policy? What matters more, people or process?

Xi Jinping has caused significant change to the political leadership system. It is clear that Xi has worked hard and been successful to shape decision-making processes around his person. He is the designated “leadership core” of the central leadership and the party and his thoughts have been declared party doctrine, therefore following party policy now essentially means for all party officials to follow Xi’s lead. At the same time, Xi Jinping advocates predictable and stable processes in governance, if they adhere to the central party line, i.e., the political-ideological priorities outlined in Xi Jinping thought. This has important ramifications for policymaking also in the economy. While Xi himself is no economist and is, to my knowledge, much more engaged in political and ideological issues, a number of trusted officials around him shape macroeconomic policy.

Wang Huning, member of the Politburo Standing Committee, is believed to be trusted by Xi Jinping and has been the main architect of recent party ideology. He has only indirect but important impact on policymaking. His ideas have long advocated a neo-authoritarian turn, with a strong party apparatus in charge of an activist state apparatus. The social theory behind his ideology views economic activity e.g., market transactions, as just one form of social activity and hence must be governed according to political (CCP) objectives just like any other social activity. The strong notion of party hegemony in his thinking predicates far-reaching regulatory oversight and steerage of the economy at large, including enlisting the private sector to contribute to the party's political objectives.

Liu He is one of the key leaders in economic policy and is believed to have friendship relations with Xi since childhood. As Xi's most trusted economic adviser, he often fills in for Xi as negotiator and key speaker with international counterparts. Liu is also in charge of coordinating much of the top-level economic policy, and through his posts in core executive organs, e.g. the Politburo and the CCDR's sub-group on economic reform, membership in the CCEF and others, he sits at the table in all strategic decision-making on economic policy.

Guo Shuqing has emerged as a main financial sector troubleshooter. He is both Party Secretary of the People's Bank of China, and Director of the China Banking and Insurance Regulatory Commission, therefore he is a key regulator in the financial sector. He appears to be a driving force behind the current "battle against financial risks," which is the main challenge to regime stability. Although not considered a direct ally of Xi, Guo mirrors Xi's position of favoring a strong state and party authority over finance and economy. This is especially visible in China's large private financial companies which he has stated have become "too big to fail," and hence must be aggressively regulated.

He Lifeng, Chairman of the NDRC, is a close ally of Xi Jinping. Given the substantial policy reach of the NDRC, and He's presence in the party commissions, Xi can trust him in matters regarding macroeconomic planning, industrial development, and market reforms – fields of influence of the NDRC.

Large provinces such as Guangdong, Shanghai and Tianjin are substantial economies even on an international scale (Guangdong's, GDP in 2019 was USD 1.6 trillion), and their leadership is expected to engage in policy experimentation and piloting. Their party secretaries are high ranking cadres with seats in the Politburo and they are therefore important spearheads for implementing central guidance and to develop the specific policy responses at local levels. Especially in the case of MNCs in China, these officials have a large impact on trade zones, large FDI inflows, and local industrial policies.

A number of think tanks and research centers, e.g. the State Council Development Research Center and the CCP Policy Research Center, are contributing to the formulation of policy by providing research, scientific input and political guidance.

What are the different strains of economic policy thinking in China's leadership today? Who advocates for these different lines of thinking, either persons or institutions, and how meaningful is their ability to shape economic policy?

It is hard to identify any meaningful opposition, or even an influential group of thinkers other than the state-capitalist authoritarian line pushed by Xi and his supporters. The previously commonly used identification of two general camps in the leadership now appear obsolete under Xi Jinping. Before he came to power, you had one camp of "reformers" or "liberals" who were in favor of market liberalization and political reforms, and another, the "leftists" or “conservatives” who were more inclined towards authoritarian governance and statist intervention in the economy. Xi Jinping has successfully staffed most key positions with people he trusts, and raised the stakes for opposition. His elevation to core of the party, and the institutionalization of Xi Jinping thought as the party line, essentially means that any open opposition is a violation of party policy. Another key priority of Xi’s is the adoption of ideology in legal and regulatory norms, the impact of which is seen in extremely limited contesting streams of thought in the public and has most likely also squeezed room for internal discussions.

Many of those individuals formerly regarded as being “reformers” have either been pushed to the sidelines or now appear as supportive but less ideologically vocal technocrats in the administration. Liu He, Wang Qishan, and even Li Keqiang could be classified in this group, as they currently align their work with the Xi’s authoritarian state-capitalist model. Anecdotal evidence also suggests that individuals and consultative support units e.g., the State Council’s Development Research Center that are not part of Xi’s trusted environment, have lost their voice in policymaking. With few exceptions, all influential private think tanks in favor of policies that challenge party rule and state intervention have been closed. Academic debates and teaching materials considered critical of party-state policy have also been greatly limited.

What stresses in the economy are most likely to shape economic policy decision-making moving forward? How do you think Chinese leaders will determine priorities in the wake of the 20th Party Congress?
To what extent, if any, is the leadership comfortable with increased economic volatility arising from policy choices? What does this tell us about their vision for China’s economic future?

The current period, and especially 2022, will be shaped by the leadership’s utmost efforts for stability, primarily political, but also economic. More generally, the Xi administration follows a paradoxical path of trying to make markets more efficient and open, while also strengthening tools for state interventions. This conflicting policymaking of meaningful reform on the one hand, and an obsession with political control on the other, is likely to continue to define economic policymaking for the months and years to come. Especially with the 20th party congress approaching, the party will try to avoid any economic and social crises to the prevent destabilizing effects on the political elite. Recent events suggest that sectoral and regionally isolated social and economic costs are not an issue for Beijing *per se*, as long as overall regime stability is not endangered, and political objectives are served. The zero-covid strategy is a prime example of this, laying tremendous cost on individual businesses, local governments, and not least lockdown-affected citizens. What’s more, the sudden regulatory tightening of entire sectors such as the tutoring industry, destroying tens of thousands of jobs and shattering large businesses overnight, serves as proof that political and/or regulatory objectives weigh heavier than the socio-economic disruptions perceived as advancing them.

At the ideological level and until 2035, Xi has introduced a new growth paradigm. It’s a shift from quantitative growth targets towards “quality” growth that adds more value and distributes gains more equally. By and large the (still very unspecific) “common prosperity” program is an attempt to achieve this more inclusive development model. Technological selfreliance is growing in importance, and persistent international tensions and uncertainties feed into its rise as a core objective. Inequality remains a pressing concern, with a GINI coefficient of around five and rising. To counteract the rising inequality, structural redistribution mechanisms such as progressive income tax and property tax might have been discussed for some time. So far, given the challenging economic reality of slowing growth and sluggish demand, Beijing has shirked back from these more intrusive – and unpopular – mechanisms, even as they might be necessary to finance the rising cost of China's public services and welfare systems. For now, calls for "patriotic entrepreneurship" and charity are growing, in which profitable private companies and wealthy individuals are strongly encouraged to donate to the national project of building a strong, party-led China.

However, stable economic performance remains the core underpinning of regime legitimacy, and given the downward trend of China's growth, and the difficulties following the Covid-19 pandemic, actions likely to dampen economic activity at large and beyond specific industries or regions have currently been delayed, even those announced over past months. To this end, Vice-Director of the CCEF, Han Wenxiu, pointed out that macroeconomic stability is not merely an economic question, but a political objective. This could mean somewhat more pragmatism and flexibility than suggested in Xi's speeches, at least during this politically important year.

Systemic financial risks are the most challenging of the "three tough battles" that the party faces, according to the leadership itself (the other two are pollution and poverty). They include, fiscal deficits and government debt at local levels and the financial trouble many large business empires face such as giant property developers Evergrande or Shimao. With growth levels falling, debt maturing after decades of high investment levels, and credit and capital harder to come by, bankruptcy of large investment businesses are a real danger to social stability, as they often involve large amount of investments by both citizens, state banks, and local governments. More interventionist regulation in the cases of large businesses, and the politically controlled dismantling of struggling business groups at risk of collapsing will become common. Closer oversight, limited equity takeover by state-owned entities, or even managerial integration of party-state agents is already happening and these are tools likely to be employed more frequently.

Poorer local governments are at risk of bankruptcy due to indebtedness as a result of rising public service expenditure, and shrinking revenue streams and fiscal allocations from the central government. Some Provinces such as Guizhou have a debt to fiscal resource ratio approaching 200%, often due to poorly regulated over investment. The limited information that the central authorities receive on local finance is becoming a pressing concern for Beijing. Fiscal tightening has already led to repeated calls by the central government to cut spending, even including scaling back salaries and benefits of public servants. Given the leadership's call for higher quality development especially in poorer regions, more state-guided investments by public and private entities form wealthier regions could be a development model for the future. There is precedent in the "Go West Strategy," and the "North-east Revitalization Plan" which aimed at steering investments into poorer regions.

> To what extent is economic policy formulation being relocated away from the state bureaucracy and toward Party organs? How have regulatory agencies' ability to interpret and modify Party directives on China's economy changed under Xi Jinping's leadership?

We observe strong attempts to strengthen party integration in all organizations, and a more dominant role of party groups, ideology, and leadership in the decision-making process throughout society. While a "separation of party and state" was advocated by Deng Xiaoping and other leaders during the 1980s, Xi Jinping now drives the institutionalization of party cells and party secretaries, particularly in leading positions of the state apparatus. The CCP is not "taking over" the state apparatus but is becoming organically integrated with it. With party cadres acting as ranking officer in all public organizations, the party apparatus is supposed to exercise leadership on all strategic decisions and guide policymaking towards its political objectives. The state bureaucracy handles the concrete implementation of policy and public service functions.

At the top, with at least 10 central commissions chaired by Xi himself, most policy issues are now directly dealt with by him and his allies. This serves both better coordination, but also enables more influence on policy formulation. It also enables the Xi administration to steer top-level policy, which is supposed to serve as blueprints for specific interpretation by lower-ranking units in charge of implementation. China has a history of policy silos and at times conflicting policymaking across ministries and localities, and this centralization of policymaking is an attempt to counter the fragmented system. Nevertheless, provincial leaders have significant authority in the implementation of central policy. Provincial party secretaries and governors hold ministry-level rank, and provincial leaders have seats in the Politburo. As a contrast, no ministers are among its 25 members. In the past, central guidance was shirked or ignored, in areas like energy development, environmental protection, and investments in infrastructure. The increased discipline inspection and audit teams sent to localities under Xi Jinping seem to be an attempt at reigning in on this issue. It also illustrates the weakness of regular oversight mechanisms and bottom-up information flows.

> What does the Central Organization Department emphasize when making appointments to state-owned enterprise (SOE) leadership and government agencies? How has its decision-making on appointments evolved under Xi's leadership?

Cadre KPIs and SOE leadership selection at the central level are somewhat of a black box to outsiders. At the top, loyalty to Xi has become a decisive factor, although not the only criteria. Several high-ranking officials are known for their skills as politicians and administrators, especially in finance and economics. In theory, a long list of KPIs exists for cadre selection and promotion, including evaluation by subordinates and seniors, performance, and ideological compatibility. It seems unlikely that central-level positions are not primarily decided by more informal rules, including performance, but also stressing network affiliation, connections, and pedigree with the top-leadership. Looking at the cohort of cadres promoted under Xi, it becomes evident that those with personal or professional ties to Xi, and/or have shown loyalty and positive engagement with his politics, are overrepresented. At the same time, while the intense anti-corruption campaign overall is in my opinion serious about fighting graft and abuse of power, it is also used to systematically remove opposition and alternative networks of power in the political system.

At local levels cadre evaluation is more complex, and likely more procedural. Recent research suggests that a small amount of non-negotiable KPIs exist, e.g., socio-economic stability, but a larger number of flexible criteria add to evaluations. Given China's heterogeneity, these can be shaped more flexibly, and range from advancing environmental protection and solving economic crises to propelling industrial development and public service innovations etc.

Research tracking SOE leaders' careers and their networks suggests that a mix of political connections, industry knowledge, and management skills are all important for promotion. All 96 SOEs owned by the central government (ca. 115,000 SOEs exist at local levels) are led by a party secretary and a general manager or CEO of vice-ministerial rank, a fact that underscores that SOE leaders are both business leaders and government officials. While the leadership is formally split by this party-CEO division, often the same person holds both titles. Moreover, the importance of the party secretary and the company's party group for deliberating on strategic decisions has been recently strengthened and codified, also for private companies. The 53 most important SOEs are directly under personnel management of the central organization department (COD), but it is unlikely that the remaining 43 central SOEs are not also closely following the COD's vetting process. SOE leaders mostly remain within their sectors, although some examples for lateral mobility exist, often between SOEs in the same industry. What's more, a limited number of business-to-government careers exist, particularly in strategic SOEs important to national security, economic development, and vital infrastructure e.g., in nuclear industry, defense, and aerospace where SOE leaders come from or are going into government posts, such as provincial leadership or ministry departments. Zhang Qingwei and Xu Dazhe are two examples, who have moved from leadership roles in China Aerospace Science and Technology Corporation to senior government posts in provincial leadership.

> The Commission is mandated to make policy recommendations to Congress based on its hearings and other research. What recommendations for legislative action would you make based on the topic of your testimony?

My recommendations revolve around two points: First, smart investment in knowledge and better understanding of China's actions and motivations at home and abroad, and second, investing in systems to support better coordinated and consistent policy that ensures domestic political resilience and socio-economic stability in a world marked by China's growing presence. While the times in which foreign actors could directly interfere in China's domestic policy is over, China is increasingly able to influence global issues and has a growing impact on other nations' economies. How a more Chinese shaped world would look, and how this will impact other nations' own political, social, and economic systems, requires more study based on sophisticated, in-depth study of beliefs, interests, and policies. Lack of in-depth knowledge and understanding of your counterpart, especially over- or under-estimation of capabilities of Chinese actors, leads to poor policy decisions. It is increasingly important to realistically understand how China's domestic developments indirectly impact global arenas, and what its current and developing capabilities and interests for shaping markets and international relations also more directly are.

There is a need to invest systematically in more knowledge and understanding of China. Two factors, in my mind, require a step-up in both China-focused education and research. First, China's growing weight in global economic and political issues. China's growing presence is a reality the world needs to adapt to and knowledge is key for this. Second, China is increasingly inward-looking in terms of its political system and its economic objectives. The dual-circulation strategy is a prime example, in putting forth a view of the world's economy as a supportive system for China's domestic development. Not least the Covid-19 pandemic and the sudden end to travel and personal exchanges has exacerbated this trend and led to narrowing access to data and information open to outsiders. This needs to be countered by smarter and "patient" research able to develop alternative information sources and research methods.

It becomes more important to generate applied social science in service of better coordinated and fact-based decision-making. Better mechanisms need to be established to link knowledge communities in universities, think tanks, and research organizations with decision makers in government and business. Smart and "patient" research needs to feed into research and intelligence systems that can be used and digested more easily by policymakers. Recognizing my personal bias here, I believe there is a strong case for think tanks as a middle road between the more theory driven "patient" research done by academia and scattered but valuable information from practitioners in business, able to cater to the more issue-specific and solution-focused reporting needed by policymakers. Benefits of establishing more systematic and well-organized collaboration between universities, think tanks, and decision-makers are the room this creates for less specialized formats that apply more result-oriented reasoning but follow data-driven and theoretically sound methods.

More fundamentally, a clear-minded and honest analysis of how to balance principles and pragmatism is needed, given the growing political-economic gravity of China that entails both legitimate claims and challenges to the architecture of existing power and value systems. China's current leadership is better characterized as a player pursuing political pragmatism for long-term national interests of a political and economic nature, while most Western nations have long pursued economic pragmatism to secure short to mid-term economic interests. Well-coordinated all-of-government policy is therefore more important than ever, especially in large systems such as the United States – the same is true for the EU – as the cost-benefit calculation for short-term economic gains and long-term strategic risks is changing.