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Subcommittee on East Asia, the Pacific, and International Cybersecurity Policy
On The China Challenge, Part I: Economic Coercion as Statecraft

Economic Coercion as a Tool in China's Grand Strategy

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Mr. Chairman and Mr. Ranking Member:

Thank you for the opportunity to testify before you today.

We are slowly waking up to a set of strategies by the Chinese Communist Party (CCP) meant to enhance Party power internally and globally at our expense. The CCP has adopted a number of strategies to strengthen the Party's grip on the country so that it can lead China back to "Middle Kingdom Centrality." These strategies have been in place for a while, but have been accelerated by Communist Party Secretary General Xi Jinping.

The broad strategic context for Chinese economic statecraft includes:

- China's Grand Strategy of the China Dream of Grand Rejuvenation, which requires:
 - Building a world class military to challenge the United States and Allied military primacy;
 - Strengthening political warfare and propaganda campaigns that interfere in target nations' politics to both block activities that the CCP does not like and to build more favorable support for China abroad.
 - Advancing unlawful claims in the South China Sea and militarizing the seas to gain control of them.
 - Challenging Japan's lawful claims in the East China Sea
 - Building ports and facilities throughout the Indian Ocean
 - Attempting to make certain countries dependent on China's loans and construction projects as part of the "One Belt One Road" initiative

I am not including more benign diplomatic initiatives that are also a tool in the CCP's broader strategy. And, as you can see, when I say "China's policies", I mean those of the Chinese Communist Party. We do not know what "China's policies" would be in a more pluralistic society that is not completely dominated by a Leninist regime. I imagine we would get along very well with a China that is not under the CCP's grip.

Economic Coercion as a tool of the China Dream

Here is some more context. The era of reform and opening is over. Now, state banks, state-owned enterprises (SOEs), and their associated links with Party officials are what drive the Chinese economy. The CCP is willing to accept slowing economic growth in exchange for a tighter grip on the Chinese economy.

Thus, China's economic coercion cannot be thought of as absent the needs of the CCP's grip on China, or its strategies for growth and influence -- which as we now know include massive technology theft, the blocking of market access in key sectors, the control of capital flight, efforts to make exports cheaper (through subsidies and consumer repression), and other related measures.

The CCP has extensively targeted the United States and its key allies in the region with this economic coercion. Let's go through the CCP's tactics in each of these countries:

1. *The United States*

The CCP's unfair and illegal economic practices, such as mass subsidization of SOEs, gives China an unfair competitive advantage. This, coupled with the widespread theft of US intellectual property (IP), hurts the US economy. We are slowly challenging them on these fronts, and while these practices are the most harmful, they can be separated analytically from direct economic coercion. Instead, direct coercion includes:

- *Forced technology transfers.* As US Ambassador Dennis Shea highlighted at the World Trade Organization (WTO) in June 2018, China's "forced technology transfers" remain an implicit requirement for overseas companies hoping to access China's domestic market, especially through partnerships with SOEs.
- *Pressuring US business executives.* That same month, Xi Jinping also spoke with a number of top American business executives at the Global CEO Council in Beijing in an attempt to pressure U.S. executives to convince the U.S. government to ease trade tensions. A major form of coercion against the US has been the attempts to force US businessmen to lobby the US government to adopt more favorable policies from China's perspective. This practice has been ongoing for decades. The CCP will split Americans into "friends of China" who might lobby on their behalf and others who refuse to do so will not be granted access to China's massive market.

2. *Taiwan*

Taiwan stands as "ground zero" for China's coercive economic activities.

- There is a longstanding practice by China of pressuring Taiwanese business people to vote for Taiwan political parties that are perceived to be more pro-China or else lose market access or face economic harassment, and to pressure the Taiwanese government to accept terms that are unacceptable to the vast majority of the Taiwanese people.
- As we have seen recently, the CCP is also pressuring international companies to not identify Taiwan by name in an attempt to erase Taiwan as a separate entity from the global "mental map." Examples of these include the incited apologies from Marriot and Delta for including "Taiwan" on the list of countries in which they operate.
- Chinese People's Liberation Army (PLA) military exercises in Taiwan's surrounding waters are meant to remind the people of Taiwan that the CCP can cut Taiwan off from international trade altogether.

- China consistently targets and lures away top Taiwanese talent from its information and communications technologies (ICT) industries in an attempt to hollow out and dominate these industries.

3. *Japan*

The CCP has used its military might and the blocking of exports and imports to pressure Japan on political disputes.

- China's combined military-economic coercive tools caught the world's attention in 2010, when a Chinese ship collided with two Japanese coast guard vessels during a standard fishing trip near the disputed Senkaku islands. The Japanese coast guard arrested the Chinese fishing trawler, which led to combative rhetoric on both sides and China halting rare earth mineral exports to Japan. At the time, China produced 93% of the world's rare earth minerals, and essentially had a monopoly on these materials. By halting these exports to Japan, Japanese products such as hybrid cars, wind turbines, and guided missiles were under threat.
- The CCP also incites the Chinese public into action after controversial events that paint China in a bad light. Given China's anti-Japanese sentiment that can be traced back throughout history, the Chinese population has served as an effective proxy that the CCP uses to indirectly pressure the Japanese government into making concessions.
 - For example, in 2012 as tensions between China and Japan became heated over the disputed islands, Japanese firms in China such as Toyota and Honda had to shut down their facilities after demonstrations and violent protests against Japanese businesses broke out across China. Such demonstrations reveal broader Chinese government attempts to "hold foreign businesses hostage to its political agenda."

4. *Philippines*

The CCP has done the same thing towards the Philippines, demonstrating a pattern in squeezing neighboring countries to achieve aims favorable to Chinese interests across the region.

- After the Philippines began challenging Chinese claims in the South China Sea in 2012, China restricted banana imports from the Philippines and abruptly cancelled several Chinese tour groups that were going to the Philippines.
- After the Philippines brought a case against China to the Permanent Court of Arbitration challenging China's expanding territorial claims in the South China Sea, China continued to squeeze the Philippines economically by tightening controls on Philippine fruit and continuing to cut the number of Chinese tourist visits to the Philippines. As the third-

biggest export market for the Philippines and the fourth in foreign tourists, such cuts have a severe impact on the Philippine economy. In response to this, the Philippines was forced to “intensify [its] efforts to diversify [its] trade with other countries.”

5. *South Korea*

The pressure on South Korea after the deployment of the Terminal High Altitude Area Defense (THAAD) anti-ballistic missile defense system reveals not only Beijing’s pressure tactics, but also some of the organizations involved and more specific practices used by the CCP.

- For example, when the CCP decided to limit tourists to South Korea after announcements of the deployment, the China National Tourism Administration became a key organization in implementing the CCP’s policies. Semi-private corporations such as Chinese airlines also limited the number of plane tickets sold or flights to and from the targeted country.
- When the CCP attempts to rally its citizens to boycott or protest foreign businesses, as it did against South Korean supermarket Lotte, Chinese state media will actively encourage it.
- As the CCP limits certain imports of foreign goods, the Chinese Customs agency will not approve shipments, while Chinese ports will wrap merchant ships up in new regulations delaying their shipment.
- Local governments and actors have also gotten involved in Chinese economic coercion efforts.
 - When the CCP targeted Korean supermarkets in China during a particularly strained period of Sino-ROK relations, it was up to the local governments to conduct “inspections” and shut down Lotte for “fire safety violations”. Or, “lone actors” in China conducted “patriotic hacks” against South Korean company databases to steal data from Samsung.

6. *Vietnam and the South China Sea*

Lastly, there is the troubling category of combined military-economic coercive tactics that China employs particularly against smaller countries in the region. For example, the CCP has used its military and economic might against Vietnam and other nations that have ongoing disputed claims to the South China Sea areas. China has engaged in operations such as:

- *Cutting the cables of oil exploration ships in the South China Sea.* In 2012, two Chinese fishing vessels cut cables of a Vietnamese vessel doing seismic oil exploration work in the South China Sea.

- *Announcing and enforcing unilateral fishing bans.* In May 2018, China unilaterally announced a fishing ban in the South China Sea for two months, directly affecting the livelihoods of Vietnamese, Bruneian, Malaysian, and Filipino fishermen.
- Or even *directly threatening countries with overt military pressure*, as was the case when China placed an oil rig in Vietnam's exclusive economic zone in May 2014 and surrounded it with an armada.

Fighting Back

Thus, China holds meaningful sway over most of the countries it targets and the scale of China's economy and resources is its biggest strength. Many countries – particularly smaller countries in Asia that China actively targets -- still hope for access to the China market or seek to receive investment from the PRC.

However, there are limitations to China's economic coercion, particularly with respect to the United States. For one thing, China's economy is more dependent on the US economy than vice versa. Moreover, "good money" is leaving China to be invested here or other Western safe havens. In fact, one of the biggest complaints by Chinese elites is that the Xi administration is making it harder for them to get their money out of China.

Since the US is not dependent on China for as much as we think, we should have plans for an economic coercion strategy of our own. Some of these measures would include:

- Limits on the children of party elite's student visas;
- Bans on market access in accord with European actors on the worst-offending SOEs (for example, those that consistently engage in forced technology transfers);
- Targeted information campaigns within China in Chinese that advertise the corrupt patronage networks that exist between the CCP and key SOEs;
- Global armadas that convoy fisherman and oil exploration vessels to areas they are lawfully allowed to conduct their economic activities;
- Enhancing economic ties including the quick signing of a Bilateral Investment Treaty and cyber-cooperation with Taiwan.

But our approach to CCP economic coercion needs to be more comprehensive. Besides some of the defensive actions we could take listed above, the United States should consider a more proactive trade agenda that targets the countries that will become increasingly important to the US in the future – Vietnam, Indonesia and the Philippines -- as well programs to help strengthen the rule of law in these countries so that they are not as susceptible to outright Chinese bribery.

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The greatest economic coercion strategy we can place on China is helping to build free-market trade agreements and free-market economies in Asia whose standards are so high that a statist CCP will not be able to join.

