



EDITED BY ALESSIA AMIGHINI AND AXEL BERKOFISKY

XI'S POLICY GAMBLES: THE BUMPY ROAD AHEAD

INTRODUCTION PAOLO MAGRI

ISPI

Xi's Policy Gambles: The Bumpy Road Ahead

Edited by Alessia Amighini and Axel Berkofsky

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Introduction

Two years after Xi Jinping completed his rise to power, China is undergoing a profound transformation that will shape the country's political and economic position and positioning over the coming years.

While philosophers like Montesquieu and Hegel used to point at China as the paradigm of Oriental despotism, presenting it as a never changing civilization, today's China is often described as a country experiencing permanent transformation. Indeed, China has yet to complete its own transition, which began with the Open Door Policy launched by Deng Xiaoping in 1979, and is still facing significant tensions between centrifugal and centripetal forces.

Xi Jinping is further contributing to such transformation by imposing his ideas and priorities in domestic politics, economy and foreign affairs in a very resolute manner. The President of the People's Republic of China has quickly become a prominent actor – also in the international arena – after shocking domestic politics with the strongest anti-graft campaign in decades and a deep reform plan which undoubtedly affects vested interests at the local level and within state-owned enterprises. He is doing so by pushing for power centralization and placing under his direct control most of the main political decisions, thus restricting political space for other Party leaders. Moreover, China's impressive economic track record is increasingly having an impact on Chinese neighbourhood policies and, more generally, on foreign policy. By taking China's rise as a matter of fact, Xi Jinping is attempting to carve out a role for China among major powers and has recently launched ambitious plans such as the

New Silk Road, while challenging the existing international institutions, for instance through the creation of the New Development Bank.

Whether Xi Jinping will succeed or fail in pursuing his “China Dream” will ultimately depend upon his ability to successfully manage the end of China’s double-digit economic growth of the last decades and to adapt to the so-called China’s economic “new normal”. This implies ensuring peoples’ livelihoods and safeguarding the Party’s legitimacy by improving its governance performance at any level, while at the same time identifying a Chinese ‘democratic’ way to give voice to people’s dissatisfaction over the ongoing economic changes and tone down foreign opposition to China’s new international role. To this aim, Xi Jinping also has to solve specific socio-economic problems brought about by overcapacity, potentially negative effects of declining investments, rising public and private debt, demographic challenges – such as the aging population – and regional inequalities.

In a nutshell, Xi Jinping’s term will be key to find out whether – and to what extent – China is going to further scale-up its position in the international arena or is just a developing country stuck in the middle of a decades-long transition. This report covers all the above-mentioned major economic and political changes China is going through, both at the domestic and international level.

Filippo Fasulo highlights the evolution of China’s domestic politics in Chapter 1, analyzing Xi’s rise to power, his policy priorities and the main challenges he and his country will be confronted with over the coming years. In this regard, a key factor is how Xi will choose to deal with Party factionalism. The CCP Secretary General was selected with a view to finding a compromise among diverging political requests and ambitions in the complex inner-Chinese power structures. However, once in power, he targeted local power groups through economic reforms and unprecedented anti-graft campaigns. Xi Jinping immediately marked his mandate by presenting the so-called “China Dream”, a

slogan calling for a national effort to regain China its long-lost international role. His policy decisions in the economic field, coupled with the growing implementation of the rule of law, will inevitably affect local power groups, but consequences over Party stability are anything but clear yet. The President will have to face opposition within his own party in the eve of the 19th Party Congress in 2017, which will probably select the person that will take up his role in 2022. Moreover, Xi will have to adapt the Chinese political system to a changing social and economic environment, and ultimately respond to inner-Chinese calls and requests for more political participation. The evolution of the so-called ‘consultative democracy’ system might suggest how the Chinese Communist Party could transform domestic political structures without having to give up governing power.

Whether China has found its own development model and whether it will succeed in modernizing its economy is covered by Zhao Suisheng in Chapter 2. Xi Jinping decided to promote his “China Dream” policy already at the beginning of his mandate, while his predecessors Hu Jintao and Wen Jiabao chose to avoid speaking of a specific China model. Historically, China’s political and economic patterns developed around a strong state that based its legitimacy on defending national independence and launching modernization programs. According to Zhao, the Chinese model originated from three unique initial conditions, which do not make it easily replicable in other developing countries: country size, labor force availability and a peculiar institutional system. Indeed, these elements cannot be found anywhere else.

To be successful, the Chinese model should also help the country solve domestic challenges, such as reforming its decision-making process, tackle corruption and curb inequality. Above all, China has to recognize that the imperative of economic growth cannot trump everything else. In addition, if Xi plans to put China on a sustainable development path, he will have to solve structural and long-term issues of the country’s economy, Alessia Amighini argues in Chapter 3. As the “New Normal” growth puts the economy on a more sustainable path after three decades of

accelerated growth targets and aims to avoid China's heading for a 'hard landing', Prime Minister Li Keqiang said slower growth makes "structural reform all the more necessary". In a sense, shifting gears to a more appropriate growth rate will help China to achieve modernization of its economy. Li confirmed it is vital for China to go ahead with reforms of state-owned enterprises to improve efficiency and productivity and with liberalizing the banking system and financial markets. Although China's policymakers are currently tackling the short-term emergencies, over the longer run they are seeking to boost consumption to relieve overdependence on export markets and cut wasteful investment. Therefore, fiscal and market reforms – implemented in the 'Made in China 2025' strategy – are also particularly high on China's reform agenda.

Also foreign policy is marking a significant shift, as Gudrun Wacker points out in her contribution. If Deng Xiaoping called for 'keeping a low profile' in the conduct of foreign policy, this slogan has gradually been replaced by a more pro-active agenda. Four pillars shape China's new foreign policy predicament: relations with major powers, neighborhood policy, relations with developing countries, and multilateral diplomacy. In this regard, the relationship with the US is key for China. Xi Jinping proposed a new type of major power relationship between Beijing and Washington, but the US did not accept a pattern that could lead to establishing Chinese and American respective spheres of influence on a regional and global basis. Neighborhood policy is also increasingly more relevant in Chinese foreign policy, as China is trying to reshape the relations with its neighboring countries when talking about a 'greater neighborhood'. Moreover, China is increasingly proactive in its relationships with emerging and developing countries and in the multilateral arena, promoting 'host diplomacy' and new financial institutions which may ultimately challenge the existing Bretton Woods Institutions.

China and the EU, Axel Berkofsky writes in Chapter 5, define each other as 'strategic partners' since 2003, but many 'sectorial dialogues' are taking place without making substantive progresses.

China is reluctant to fully trust the EU because it fears European countries are backing US containment policies toward Beijing. China, Berkofsky suggests, is also exploiting Europe's lack of a coherent set of policies when dealing with Beijing. Since any EU member state will continue to adopt its own strategies toward Beijing, China will inevitably continue to regard Europe as a 'supporting actor' in international politics and security. Against this background, the EU's capability to influence Chinese security and foreign policy choices is very limited.

In this context, Wang Yiwei provides the reader with a Chinese point of view on EU-China relations, using the above-mentioned "New Silk Road" project as a case study. Wang argues that the Eurasian trade road stands for nothing less than the 'revival' of European civilization, which – according to Wang – is in decline. The strengthening of Eurasian trade and investment through the Silk Road will help stop such decline and move the geopolitical center of gravity away from the US and back to Europe and Eurasia. Today, Wang points out optimistically, Europe is faced with the historic opportunity to return to the center of the world, which is accompanied by the revival of Eurasia. As regards the benefits for Europe's relations with China, the Silk Road will be a second chance to discover China.

Finally, the report provides policy implications for the EU. If Europe really wants to prevent China from picking and selecting the preferred European country while ignoring others on a case by case basis, it has to strengthen its External Action Service (EEAS) and, more generally, its common foreign and security policies. It remains to be seen whether and to what extent today's Europe is willing and able to do so.

Paolo Magri, *ISPI Executive Vice President and Director*

1. Xi's Domestic Bet: Deng or Gorbachev?

Filippo Fasulo

In less than three years Xi Jinping grew from the rank of largely unknown Party functionary to one of the world's most powerful leaders. Such an outstanding political rise was possible thanks to Xi Jinping's commitment to defining his own political agenda and to a significant power-building initiative within the Party. Power centralization, the anti-graft campaign and the introduction into Chinese politics of new concepts like the 'China Dream' and the 'Four Comprehensives' gave Xi Jinping power comparable to that exercised by Mao Zedong or Deng Xiaoping. This transformation followed a succession process in which Xi was mainly seen as a pawn without charisma. Indicated as the man of compromise between two major factions, Xi Jinping ruled against Party factionalism. Now Xi has to conclude his power consolidation and to face inner opposition led by power groups affected by his reforms. His main challenges are to drive the Chinese Communist Party (CCP) out of economic slowdown and its traps and to disprove predictions of the People's Republic of China's (PRC) collapse.

1.1 The rise to power of Xi Jinping

Looking back at Xi Jinping's designation as the CCP Secretary General one can easily see how he was already preparing his rise at least in the previous five years. In fact, given the succession system of the CCP, it was already clear that he or Li Keqiang

would have become China's prominent leader in 2012. What was not that clear is that two and a half years later Xi Jinping is, almost on a daily basis, compared by scholars either to Deng Xiaoping or Mao Zedong. His rise to power indeed was seen as a fragile equilibrium between two leading factions, both of them connected to previous CCP Secretary Generals: Hu Jintao and Jiang Zemin.

China's prominent leader is the Party's Secretary General, who is elected every five years by the Congress within the Central Committee, and concurrently holds the position of President of the PRC and Chairman of the Central Military Commission (CMC). The Politburo is the leading core within the Party's Central Committee, and its inner seven-person Standing Committee encompasses the Party's most powerful cadre members. Standing Committee membership need to respect age limits (around 70 years) and this is the reason why Xi and Li were almost sure to be leading the country five years after the 2007 Party Congress: only they had the required age to be confirmed as Standing Committee members in 2012 during the 18th Party Congress. When Xi Jinping and Li Keqiang were appointed as members of the Politburo Standing Committee they were seen as representatives of two leading factions within the CCP: elitists and populists. Outstanding scholar Cheng Li sketched¹ their characteristics both in terms of membership and political visions. Elitists were supposed to have grown up as *taizidang* (princelings), that is, as sons of elder party cadres, and thus constituted a kind of red aristocracy. Thanks to their origins, their political careers were seen as highly facilitated. In fact, many of them started political activity as high cadres' political assistants (*mishu*) and later they were appointed directly to important levels of public administration. Moreover, *taizidang* usually spent their careers in coastal and richer provinces, where it was much easier to achieve outstanding economic results. Cheng Li described elitists also as keen on market economy, financial liberalization and international integration, thus allowing scholars to call them reformists. On the contrary,

¹ Cheng Li, "China's Team of Rivals", *Foreign Policy*, March/April 2009, <http://www.brookings.edu/research/articles/2009/02/03-china-li>.

populists can be defined as a group who came to power after long experience in the ranks as cadres in poorer provinces, usually located in inner China. Many of them started their careers within the Communist Youth League and their policies are much more pro-redistribution. The post-17th Congress scenario presented Xi Jinping as representing elitists and Li Keqiang as one of the populists. Li Keqiang came from the Youth Communist League, as Hu Jintao did, and spent his early career in poorer provinces, while Xi Jinping – the son of an outstanding politician who launched the first Special Economic Zones in Guangdong in the early 1980s – served as a high-ranking cadre in rich and coastal provinces such as Fujian, Zhejiang and Shanghai. Even if Xi held a higher position than Li, many at that time believed Xi would have been dismissed to make room for Li Keqiang². In fact, Li as populist was connected to then-Secretary General Hu Jintao, while Xi Jinping was close to 1990s Secretary General Jiang Zemin and his Shanghai clique. General interpretation was that Hu Jintao would have retained his power even after the 18th Congress in 2012 through his *protégé* Li³.

Indeed, succession in Chinese politics has always been a complex and not predictable matter. Chinese politicians described evolution among leadership as generations of collective leaderships. The First generation was led by politicians such as Mao Zedong and Zhou Enlai who governed China till 1976; Deng Xiaoping and the Party's Secretary Generals in the 80s, Hu Yaobang and Zhao Ziyang, are among those of the Second generation; Jiang Zemin and Zhu Rongji governed China in the 1990s and were the leaders of the Third generation; Hu Jintao and Wen Jiabao were at the head of the Fourth generation while Xi and Li are the core of the Fifth generation while the Sixth

² A. Miller, "The Preparation of Li Keqiang, *China Leadership Monitor*, Issue 31, Winter 2010, <http://media.hoover.org/sites/default/files/documents/CLM31AM.pdf>.

³ D. Shambaugh, "Don't expect reform from China's new leaders", *Washington Post*, 15 November 2012, http://www.washingtonpost.com/opinions/dont-expect-reform-from-chinas-new-leaders/2012/11/15/82cd4402-2f47-11e2-9f50-0308e1e75445_story.html.

generation is already gaining experience in the provinces. The shift from one generation to another has gradually become more and more institutionalized. From Mao to Deng the change was due to Mao's death and Deng's outstanding personal rise as paramount leader. Jiang and Hu, on the contrary, were both designated by Deng as successors in a newly institutionalized political environment.

The leadership change from the Fourth to today's ruling Fifth generation has been the first one in which neither Mao nor Deng were involved in any way. Succession is now clearly designed as a move from a 10-year long dualistic leadership (composed of the PRCs President and the Premier) to another dualistic leadership that is supposed to give up the helm after ten more years. However, predictions were that Xi Jinping would have been surpassed and dismissed by Li Keqiang, and once this did not happen that Hu Jintao would have kept part of his power at least for two more years⁴. Indeed, at the time of Jiang-Hu's generation change, Jiang Zemin maintained his position as Chairman of the Military Commission till 2005.

Contrary to scholars' expectations, Xi Jinping took over full control of the Party and the military from the beginning, while Hu Jintao immediately retired, downgrading his public appearances to a few visits, mainly within the borders of his home province, Anhui. In addition, Hu's *protégé* Li Keqiang, after a start in which he was given a great deal of attention, subsequently gradually left political centrality to Xi Jinping alone⁵. For example, in 2013 the Chinese media extensively dealt with so-called 'Likonomics' making a comparison between economic policies proposed by Li Keqiang and those implemented by other leaders in history. However, after little more than a year Likonomics has been almost forgotten and Li Keqiang is overshadowed by Xi Jinping. Furthermore the 18th Party Congress was still shocked by the Bo

⁴ W. Lam, "Xi will have limited power with Hu on the sidelines", *Deutsche Welle*, 25 October 2012, <http://dw.de/p/16UtS>.

⁵ On this regard, is important to highlight how Li Keqiang did not participate in drafting Third Plenum's reforms, a signal that might reveal Xi's power.

Xilai affair: the then-Party Chief in Chongqing, one of the most popular politicians in China and one of the possible members of the to-be-elected Politburo Standing Committee (PBSC) was at the center of a 'spy story' begun in spring 2012 that eventually ended with his expulsion from the Party and with his and his wife's conviction for, among other things, corruption and abuse of power. This case is considered the first step in the subsequent anti-graft campaign and led to a confrontation between radical leftists (close to Bo) and those accused of being rightists.

Xi Jinping thus kicked off his decade in a highly factionalized Party in which leadership selection could be seen as the outcome of balancing power groups. However, quite soon he gained a position as prominent leader, dismissing by facts the existence of dual leadership as it was in the so-called Jiang-Zhu and Hu-Wen era. Today's China is much more Xi's China rather than Xi-Li's. In addition Xi also questioned his linkage with Jiang Zemin's clique, because he did not support the main political initiatives promoted by Shanghai's Party members in the last few years. In fact, he did not show up at Shanghai's Pilot Free Trade Zone opening and when he visited it several months later he publicly made critical remarks about local leaders⁶. Moreover, his anti-graft campaign targeted many politicians close to Jiang.

In conclusion, Xi Jinping's rise to power was carefully prepared within the party at least five years before he became Secretary General in 2012. He was regarded as a piece of a power equilibrium based on a dualistic leadership composed of himself and Li Keqiang. However, he quickly gained full control of the Party and promoted his image so as to be labeled the new Deng or new Mao in less than two years. This outstanding political career was possible thanks to his profound impact on power centralization and to his war on power groups within local and central administrations. Xi Jinping is having a strong influence on Chinese politics by launching critical reforms of the decision-making system, and the anti-graft campaign, and placing emphasis

⁶ Xinhua, "Xi urges Shanghai stronger competitiveness", *ChinaDaily.com*, 24 May 2014, http://www.chinadaily.com.cn/china/2014-05/24/content_17538863.htm.

on ideology as well as on reshaping China's political image. However, great issues still remain unsolved, especially at the present time of China's new normality.

1.2 Xi Jinping is in charge

As soon as Xi Jinping became China's most powerful man, he presented a simple and catchy idea that has filled the Chinese media and covered the walls of Chinese towns till now: the Chinese Dream. This political campaign was informally presented in October 2012 during a visit of the newly established Politburo Standing Committee to China's National Museum in Beijing. The occasion was an exhibition titled "The Road to Renewal" dedicated to China's history since the first Opium War⁷. The exhibition's theme might help better understand the Chinese Dream, sometimes simply mistaken for an "American Dream with Chinese characteristics". The Chinese Dream, in fact, is related to a national collective effort to make China regain its outstanding position in the world after a long term of humiliation. The Chinese Dream is thus much more about patriotism than personal success and stresses collectivism over individualism⁸. With the Chinese Dream, Xi Jinping immediately characterized his term as a long-term promise of a better future. The collective Chinese Dream was intended as a tool to improve common peoples' livelihoods, setting goals to be achieved in the following decades. *The New York Times's* Robert Lawrence Kuhn reported⁹ that the Chinese Dream is seen as achieving specific goals named the "Two 100's" with reference to the double anniversary of the foundation of the

⁷ "Xi Pledges "great renewal of Chinese nation", *Xinhua*, 29 November 2012, http://news.xinhuanet.com/english/china/2012-11/29/c_132008231.htm.

⁸ Zhen Wang, "Not Rising, but Rejuvenating: the Chinese Dream", *The Diplomat*, 5 February 2013, <http://thediplomat.com/2013/02/chinese-dream-draft/?allpages=yes>.

⁹ R.L. Kuhn, "Xi Jinping's Chinese Dream", *International New York Times*, 4 June 2013, http://www.nytimes.com/2013/06/05/opinion/global/xi-jinpings-chinese-dream.html?pagewanted=all&_r=1.

Chinese Communist Party in 2021 and of the People's Republic of China in 2049. For 2021 China's aim is to become a "moderately well-off society" in which every citizen enjoys a higher standard of living, which in practice means doubling the approximately \$10000 of 2010 per capita GDP (Gross Domestic Product) by 2020 and completing urbanization by about 2030 with almost 1 billion people living in urban areas. The goal for 2049 is to make China a fully developed nation, completing the rejuvenation process with China finally restored to its role as world leader in science and technology, culture, economy and diplomacy.

Defining a long-term goal with such an impact was in line with both Chinese and communist traditions of setting long-term, utopian objectives and allowed Xi Jinping to immediately mark the start of a new era. Xi Jinping could thus focus on important reforms and political campaigns among which the anti-graft campaign holds a special position. Xi Jinping launched his war on corruption within the Party soon after the 18th Congress and as of spring 2015 more than 300,000 party cadres had been put under investigation with a 30 per cent increase in 2014 over 2013. In addition, Xi Jinping's anti-graft campaign not only targeted more Party members than previous years' campaigns, but it also has hit prominent members of the Party. As his slogan promises¹⁰, Xi Jinping throughout this campaign has excluded from political life dozens of high-level officials even at the provincial and ministerial level. There is no doubt that the biggest quarry for the Chinese Discipline Inspection Commission (CDIC) led by Xi's close ally Wang Qishan¹¹ has been Zhou Yongkang. The former security czar of China is the highest member of the CCP to be put on trial since the Gang of Four in the late 1970s. Zhou is accused of having created a strong personal power group, thanks to his career in the national oil sector and as Minister of Land and Resources

¹⁰ Xi Jinping targeted both high level cadres (Tigers) and small officials (Flies).

¹¹ For the relationship between Xi Jinping and Wang Qishan see Cheng Li, "Xi Jinping's Inner Circle (Part 2: Friends from Xi's Formative Years)", *China Leadership Monitor*, no. 44, Summer 2014, <http://www.hoover.org/sites/default/files/research/docs/clm44cl.pdf>.

that permitted him to divert money from the oil business; as Party Chief in Sichuan Province; and in security-related positions like Minister of Public Security and Secretary of the Central Political and Legal Affairs Commission of the CCP. Xi Jinping's action against corruption weakened political factions within the party and created a feeling of fear among party cadre members. Even though the anti-graft campaign has gradually expanded its hunting territory from Zhou's and Bo's circles to main sectors of Chinese business and political life such as the People's Liberation Army and, later, state-owned enterprises, Xi Jinping has not avoided the accusation of simply conducting a huge purge within the Party. Apparently such criticism has not affected the CCP Secretary General, who paralleled his crackdown on corruption with significant power centralization.

In November 2013, in fact, the Third Plenum of the CCP's Central Committee was held. This political event has traditionally been a reform cornerstone in China's past thirty year of politics. As the Chinese media extensively stated, Deng Xiaoping launched and re-launched economic reforms during Third Plenums in 1979 and 1993. Along with social and economic reforms, the establishment of a Central Leading Group on Comprehensively Deepening Reforms (Clgcdr) deserves great attention. This inter-departmental office is chaired by Xi Jinping himself and covers any issue to be reformed, from the credit system to Chinese Football Association. With this decision, Xi Jinping put himself at the center of the Chinese decision-making process, reducing the political space of his supposed-to-be-twin-leader Li Keqiang.

The evolution of Leading Small Groups (LSG) has shaped Chinese politics since the start of the reform period and their number has expanded and contracted according to different political circumstances. Those groups are informal coordination mechanisms to implement policies set up by the LSG leader and supervisor and can be permanent, term-oriented or task-oriented. They cover all the most important issues and during Hu-Wen's era a power decentralization process assigned a leading group to each

member of the Politburo Standing Committee¹². This led to the creation of several fragmented political areas, guided by different leaders who cultivated their own circles, affecting the reach of Party decisions so much that some used to say “policies stop at the gate of Zhongnanhai (Party headquarters)”¹³. In addition, LSG composition has always been surrounded by mystery and secrecy, while recently official media have even started to report on LSG regular meetings. This budding of LSG’s gradual institutionalization is connected to Xi’s decision to create the CIGcdr. Membership in the new Reform Commission is given, among others, to 4 out of 7 members of the PBSC (including Xi and Li Keqiang), 14 out of 25 members of the Politburo and outstanding figures from the CDIC, National People’s Congress (NPC), State Council (government), Chinese Political Consultative Conference (CPCC), army, Supreme Court and Supreme Procuratoriat. It covers the functions of designing, planning, coordinating and implementing reforms, especially at the national, long term, cross-sectorial and cross-regional levels. In addition, the CIGcdr supervises six sub-groups dealing with issues like economics, the legal system and inspections that were previously dealt with by *ad hoc* LSG. With this decision Xi Jinping thus ensured himself an institutional instrument that can help him to bypass power group interests, fighting against excessive fragmentation and pushing toward power centralization.

By the same token, fall 2014’s Fourth Plenum was the stage for significant stress on the rule of law. However, legal reform is not intended as a step towards legal and bottom-up control over politics. On the contrary, it is aimed at limiting the power of local authorities in judicial cases and weakening local authorities’ resistance to economic reforms directed against vested interests. On the one hand this reform will be useful to ensure the rights of

¹² A. Miller, “More Already on the Central Committee’s Leading Small Groups”, *China Leadership Monitor*, no. 44, Summer 2014, <http://www.hoover.org/sites/default/files/research/docs/clm44am.pdf>.

¹³ L.L.P. Gore, *China’s Leading Group for Comprehensively Deepening Reforms*, EAI Background Brief no. 908, 10 April 2014.

market players and, on the other, this is once again an attempt to reduce power decentralization¹⁴. Recalling an old Mao metaphor, rule-of-law reform has been described by Xi Jinping himself as a knife in the Party's hand¹⁵ and high-level cadre members have put much effort into explaining how China's legal system differs from the Western systems. In this case the adopted metaphor is "to wear shoes that fit"¹⁶, a topic strictly related to the debate about Chinese constitutionalism. Indeed, in the last two years constitutionalism has gained much space on the political stage. First of all, some op-eds calling for Western-style constitutionalism did not pass censorship checks and in the following months many Chinese scholars presented their views on whether to implement a constitution or not¹⁷. Finally, Xi Jinping gave importance to the Chinese Constitution while celebrating its 32nd anniversary. This apparent contradiction can be better understood by looking at the opposing significances of 'constitutionalism' and 'constitution'¹⁸, in which the former is intended as a liberal tool to limit the state and thus the Party, while the latter refers to China's basic law in which it is clearly stated that the Party leads the country. The problem at stake, then, is whether the law should be higher than the Party or not. Xi Jinping's current solution is that the Party is still unquestionable because it represents the Chinese people and

¹⁴ C. Minzner, "After the Fourth Plenum: What Direction for Law in China?", *China Brief*, vol.14, no. 22, 20 November 2014, http://www.jamestown.org/uploads/media/China_Brief_Vol_14_Issue_22_3_01.pdf; Z. Keck, "4th Plenum: Rule of Law with Chinese Characteristics", *The Diplomat*, 20 October 2014, <http://thediplomat.com/2014/10/4th-plenum-rule-of-law-with-chinese-characteristics/>.

¹⁵ R. Lu, "China's President Raises Eyebrows with Sharp Rhetoric on Rule of Law", *Foreign Policy*, 3 February 2015, <https://foreignpolicy.com/2015/02/03/chinas-president-raises-eyebrows-with-sharp-rhetoric-on-rule-of-law/>.

¹⁶ D. Bandurski, "The shoe that fits: China's 'rule of law'", *China Media Project*, 3 February 2015, <http://cmp.hku.hk/2015/02/03/38075/>.

¹⁷ R. Creemers, "China's Constitutionalism Debate: Content, Context and Implications", *The China Journal*, Forthcoming, available at SSRN: <http://ssrn.com/abstract=2511526>.

¹⁸ D.S. Rajan, *China: Xi Jinping's Ideological Dilemma*, South Asia Analysis Group (SAAG), Paper no. 5842, 16 December 2014, <http://www.southasiaanalysis.org/node/1677>.

acts in their interests, while the constitution and rule of law should be implemented at local levels to limit local power holders' interference. In conclusion, Chinese rule of law and reference to the constitution should be viewed as tools to regulate lower-level political excesses and to confirm the CCP's political guidance of the PRC.

In order to implement such a radical agenda, which is aimed at eradicating power groups within the party, Xi Jinping had to look for consensus both within the Party and among the Chinese population. If the first step on this path has been the launch of China Dream, the second move consists of strengthening ideology. Xi Jinping put much emphasis on defending Mao's legacy as legitimising the Party's rule. During New Year's celebrations in February 2015, he made a heavily publicised trip to Yan'an, Communist headquarters from the late 1930s till the foundation of the People's Republic of China in 1949. By recalling the Yan'an experience, Xi intended to recall the origin of the Chinese Communist Party and strengthening ideological links with Mao. In addition, he launched a campaign against 'Western values' in Chinese universities and raised the level of media control. Those decisions might be seen as a way to control the Party in a sensitive period for reforms. Some observers are also suggesting that lifting restrictions on freedom of speech is an attempt to hide dissatisfaction with Xi's political and economic agenda.

More recently (December 2014), Xi Jinping presented a new political theory called the 'Four Comprehensives'. Local commentators have praised this formulation, which is linked to the Chinese political tradition of selecting a few bullet points to focus on, as a step forward in Marxism. The four elements are "comprehensively building a moderately prosperous society, comprehensively deepening reform, comprehensively advancing the rule of law, and comprehensively strictly governing the Communist Party of China (CPC)". The four parts recall the main political campaigns promoted by Xi since taking power. Achieving a wealthier society is one of the main goals of the China Dream, while the others can be referred to emphasis on reform, rule of law and the

anti-graft campaign. It is worthwhile underlining that no evolution of the Party's role is presented. In the Party's view this is a practical ideology to reach the China Dream's goal and many commentators in the Chinese media largely referred to this new ideological strategy as a tool aimed at finally achieving a two hundred years old objective (reference here is to the era that preceded the First Opium War), that is, rejuvenation of the Chinese nation as described by the China Dream. The Four Comprehensives will therefore probably be the formulation through which Xi Jinping's ideological contribution will be registered within the Chinese Constitution and the Party's Constitution, as occurred in the past with each generation's 'achievements': the theory of Deng Xiaoping, Jiang Zemin's Three Represents and Hu Jintao's Harmonious Society and Scientific Development.

To sum up, Xi Jinping has heavily influenced Chinese politics in the last two years, but he will be in charge of China's highest power probably until 2022 and the Four Comprehensives will have to show their effectiveness in tackling China's main political challenges.

1.3 What's now on Xi's political agenda?

The elephant in the room in every discussion about China is whether the country with the world's biggest population will ever adopt a Western liberal democratic election system. Major China observers¹⁹ now tend to agree that it won't happen, but probably this is not enough to dismiss any possible evolution of China's political institutions and decision-making process. In the coming years, Xi Jinping will have to face two main issues: controlling competition among the Party's inner factions and adapting the CCP to rising political challenges.

¹⁹ K. Lieberthal, Cheng Li, *Preface* in K. Lieberthal, Cheng Li, Yu Keping (eds.), *China's Political Development*, Washington D.C., Brookings Institution Press, 2014.

If we assume that the succession path that let Xi Jinping become China's prominent leader in 2012 is now sufficiently institutionalized, spring of 2015 is already time to prepare room for Xi's heir. Indeed, Xi was elected as member of the Politburo Standing Committee during the 17th Party Congress in 2007 and one might take for granted that such a decision was taken at least few months earlier. To give an accounting of succession timing, it is interesting to note how Hu Jintao is said to have been chosen as China's new leader by Deng Xiaoping, even though Hu became Secretary General in fall 2002 while the Second Generation's paramount leader had passed away in 1997. In the light of this process, the 19th Party Congress to be held in 2017 appears incredibly close. Selecting the future leader of the Sixth Generation already during the 19th Party Congress will allow him to get government experience and reach 2022 ready to lead China. However, Xi Jinping appears much stronger than Jiang Zemin and Hu Jintao and might opt not to choose his heir so early. This decision would be an important move as well, since its meaning would be that the succession path is not yet fully institutionalized and that the Chinese political system is still at a transitional stage.

However, the Sixth Generation will probably debut at the Politburo Standing Committee during the 19th Party Congress even if the next leader has still to be selected. Experts have started to individuate those that can succeed in the race. Hu Chunhua and Sun Zhengcai are among the most prominent leaders of the Sixth Generation. They hold, respectively, the position of Party Chief in Guangdong and Chongqing, resembling once again the competition between Wang Yang's Happy Guangdong and Bo Xilai's Chongqing Model that went on right before Bo's disgrace. Xi Jinping's political campaigns have heavily affected Chinese political factions, and the 19th Party Congress will represent a first reckoning of winners and losers. From the composition of the next Politburo Standing Committee it will be possible to forecast whether Xi Jinping's reformist approach is finding support or opposition within the CCP. The Chinese President will have to be very careful in dealing with those issues in order to avoid a strong

conflict among Party cadre members that might slow down the decision-making process.

Nevertheless, Xi Jinping has already proven that he has a long-term vision and that his political horizon cannot be limited to the Party's inner disputes. For this reason he will have to take a stand in the debate over reforming the Chinese political system. Any change in China will surely be gradual and subjected to several vetoes and turnabouts, but the PRC demonstrated in the past its ability to transform itself when needed. The CCP's big issue is to complete its transformation from a revolutionary to a ruling party. After the historical breakthrough represented by the launch of reform and the Open Door Policy, many have suggested the exigency to adopt not only the market system but also Western liberal democratic elections. Reforming Chinese political institutions has been delayed for thirty years, leaving aside the gradual institutionalization process. Greater pressure on Xi Jinping might come from the '70-year itch' and from the outcomes of a slowing economy. Larry Diamond depicted as the '70-year itch'²⁰ an authoritarian government's tendency to collapse after 70 years in power, as happened in the USSR or Mexico. Those leadership changes were mainly due to lack of efficiency, a warning that should force China to restructure its political system. The second warning comes from the recognition of economic new normality and even the fear that China's economic boom is over²¹. In March 2015 China scholar David Shambaugh made a really provocative accounting of the state of the Party's health, stating that "the endgame of communist rule in China has begun" because of wealthy Chinese citizens' scarce confidence in their own country, the Party's insecurity as shown by ideological campaigns, lack of ideological strength, corruption and inner party fights caused by

²⁰ L. Diamond, "Chinese Communism and the 70-Year Itch", *The Atlantic*, 29 October 2013, <http://www.theatlantic.com/china/archive/2013/10/chinese-communism-and-the-70-year-itch/280960/>.

²¹ S. Babones, "China's Predictable Slowdown", *Foreign Affairs*, 18 February 2015, <http://www.foreignaffairs.com/articles/143108/salvatore-babones/chinas-predictable-slowdown>.

Xi's purges hidden by anti-graft campaigns²². According to the paradigm that Party legitimacy derives from ruling performance, worsening economic conditions might lead to rising social instability that could deadly wound the CCP. Crackdowns on corruption and ideological radicalization have been read as a way to prevent those kinds of problems²³. Xi Jinping's *sine qua non* is to manage possible social uprisings, to keep Party consensus and to improve government's efficiency. To achieve those goals, he will have to 'Go outside Zhongnanhai' and to make some room for government-people confrontation, something that within liberal democracies happens through elections. However, the CCP does not at all intend to give up its vanguard position, nor to open leadership and policies selection to procedural democracy's processes. What China did in past decades was to find apparently contradicting solutions to its main issues on the agenda. "Market socialism with Chinese characteristics" or "One country, two systems" are just the main examples of this practice. Today's problem is how to reform governance maintaining the Party's direction but allowing more extra-party participation. Looking at the current Chinese political system we might spot some ready solutions within the Chinese Political Consultative Conference (CPPC), an advisory assembly composed of members of eight political parties that traces its history back to the late 1940s, prior to establishment of the PRC. The CPPC is the main manifestation of the so-called 'consultative democracy', which is the CCP's and China's 'own brand of democracy' as the national press agency Xinhua stated²⁴. According to official definitions, consultative democracy is "a democratic pattern in which, led by the CPC, all sections of society are consulted on major issues before and during policy-making processes".

²² D. Shambaugh, "The Coming Chinese Crackup", *Wall Street Journal*, 6 March 2015, <http://www.wsj.com/articles/the-coming-chinese-crack-up-1425659198>.

²³ M. Auslin, "The Twilight of China's Communist Party", *Wall Street Journal*, 25 January 2015, <http://www.wsj.com/articles/michael-auslin-the-twilight-of-chinas-communist-party-1422551788>.

²⁴ "CPC proposes developing 'consultative democracy'", *Xinhua*, 9 February 2015, http://news.xinhuanet.com/english/china/2015-02/09/c_127476509.htm.

The CIGCDR proposed during its sixth meeting held in late December (as of March 2015 more details were not available) to improve a consultative pattern that builds “a more favorable environment for consultations and takes a more open-minded and modest attitude in listening to non-CPC parties’ advice and suggestions on major state issues”. This has been the third signal in a few months about consultative democracy, after Xi’s speech at the CPPC anniversary in October and after a meeting with eight democratic parties’ leaders to celebrate the Chinese New Year. Thus, it seems that there are some timid moves towards gradual implementation of a Chinese form of democracy, a system that never questions the CCP’s legitimacy, but might enlarge the Party’s link with the people and can improve a kind of ‘feedback-chain’ about Party policies. The goal Chinese leadership has to achieve is government efficiency, especially in a time of economic slowdown and decreasing business opportunities. Village elections – experienced to different degrees since the 1980s – and attempts to affirm intra-party democracy and state-party separation are all elements that might be part of Xi Jinping’s political reform, whenever he will launch it.

Conclusions

Is Xi Jinping really following the path of Mao Zedong and Deng Xiaoping or will Mr. China Dream be the PRC’s Gorbachev? Today Xi Jinping holds more power than the previous two Party Secretary Generals, Hu Jintao and Jiang Zemin, but his political agenda might be only at the beginning. Chosen as the CCP’s leader in a highly factionalized environment, Xi Jinping has been able to tackle strong power holders within the party by promoting a war on corruption and on local power groups. The PRC’s president has taken significant action against power decentralization, establishing a new oversight commission dedicated to reforms. He has also adopted the rule of law to limit interference by local authorities without affecting the Party’s supremacy in guiding the government. Xi Jinping now has to face inner Party

opposition to his actions and has to find a way to adapt Chinese political institutions to contemporary issues and to stronger than ever predictions of the PRC's imminent collapse. In Xi's view, since Western solutions are unfit for China "the concept of consultative democracy" might lead to gradual political evolution. This instrument has the potential to be Xi's political contribution to the modernization of Chinese politics, while rejecting Western political ideals. This gamble might allow the CCP to retain its performance-based legitimacy and to avoid the collapse experienced by other communist regimes.

2. The Chinese Recipe: A Unique Model for Modernisation?

Suisheng Zhao

While top Chinese leaders such as President Hu Jintao and Premier Wen Jiabao were reluctant to publicly endorse the China model amid the hot debate about whether China has created a new model of state capitalism for itself and potentially for other emerging economies as an alternative to the model of liberal capitalism, President Xi Jinping has not hesitated to include the China model as part of his “China Dream” and is determined to pursue a unique path for China’s modernization. Has President Xi has found a unique path of modernization for China?

2.1 “Only the wearer knows if the shoe fits his foot”

The China model debate started after an American journalist, Joshua Cooper Ramo, in 2004 proposed the Beijing Consensus of state-led economic growth in contrast to the Washington Consensus based upon neo-classic liberal traditions. While Ramo’s provocative argument was fresh at the time, some scholars quickly pointed out the clear flaws in the concept. Scott Kennedy described the Beijing Consensus as a myth because China did not follow any of its tenets¹. Chinese scholars joined the debate quickly and enthusiastically. The advocates of the China model were mostly nationalistic new-left intellectuals who were

¹ S. Kennedy, “The Myth of the Beijing Consensus”, *Journal of Contemporary China*, vol. 19, no. 65, 2010.

convinced that the China model worked better for China than the Western model of modernization, particularly after the Western world fell into the financial crisis in 2008. The China model debate cooled down for a while because the top officials in the Hu Jintao-Wen Jiabao administration were careful to avoid endorsing the concept, reflecting their hesitancy to engage in ideological debates as well as their efforts to dispel the perception of China as a threat during the period of China's rapid economic growth². Only two politburo standing committee members in charge of ideology and propaganda, Li Changchun and Liu Yunshan, mentioned the China model, while neither President Hu Jintao nor Premier Wen Jiabao ever used the term in formal remarks. Responding to criticism of China's promoting its model to developing countries, Premier Wen Jiabao at the Forum on China-Africa Cooperation (Focac) IV in 2009 said that neither the 'Washington Consensus' nor the 'Beijing Model' offered prescriptions for Africa's development, which should be based on its own conditions and follow its own path, that is, the African Model. All countries had to learn from other countries' experience in development. At the same time, they had to follow a path suited to their own national conditions and based on the realities of their own countries³.

As noted in Chapter 1, the China model debate, however, resurged after President Xi Jinping came to office and he has vigorously promoted the China model as a unique path of modernization in his campaign to realize the "China Dream" since being instated, reflecting his confidence in China's rising power position. Shortly after taking the position of Party General Secretary, Xi made a highly publicized visit to the National Museum's "Road to Revival" exhibition on 29 November 2012. Tracing modern Chinese history from the country's humiliating

² Jianmin Qi, "The Debate over 'Universal Values' in China", *Journal of Contemporary China*, vol. 20, no. 72, 2011.

³ "Full text of Wen's speech at 4th Ministerial Conference of FOCAC", *Xinhua*, 9 November 2009, http://www.china.org.cn/world/2009-11/09/content_18849890.htm.

defeat by Great Britain in the mid-19th Century, Xi called on the Chinese people to realize the “China Dream” as a great national revival.

Xi’s promotion of the China model starts with an emphasis on China Communist Party (CCP) leadership. In his inaugural speech after assuming the presidency at the National People’s Congress (NPC) on 17 March 2013, talking about the importance of finding a Chinese path toward China’s rejuvenation, he proposed ‘three confidences’: i.e., confidence in the theory of socialism with Chinese characteristics, in the road the country is now following, and in the current political system (坚定中国特色社会主义的理论自信，道路自信，制度自信). In his visit to Macao on 21 December 2014, he added cultural confidence (文化自信) as the fourth confidence and stated that cultural confidence is the foundation.

Xi justified the unique model of modernization for China in terms of China’s unique history, culture, and national conditions. In his first overseas visit as President in March 2013, Xi made the famous remark in Moscow that “Only the wearer knows if the shoe fits his foot. Only the people of a country know best whether or not the development path is appropriate for the country” (鞋子合不合脚，自己穿了才知道。一个国家的发展道路合不合适，只有这个国家的人民才最有发言权). Speaking to a European audience in April 2014, he said that “China’s unique cultural tradition, unique historical fate [destiny], and unique national conditions have determined that China must follow the road of development that fits Chinese characteristics”. Speaking at Peking University on 4 May 2014, Xi told the students that, nurtured by the Chinese culture that the Chinese nation has developed in its long struggle and supported by 1.3 billion Chinese people, “We will take our own path... While we should learn from all civilizations in human society, we cannot forget our ancestors and cannot copy the development models of foreign countries. Nor we can accept any instructions imposed by foreigners”. These statements made clear not only his determination to pursue a unique China model but also his justification that, because China

is completely unique among world nations, only a quintessentially Chinese model can accommodate China's unique 'national circumstances'. China, therefore, will have to follow its own path, not that of the West.

Encouraged by the leadership endorsement, Fudan University in Shanghai established a first China Development Model Research Center in December 2013. The founding director of the Center is Zhang Weiwei, a Chinese scholar trained in Europe and author of *The China Shock: the Rise of Civilizational Nation* (《中国震撼：一个文明型国家的崛起》), a book recommended by President Xi Jinping. Zhang explained that: "China is the only nation where a millennia-old civilization fully coincides with the morphology of a modern state... It is as though ancient Rome was never dissolved, and continued to the present day, making the transition to a modern nation-state, with a central government and a modern economy, incorporating traditional cultural elements, having a massive population in which everyone speaks Latin"⁴. According to Zhang, China's dramatic rise should be understood in the context of China as a civilizational state, an amalgam of the world's oldest continuous civilization and a huge modern state, a product of hundreds of states amalgamated into one over the past thousands of years of history. The civilizational state is characterized by four factors: a super-large population, a super-sized territory, a super-long history and a super-rich culture. The civilizational state shaped all the key features of China's development model, with all its possible ramifications for China's trajectory into the future and beyond⁵.

The Fudan Center for China Development Model Research has gathered some strong advocates of the China model. A senior fellow at the Center used 'the three bests' (China today is in the best time and best system and best developed country in the world

⁴ Zhang Weiwei, "一个奇迹的剖析：中国模式及其意义" (The Analysis of a Miracle: The China Model and its Significance), 红旗文稿, June 2011, http://www.qstheory.cn/hqwg/2011/201106/201103/t20110325_74156.htm.

⁵ Zhang Weiwei, "中国崛起与文明型国家的逻辑", 观察者网, 9 January 2014, http://www.guancha.cn/zhang-wei-wei/2014_01_09_195305_2.shtml.

since 1840) to back Xi's 'three confidences'. Advocating the China model, he argued that: "China has greeted the time of its confidence when the Western elites have lost their confidences"⁶. Eric X. Li, a venture capitalist and a senior fellow at the Center, has published numerous articles in mainstream English journals and newspapers to elaborate the success of the Chinese unique political and economic system. Soon after Xi Jinping became the Party General Secretary in November 2012, Li published an article in *Foreign Affairs* and declared that in the capital of the Middle Kingdom, the world might witness the birth of a post-democratic future because Beijing was able to meet the country's ills with dynamism and resilience, thanks to the CCP's adaptability, system of meritocracy, and legitimacy with the Chinese people. The country's leaders would consolidate the one-party model and, in the process, challenge the West's conventional wisdom about political development and the inevitable march toward electoral democracy⁷. In another article he found that "with a few exceptions, the vast majority of developing countries that have adopted electoral regimes and market capitalism remain mired in poverty and civil strife. In the developed world, political paralysis and economic stagnation reign. The hard fact is this: democracy is failing from Washington to Cairo". In contrast, China discovered its unique and successful path of modernization⁸. In a lecture in Seoul in early 2014, Li declared that "China's most notable accomplishment in the past three decades is, perhaps, its success in engaging, and in many cases mastering, the international economic system set up and maintained by the U.S.-led West

⁶ 宋, "只有去中国才能看到未来——中国正迎来自信时代", 《求是》, September 2013,

http://www.qstheory.cn/zxdk/2013/201309/201304/t20130426_226224.htm.

⁷ Eric X. Li, "The life of the party: the post-democratic future begins in China", *Foreign Affairs*, vol. 92, no. 1, 2013, [http://0-go.galegroup.com.bianca.penlib.du.edu/ps/i.do?action=interpret&id=GALE%7CA315371145&cv=2.1&u=udenver&i=r&p=AONE&sw=w&authCount=1](http://0-go.galegroup.com/bianca.penlib.du.edu/ps/i.do?action=interpret&id=GALE%7CA315371145&cv=2.1&u=udenver&i=r&p=AONE&sw=w&authCount=1).

⁸ Eric X. Li, "The West can avoid conflict by allowing China to go its own way", *South China Morning Post*, 23 November 2013, <http://www.scmp.com/comment/insight-opinion/article/1362907/west-can-avoid-conflict-allowing-china-go-its-own-way>.

without being absorbed by it". He further stated that: "China adopted a market economy, but not capitalism. It effectively negotiated its way into the World Trade Organization (WTO) on preferential terms by taking advantage of the West's illusion of the eventuality of a globalized economic order. In one generation's time, it has gone from a negligible player in the global economy to an 800-pound gorilla within it"⁹.

2.2 Overpowering the authoritarian state

For President Xi, the key for success in China's search for a unique model of modernization is the authoritarian state led by the Communist Party, reflecting the long struggle of the Chinese political elites to build and maintain a powerful state to lead China's modernization. Lucian Pye famously observed that China suffered a 'crisis of authority' in a deep craving for the decisive power of 'truly effective authority' ever since the collapse of the Chinese empire in the 19th Century. Chinese elites attribute China's modern decline partially to the weakening of state authority. The crumbling of state authority was in essence equated with China's humiliation. Therefore, "the basic problem in development for the Chinese has been that of achieving within their social and political life new forms of authority which can both satisfy their need to reassert a historic self-confidence and also provide the basis for reordering their society in modern terms"¹⁰.

The authority crisis called for the creation of an authoritarian state through revolution and nationalism. The Chinese communist revolution was a collective assertion of the new form of authority and a strong state to build a prosperous nation. The very essence of the CCP's legitimacy for the founding of the People's Republic

⁹ Eric X. Li, "The Middle Kingdom and the Coming World Disorder", *The World Post*, 4 February 2014, <http://feedly.com/k/1e3JeDm>.

¹⁰ L. Pye, *The Spirit of Chinese Politics: A Psychocultural Study of the Authority Crisis in Political Development*, Cambridge, MA, MIT Press, 1968, p. 55.

of China (PRC) was partly based upon its ability to establish a powerful state to defend national independence and launch modernization programs. This led to a concentrated effort to empower the authoritarian state as an organizing and mobilizing force to lead China's modernization.

As a result, the authoritarian state played a crucial, if not unique, role in shaping the path of China's modernization. The Communist Party used state power to control inflation, established a mixed economy to help the urban economy recover, carried out land reform to expand agricultural production in the early 1950s. The state's power was further strengthened after China adopted the Soviet Model of industrialization in the late 1950s.

Deng Xiaoping launched economic reforms to dismantle the Soviet-style command economy in the 1980s. The reforms not only reduced the state's administrative control over enterprises and continued decentralization of the state authority in economic decision-making but also gave opportunities to some intellectuals turning to Western liberal ideas and calling for Western-style democratic reform. The authoritarian rule of the CCP was challenged in several waves of popular protests, leading to the large-scale anti-government demonstrations on Tiananmen Square in the spring of 1989.

Although the demonstrations were suppressed by military force, how to restore the Chinese people's confidence in the government's ability to develop the economy became the most serious challenge to the post-Tiananmen leadership. As a result, neo-authoritarianism was advanced into mainstream thought with the new label of neo-conservatism. Before the Tiananmen crackdown, neo-authoritarianism was only a heatedly debated topic, advocated mainly by some personal aides to Zhao Ziyang, then the CCP general secretary, and by a few scholars such as Shanghai-based Xiao Gongqin and Wang Huning, who later became President Jiang Zeming's personal aide. It had been argued that the economic miracle of the four 'little dragons' in East Asia was created because they all espoused Confucian collectivism, family loyalty, and frugality, as well as a patriarchal

power structure¹¹. Neo-conservatism now argued that a centralized power structure must be strengthened in order to maintain social stability and economic development. Neo-conservatism emphasized political and economic stability and control while restoring moral values based on the conservative elements of Confucianism¹².

In the meantime, two Chinese scholars, Wang Shaoguang at Yale University and Hu Angang at the Chinese Academy of Science published *Report of China State Capacity*, in 1993, which made specific responses to the post-Tiananmen leadership's concern about the need to restore the central state's authority in economic policy-making¹³. They defined state capacity as the capacity of the state to transform its preferences and goals into reality, including fiscal extractive capacity, regulatory and control capacity, legitimation capacity, and coercive capacity. They argued that the state's capacity to exercise macro-economic control had declined because of the massive decline of the central government's fiscal revenue. Therefore, a massive enhancement of the state's capacity to balance economic reform was urgent. Their report focused on how to strengthen the state's extractive capacity by increasing the so-called 'two ratios', i.e., the ratio of government revenue to GDP and of central revenue to general government revenue. Their argument attracted the attention of then-Premier Zhu Rongji and helped to prompt the 1994 fiscal reform to increase 'the two ratios'¹⁴. In June 2013, Beijing University held a conference to celebrate the 20th anniversary of the publication of the *China State Capacity Report*. The participants in the conference praised the Report for having guided the direction of

¹¹ For a collection of debate articles, see 齐墨 (Qi Mo), 新权威主义：对中国大陆未来命运的论争 (New Authoritarianism: A Debate for the Future of Mainland China), 台北, 唐山出版社 (Taipei: Tangshan Chuban She), 1991.

¹² For one systematical analysis of neoconservatism, see J. Fewsmith, "Neoconservatism and the End of the Dengist Era", *Asian Survey*, vol. 35, no. 7, 1995, pp. 635-51.

¹³ 王绍光 胡鞍钢, 中国国家能力报告, 辽宁人民出版社, 1993.

¹⁴ Shaoguang Wang, "China's 1994 Fiscal Reform: An Initial Assessment", *Asian Survey*, vol. 37, no. 9, 1997, pp. 801-802.

the national strategy for the past 20 years (这份报告为后来20年的国家战略标示了路线)¹⁵.

Whether or not this report guided China's national strategy, recentralization of the state's authority helped China to weather the 1997 Asian financial crisis and the 2008 global financial crisis because the authoritarian rule of the party-state remained strong and displayed the following three important features in leading its economic development. First, the authoritarian state was guided not by any ideological doctrine or principles but by pragmatism. Based on Deng Xiaoping's concept of "socialism with Chinese characteristics", the authoritarian state took a two pronged approach toward modernization to develop the economy while maintain political stability. Second, the authoritarian state was strongly pro-development, emphasizing economic growth rather than civil and political rights as an overarching national goal. Third, selectively adopting elements of free market system and liberalizing the Chinese society, the authoritarian state still played a balanced role of invisible and visible hands in the economy¹⁶.

After coming to office, President Xi has made concentrated efforts to overpower the authoritarian state while continuing market-oriented economic reform. Xi formulated his view of a mixed economy with the idea of 'two hands': the 'visible hand' of the state and the 'invisible hand' of the market, and insisted that the two complemented each other¹⁷. To rectify his predecessors' overemphasis on the transformation of China through market-

¹⁵ "王绍光胡鞍钢《中国国家能力报告》出版20周年 强世功,房宁,甘阳等到场祝贺", *观察者*, 3 July 2013,

http://www.guancha.cn/politics/2013_07_03_155658.shtml.

¹⁶ Suisheng Zhao, "The China Model: Can it replace the Western model of Modernization?", *Journal of Contemporary China*, vol. 19, no. 65, 2010.

¹⁷ P. Martin, "A Mandate, Not a Putsch: The Secret of Xi's Success", *China Brief*, vol. 15, no. 3, 4 February 2015,

http://www.jamestown.org/programs/chinabrief/single/?tx_ttnews%5Btt_news%5D=43500&tx_ttnews%5BbackPid%5D=25&cHash=089fb56a35d08ccdd2a88105935d6a4d#.VNOLUijRe5J.

oriented economic reforms, President Xi has “put politics back in command of economics”¹⁸.

Repeatedly warning against ‘Westernization’, Xi emphasized a unified national ideal of the “China Dream” and allowed the security/propaganda axis to tighten up on ideological control and the expression of different political opinions. Taking strong measures to strengthen central Party and government authority, he set up new and powerful Leading Small Groups, such as the Central National Security Commission, Comprehensive Deepening Economic Reform Small Group, with himself as the head to bypass government bureaucracies.

Looking to Mao Zedong for inspiration to manage the country, he launched the largest rectification and mass line campaigns in decades to fight corruption and revived the tradition of self-criticism sessions in which cadres pointed to each other’s failings. A number of senior party and government officials or big tigers as he called them were purged. Some of them were political foes. Describing Mao as “a great figure who changed the face of the nation and led the Chinese people to a new destiny”, Xi has emerged as a champion of party-state power, with himself at the top as a strongman.

2.3 A symbol of national pride

In President Xi’s push for a unique model of China’s modernization maintaining social stability and economic growth while not compromising the party’s authority to rule, the China model has become a symbol of national pride among Chinese nationalistic intellectuals and government officials. It has also appealed to leaders of some developing countries who looked for a recipe for

¹⁸ R.L. Moses, “China’s Xi Builds Support for Big Move: Putting Politics Ahead of the Economy”, *The Wall Street Journal*, 26 January 2015, <http://blogs.wsj.com/chinarealtime/2015/01/26/chinas-xi-builds-support-for-big-move-putting-politics-ahead-of-the-economy/?mod=chinaablog>.

faster growth and greater stability than that offered by the liberal prescriptions of free markets and free elections.

The most important strength of the China model lies in its ability to make complex and difficult decisions quickly and translate them into actions on issues such as large investment and infrastructure construction projects effectively without the disruptions of democratic institutions. Given its strong political will, the Chinese government was able to move more than a million people out of the Three Gorges Dam floodplain and build the longest high-speed railways in the world with little resistance because the Chinese state, in contrast to its Western counterparts, doesn't have to put up with the distractions of a vocal opposition party or have to submit itself to electoral scrutiny at regular intervals. Troublemakers are silenced by tossing them into jail. Even Internet dissents are censored and blocked. China has thus become the world's fastest-growing economy without the visible social and political disorder that often comes with democratization.

The Chinese state's capability is also supported by the huge resources at its disposal. Besides taxation, the Chinese government owns and receives a steady stream of profits from many state-owned enterprises. It also owns all the land in the nation. If the government needs money, it can just sell some land. The Chinese government was therefore much more effective in deploying its enormous state capacity to ward off the global recession than its Western counterparts in 2009-2012. After Lehman Brothers fell in September 2008, the CCP Politburo called for a two-day meeting in early October to fend off the financial crisis. After the meeting, the State Council announced a four trillion-yuan (\$586 billion) economic stimulus package on 9 November. Thereafter, state-run banks pumped huge amounts of money throughout the economy. This huge fiscal stimulus package quickly pushed China's economy out of the downturn.

Hence, the China model's appeal to many political leaders of third-world countries, who see the paramount task as the eradication of poverty, a root cause of conflicts and various forms of

extremism, rather than promotion of liberal democracy. Only three decades ago, China was as poor as some of the poorest third-world countries. While most of the latter remain among the poorest in the world, China's economy has expanded rapidly. Since poverty is the top problem confronting developing countries, China seems to offer a model of how to fight poverty and ensure good governance, albeit one that challenges the conventional wisdom offered by Western countries and the international financial institutions.

The appeal of the China model is also supported by China's value-free diplomacy toward many developing countries, in contrast to Western diplomacy that sets moral principles such as good governance, democracy, transparency, rule of law, and human rights as some of its foreign policy objectives. Guided mostly by economic and strategic interests rather than moral principles, China has developed friendly relations with many developing countries without any preconditions. Given China's rising power status, political leaders in these countries are ready to use Beijing as a hedge against the Western powers and welcome the China model, together with its value-free diplomacy, as an alternative to the European and U.S. versions of both. China has reinforced this attraction through economic aid and access to its growing market¹⁹.

2.4 The fault lines of the China model

For all their glitter and appeal, China's development experiences may not be easily transferable to other countries. While democratic countries committed to the rule of law and the free market cannot learn from the Chinese state's ability to intervene in the economy and control society, the fact that China had three unique initial conditions for development also disqualify Chinese

¹⁹ Suisheng Zhao, "A Neo-Colonialist Predator or Development Partner? China's Engagements and Rebalances in Africa", *Journal of Contemporary China*, vol. 90, no. 23, November 2014.

experiences from easy transposition to other developing countries. First, China's size implies that it has (and had) a large potential internal market able to foster competition and attract foreign interest and investment. Only the U.S. in the 19th Century and India in the 21st have had a similar initial size advantage. Second, China as a labor-abundant economy followed a capital-intensive socialist development strategy. When China finally shifted into a labor-intensive development strategy, the results were explosive. Third, China as a transitional economy retained and rebuilt a hierarchical authoritarian state that it actively deployed in the new market economy environment. Each of these features on its own is potentially important and unique because no other country is so big, possesses such a unique comparative advantage, or operates a remotely similar political system²⁰.

In addition, the China model has some clear fault lines that may make it unsustainable. First, the Chinese state's ability to make quick decisions has come often with high economic and environmental costs. Because one-party rule has put the Chinese government in a position of power without accountability, its quick decision-making ability has often led to politically motivated but economically irrational and distorted investment, waste of resources and environmental deterioration. For example, the quick decision on the four trillion-yuan (\$586 billion) economic stimulus package in the wake of the global financial crisis in 2009 created dangerous long-term economic imbalances, "causing overcapacity in certain infrastructure areas, significant fiscal risks due to reckless local government borrowing, inflation, asset bubbles and potential bad debts following the huge expansion of credit"²¹. The country's high investment rate (about 50 per cent of GDP) of investment rate is a clear reflection of China's low capital efficiency. In the meantime, China has become one of the world's most polluted countries.

²⁰ B. Naughton, "China's distinctive system: Can it be a model for others?", *Journal of Contemporary China*, vol. 19, no. 65, pp. 438-439.

²¹ Yiping Huang, "'Likonomics' policies in China," *East Asia Forum*, 7 July 2013, <http://www.eastasiaforum.org/2013/07/07/likonomics-policies-in-china/>.

Second, a combination of authoritarian state and a market economy has produced a corruptive state capitalism in which power and money forge an alliance. Because there is no opposition party to keep watch on the privileged state officials who may channel their authority into hefty personal fortunes, the government officials, their cronies, and senior managers in state-controlled enterprises have formed strong and exclusive interest groups to pursue economic gains. Acting to protect and enrich specific interests, the state has come to infringe on ordinary people's rights. Arbitrary land acquisitions are prevalent, labor unions are suppressed, and workers have to endure long hours and unsafe conditions. The predatory attitude of the state towards ordinary citizens who enjoy no privilege has caused deep discontent within the society. President Xi's anti-corruption campaign has not aimed at transforming the fundamental features of state capitalism but only punishing corrupt individuals. Questions have, therefore, been asked as to whether Xi and Wang have used the anti-corruption campaign as a weapon to bring down political rivals. The state will remain corrupt unless its power is checked not only by improved responsiveness on the part of its own hierarchy but also by a bottom-up process or what is known as a democratic process.

Third, China now ranks among the countries with the highest income inequality in the world. The last Chinese government's published official national Gini co-efficient was 0.47 in 2010 and the Chinese government has stopped publishing it since then. Even the 0.47 Gini co-efficient makes China more unequal than any developed country: Sweden, for example, has a score of 0.23, and the United States' is 0.45. This alarming inequality arose when China dismantled its social welfare state, leaving hundreds of millions of citizens without any or inadequate provision for healthcare, unemployment insurance, cost of education, and a variety of other social services. These growing gaps have therefore become a serious threat to political stability. Because the worsening inequality led many people to take to the streets in protest, China has entered a period of deepening social tensions

with widespread unrest and protests. The Chinese government is apparently frightened and has relied more and more on coercive forces. The growth and scale of the resources invested by the government in response to growing social conflict has reached alarming levels.

Finally, the China model is based on a false assumption that economic growth trumps everything else. If the government takes care of economic growth, people will be willing to give up all manner of other moral demands, including transparency, accountability, and liberty, and happily leave governance to the government. In fact, once basic subsistence is met by economic growth, the Chinese people have expressed greater demands for the protection of their rights against corruptive state capitalism and the growing inequality it has created. Lacking democratic legitimacy, the Chinese regime has sought performance-based legitimacy by continuous economic growth. But no economy keeps growing at the same pace forever. China is an emerging economy with the problems of all other emerging economies in history, one of which tends to be periods of rapid unbalanced growth followed by periods of stagnation as the imbalances are reversed. Put in a long-term context, China's growth would be more or less in line with its Asian neighbors, such as Japan and South Korea, which all experienced stagnation following high growth. After about three decades of remarkable growth rates, China's economic growth has slowed down since the end of the global financial crisis and could come to a pause or even a setback, given the increasingly tense domestic environment and what breakneck growth engenders, from environmental destruction to rampant corruption and a growing gap between rich and poor. The huge social, economic and environmental prices China has paid for its rapid economic growth could eventually derail China's growth path. The challenge to the China model will ultimately come when economic growth significantly slows down and the government is unable to sustain regime legitimacy simply by its economic performance.

Conclusions

President Xi believes that he has identified a unique model of modernization in which the authoritarian state plays a crucial role in developing the economy while maintaining one-party rule. The peculiar combination of authoritarian state and capitalist economy, nevertheless, has too many serious limitations for the China model to be sustainable in the long run. While undeniably impressive, the China model is widely associated with political oppression and social segregation, environmental pollution and moral disintegration, which raise the question of its sustainability over a prolonged period. Without further reform, including building institutional checks on the state's authority, the negative outcome of the China model would only get worse. One of the striking findings from the 2010-2012 Asia Barometer Survey is that despite China's rising power on the global stage, this is not associated with high levels of East Asians and Chinese themselves selecting their country as a model for development. China on average was the choice of 12.1 per cent of East Asians and a quarter of its own citizens, 26.3 per cent²².

As the social cost of development becomes increasingly unbearable, even those who benefited from rapid economic growth do not think the existing model fits China anymore, evidenced more and more by China's new rich who voted with their feet by choosing to emigrate abroad and send their money out of China. While Chinese law limits individual citizens to the equivalent of \$50,000 per year in foreign exchange, wealthy Chinese have found a variety of alternative ways to move enough money out and acquire US immigration green cards through investment. According to the annual Report on Chinese International Migration 2014, published by the Centre for China and Globalization, in 2013, three-quarters of US investment immigration visas were issued to Chinese nationals, with 6,124 Chinese receiving US green cards through the scheme – almost eight times more than

²² B. Welsh, A. Chang, "Choosing China: Public Perceptions of China as a Model?", *Journal of Contemporary China*, vol. 93, no. 24, 2015.

in 2010. The number of Chinese immigrants reached 9.34 million in 2014 and China is now the world's fourth-largest source country for migrants.

Xi has to convince these wealthy Chinese before he can convince others that he has found a successful modernization model for China.

3. China's Economic Growth. Heading to a “New Normal”

Alessia Amighini

As downward pressures on the Chinese economy are intensifying, President Xi Jinping said the nation needs to adapt to a “New Normal” in the pace of economic growth, with the aim of shifting focus from the speed to the quality of growth. The Chinese economy can no longer postpone facing and solving a series of structural imbalances. Rebalancing the drivers of growth to change the structure of the economy will require deep economic and institutional reforms.

3.1 Introducing a “New Normal” for China's growth

At the opening of the annual National People's Congress (NPC), Chinese premier Li Keqiang officially announced that the growth target for China in 2015 will be of “approximately 7 per cent”, considerably lower than in the past. The announcement came as no surprise as it had been anticipated in a speech by Mr Li in Davos in February stating that the country had “entered the stage of the new normal, shifting from high speed to medium-to-high speed”.

The new growth target set by Beijing is now lower than last year's 7.5 per cent, and more than 2 percentage points lower than in the past two decades. The government's ambitions therefore align with the recent slowdown experienced by the Chinese economy since the beginning of the financial crisis in 2008.

After the first two years of Xi Jinping's term, the Chinese economy grew by 7.4 per cent ‘only’ in 2014 – the lowest rate

since 1990 – low enough to convince Chinese policy makers to shift to a new policy stance, as they realize previous growth targets are no longer sustainable. The shift to a lower but more sustainable growth target came soon after the International Monetary Fund (IMF) warned last year that a series of danger signs suggested that China would probably face a hard landing in the absence of crucial reforms. More specifically, the IMF said that without change, the risk of depressed annual growth of just 2.5 per cent for a ‘protracted period’ of time was ‘medium’ to ‘likely’ before 2030.

Mr Li said that China is likely to face even more serious difficulties in the year ahead, as “downward pressures on China’s economy are building” up quickly and the country is facing “deep-seated problems in development” that can no longer be postponed.

Mr Li assured that the new normal will not be inconsistent with the government’s goal “of finishing building a moderately prosperous society”. In fact, he said “this target is both aligned with our goal in all respects and is appropriate in terms of the need to grow and upgrade our economy”. “A growth rate of approximately 7 per cent will ensure ample employment”, and the government still aims to create 10 million jobs per year to keep the urban unemployment rate at 4.5 per cent or below.

The official announcement has been welcomed by the more dynamic business community. According to Xinhua, the official news agency, Jack Ma, the founder of Alibaba, described growth in China as being “like a man’s height: it can’t grow higher forever”.

Why did the Chinese government decide to shift to a new growth model at Xi Jinping’s mid-term? What are the roots of China’s growth decline? Which structural policies should be put in place to rebalance the Chinese economy?

In fact, the process of rebalancing the economy had already started in China in mid-2005, precisely on 21 July, with introduction of a new exchange rate rule (anchoring the yuan to a basket of currencies). The new exchange rate regime has progressively reduced the profitability of exporting compared to producing for

the domestic market, and therefore has reduced the incentive to invest in the export sector, especially in manufacturing exports¹. Since then, investment has started increasing in services sectors and more recently in construction and infrastructure building. A substantial part of these new investment programmes were financed by local governments (through local banks, which are in turn state-owned). Therefore, the first attempts to rebalance the Chinese economy led to a number of further imbalances, namely excessive investment in the real estate sector and rising public debt both at the central and local levels of government. As that growth model has become visibly unsustainable, the Chinese government eventually opted for a new regime, which has been called the 'New Normal'.

3.2 Understanding China's growth decline

After more than two decades of double-digit growth rates, China is preparing to mark a significant slowdown in 2015, with GDP (Gross Domestic Product) growth estimated at 7 per cent, a further decline from the already unsatisfactory 7.4 per cent in 2014. Industrial production limps and with it investment, which in the final quarter of 2014 reached the lowest rate in 13 years.

In an attempt to limit the damage, the central bank cut rates in November for the first time in two years, further accelerated credit and reduced mortgage rates to stimulate demand. And it is ready to reduce the required reserve ratio of banks to loosen the constraints, which are already low, on credit supply.

In a nutshell, the slowdown is partly the expected result of the phasing out of the impact of an enormous stimulus programme introduced after the financial crisis of 2008 (see Chapter 2). The emergency measures, designed to prevent an excessive drop in production and employment, are likely to further undermine the

¹ O. Blanchard, F. Giavazzi, "Rebalancing Growth in China: A Three-Handed Approach", *China & World Economy*, Institute of World Economics and Politics, Chinese Academy of Social Sciences, vol. 14, no. 4, 2006, pp. 1-20.

economy's ability to reposition itself on a path of sustainable growth. Chinese expansion over the last three decades in fact relied on a set of imbalances. First, macroeconomic imbalances: the excess of investment and credit made the economy vulnerable in being full of low-profit investment projects, which can lead to an increasing amount of bad loans for banks. Today, further accelerating credit to avoid a sharp slowdown has the bitter scent of oil on fire... The excessive role of investment – compared to household consumption – is accompanied by another excess, in foreign demand (exports) compared to domestic demand. This makes the Chinese economy highly dependent on the rest of the world, which adds further fragility.

The other imbalances that Beijing can no longer ignore are the demographic one – with a workforce that is going to shrink, and the demographic dividend now exploited – and the regional divide – with many provinces highly specialized in few sectors producing capital and instrumental goods.

Declining investment

To face the negative impact of the global financial crisis, China launched a major investment programme in the second half of 2008 and 2009, which saw credit expansion and large-scale investment in real estate and infrastructure. Each of those two sectors have since then accounted for one third of China's total investment. Fuelled by massive credit facilities, the housing boom and infrastructure projects kept investment at extremely high growth rates, sustaining the whole economy. But once overcapacity had been reached, the decline in investment projects has dragged the whole economy into a substantial slowdown. As the Chinese economy relies heavily on investment for growth, the decline in investment growth has been a major driver of the current slowdown.

To be blamed now is a stagnant housing market compared to the boom of the last decade, which now – as the history of real estate bubbles teaches – is about to burst, threatening to drag much of the economy with it. The end of the real estate boom has an

impact on many other manufacturing sectors (from materials to furniture) with dramatic consequences on employment.

The national government began to respond to falling growth in the final quarter of 2014, when the National Development and Reform Commission (NDRC) approved infrastructure projects worth more than Rmb693bn (\$112.7 bn). Although the government has substantially redefined its GDP targets, other targets, such as those for rail construction or hydropower installation, remain in place. Further investment in construction and infrastructure will be spurred by the launch of the 'one belt, one road' initiative, which combines the concepts of the Maritime Silk Road and the Silk Road Economic Belt². However, investment projects might be increasingly difficult to realise because of rising constraints on the main sources of revenues for local governments, i.e. land sales, which are contracting as demand for residential and commercial space is on the decline.

Rising public debt

China has accumulated very high debt, close to 210 per cent of GDP. This and other data disclosed in these days refer not only to the debt held by the central government but to the total debt accumulated by all operators resident in China, including local government, businesses and households. If we consider only public debt – that is, the debt of the central government – the percentage of GDP falls below 45 per cent. In this sense, China is far from risking a debt crisis, unlike countries with higher debt/GDP ratio (in descending order: Japan 245, Greece 174, Italy 136, Portugal 131 and the United States 105).

What are the other components of China's debt? If we look at the composition of China's public debt, we see that much of it is made up of bank loans (130 per cent of GDP), given of which 40 per cent to medium and large enterprises, 25 per cent to local government, that is, the provinces, 17 per cent to small companies and another 17 per cent to households. This amount of credit is the

² See Chapter 6.

result of major structural imbalances in the Chinese economy: the high rates of investment that Chinese companies, many of which are state-owned, have been able to sustain were financed by easy credit obtained from banks, which are also state-owned. As long as things go well, no one complains. Since 2009, this mechanism has worked well, because credit has increased from 58 per cent of GDP to current levels. Today it is evident that many of those loans are or will be non-performing, because many of the financed investments, especially in real estate, are not profitable. It is estimated that the amount of non-performing loans reached \$125 million at the end of 2014.

So even if China does not risk running a debt crisis, certainly the situation is delicate because it threatens to overwhelm the whole economic system. Part of the problem is represented by so-called shadow banking, which accounts for 23 per cent of total loans. These are loans made outside the banking sector, of which only 10 per cent are loans made by a trust company. These claims are outside the banking supervisory system that requires banks' efficiency criteria to ensure the soundness of the banking system. In the case of China, however, the problem that is often linked to high debt, that is, the difficulties in repaying debt held abroad, will not arise. Less than 10 per cent of China's debt is in foreign hands, or about \$1 billion, much less than the foreign reserves in the hands of China, four times larger.

Debt is a big burden for the economy. With an average cost of loans at about 7 per cent, borrowers have to generate much higher revenue growth in order to be profitable, and with an economy growing at 7 per cent, this is no longer possible. To face rising financing difficulties, the government plans in 2015 to run its biggest budget deficit since the global financial crisis and has allowed local governments to issue bonds directly. This will introduce further disparities among provinces, as richer, more populous provinces have larger and richer markets, which will support consumption as a driver of growth.

Provinces have a crucial role in this scenario, because it is precisely the uneven development within China that pushes less

advanced provinces to keep up with the more developed coastal provinces. This is partly due to the need to improve internal economic conditions, partly to make them beholden to Beijing. The risk of default is much higher in some provinces, whose growth rates are far below the national average, particularly Liaoning, Yunnan, and Gansu. Some central provinces, Henan, Hubei and Hunan, have better prospects as they grow more than others. Therefore, economic development can be affected in the sense that the most backward and less diversified provinces will have less chance of finding new sources of revenue. This could further worsen divergence among provinces and therefore undermine the efforts by Beijing to overcome the dual model of development, with the coastal provinces far more advanced than others.

The China Banking Regulatory Commission has enabled many provinces to open Asset Management Companies (AMC) since last July. AMC buy distressed assets from banks at discount rates and sell them after they have been securitized, that is, included in a package of securities that have their own dedicated market. It is currently the only action taken with direct effects. These measures, however, treat the effect and not the cause, which remains excessive credit growth. In this sense, the reduction in interest rates and other incentives to stimulate demand for credit in part act in the opposite direction. What we need to look carefully at is the behavior of the individual provinces, declared and implemented, regarding the default of individual cities. Shandong has declared that it will not save the city from bankruptcy. This means that the securities issued by these governments become in fact junk, and that many other provinces will have difficulty in continuing to finance themselves. It seems unlikely that Beijing will allow individual provinces to let local governments go into default, and may take care of the problem. In this case, however, it will exacerbate the origin of the problem, namely the separation of spending decisions from financing capacity at the provincial level.

Demographic transition

China is in the midst of an important demographic transition. This demographic transition is double-sided. Firstly, the age structure of the whole population is changing. The country's working-age ratio (i.e., the number of people between 16 and 65 years old divided by the number of people in non-working age, i.e. children – younger than 16 – and older people – aged over 65) reached its peak of 2:6 in 2010 and has since begun to decline³. In fact, the absolute number of working-age people began to decline in 2012. Secondly, the labor force is moving from the countryside to cities. The rapid economic expansion over the last decade, before the start of the financial crisis in 2008, brought about 200 million people out of agriculture. But recently the rate of migration has slowed substantially, although 35 per cent of China's total labor force still works in the countryside (a much higher percentage than the contribution of agriculture to GDP, i.e. around 10 per cent). These two transitions have together contributed to the slowdown of the economy since 2010, because the labor force started shrinking on the one hand, and on the other, because productivity gains due to the movement of workers from less productive agricultural sectors to more productive urban sectors decelerated.

The net loss of labor in China will be partly offset by a substantial improvement in human capital among young people. Because new workers are twice as productive as retiring workers, China will enjoy large educational dividends created by cross-generational substitution in the next 20 years. Moreover, the educational attainment of the young is improving steadily. Currently, 27 per cent of 18 to 22-year-olds have a college education; by 2020, that number will reach 40 per cent.

Another factor that will further compensate for a declining labor force will be a rise in the retirement age. It is widely accepted in China that the current retirement ages should be

³ Yang Yao, *A New Normal, but with Robust Growth: China's Growth Prospects in the Next 10 Years*, 2015,

<http://www.brookings.edu/~media/Research/Files/Interactives/2014/thinktank/20/chapters/tt20%20china%20growth%20prospects%20yao.pdf>.

raised. Currently, China's retirement age is very low by any standard. Female workers can now retire at the age of 50, and male workers at the age of 55. By the age of 52, half of the women are no longer working; by the age of 58, half of the men. As a result, the labor force participation rate is barely above 60 per cent in the whole population. Even if the retirement age were to be raised by half a year each year over the next 10 years, the reduction in the working-age population, now standing at 2.5 million a year, would be more than compensated.

Regional disparities

Since the beginning of 2014, when the central government announced plans to change the growth model, it also explicitly considered the incentives to offer individual provinces to grow rapidly and be particularly beholden to Beijing. Among the criteria for the promotion of local public managers, more weight is now given to indicators of well-being, innovation, and reducing pollution. Because social stability is still a priority objective of the central and local government, the attraction of big business in the territory will always be a priority. In some provinces, the effects are already visible. Heilongjiang has announced a two-year package of stimulus measures to finance infrastructure projects. Shanxi is moving towards the development of technologies to reduce the use of coal.

Regional disparities within the country are also still substantially large. Although every province recorded lower growth rates than in 2013 – reflecting the national-level slowdown from 7.7 to 7.4 per cent – growth slowdown has not been equally distributed across provinces, but instead has been highly uneven across the country; it mostly occurs in the coastal provinces that produce more than 85 per cent of China's output and exports. Inland provinces have continued to grow at relatively high rates, and this has contributed to increasing convergence within the country. As a result, the rebalancing of China's growth has somehow helped to

improve income distribution (the national Gini coefficient⁴ of personal income declined from 0.481 in 2010 to 0.473 in 2013, according to Yao⁵). Only 5 (out of 31) provinces did not experience a stagnation of GDP in the second half of 2014, four of them (Tibet, Chongqing, Guizhou and Xinjiang) in the western regions, and, in some cases, mainly thanks to central government outlays to ethnic minorities. Other provinces, that are more resistant and stable, are also more diversified by sector, and more devoted to the production of consumer goods, i.e. the coastal provinces. The slowdown of the real estate sector had a negative impact on some western provinces rich in natural resources and based on heavy industries. The most affected by the slowdown, however, are provinces rich in natural resources (such as Shanxi and Hebei). The latest figures also show growing income disparities expected to worsen over the next year. Compared to an average growth of disposable income in urban areas of 9.3 per cent in 2014, some provinces are lagging behind (Chongqing grew by 3 per cent and Hainan by 6 per cent). By contrast, some provinces whose growth rates were already comparatively low in 2013, at around 8 per cent – Shanghai, Beijing and Zhejiang – had much lower declines in growth. This is also due to the fact that their economies are also more diversified, with stronger services sectors and more numerous retail centers, which compensated for the impact of falling investment.

Beijing has indicated that the new growth model must contemplate a move to more modest but more sustainable growth, pledging to reduce the debt of local governments and the overcapacity of many sectors and provinces. But inequality and the growing inter-provincial differences will test the government's ability to cope with the growing socio-economic imbalances: consumption expenditure grew by 12.4 per cent in Jiangsu and 14.2 per cent in Zhejiang, but only 2.8 per cent in Chongqing.

Moreover, richer provinces have more developed and diversified economies, and will be more likely to be able to secure

⁴ See Chapter 2.

⁵ Yang Yao (2015).

funding for their projects. They are also more active in putting in place policies of their own, aimed at sustaining growth. In this spirit, parts of Guangdong, Fujian and Tianjin will launch their own free-trade zones similar to that set up in Shanghai in 2013. Unlike western parts of the country, coastal provinces can benefit from stronger pools of labour force, which can fuel the growth of higher-value-added industries and services.

3.3 Structural reforms to rebalance the economy

As the "New Normal" growth puts the economy on a more sustainable path after three decades of accelerated growth targets and aims to avoid China's heading for a 'hard landing', Mr Li said slower growth makes "structural reform all the more necessary". In a sense, shifting gears to a more appropriate growth rate will help China to achieve modernization of its economy.

By following a more sustainable development path, China intends to avoid falling into the 'middle income trap'. To do so, structural change – rather than the rapid growth of GDP – is the way to achieve a level of average income equal to that of the advanced economies. The main ingredients of structural change are increasing agricultural productivity through the mechanization of sowing and harvesting, progressive urbanization that allows millions of rural workers to move from agriculture to manufacturing and services and find better-paid jobs in urban areas, investment in infrastructure and the introduction of advanced production technology in manufacturing, also (but not exclusively) by foreign multinationals. Moreover, Li said it is vital for China to go ahead with reforms of state-owned enterprises to improve efficiency and productivity and with liberalizing the banking system and financial markets.

Fiscal and market reforms are particularly high on China's reform agenda. The fight against pollution and corruption has contributed to the slowing economy, as dirty industries have been downsized, and the anti-graft campaign has had a chilling effect on some business activity. Although China's policymakers are

currently tackling the short-term emergencies, over the longer run they are seeking to boost consumption to relieve overdependence on export markets and cut wasteful investment. Also, market reforms – implemented in the ‘Made in China 2025’ strategy – will pursue innovation-driven development, apply smart technology, refocus on green development, tackle overcapacity in polluting heavy industries and move Chinese factories up the global value chain. Li also promised a greater role for private business in the economy, which will be further opened up by halving the number of industries in which foreign investment is restricted.

3.4 What to expect next?

As the new normal implies lower growth rates for the Chinese economy, what should we expect in the next decade? Since export growth declined from an average of 29 per cent per annum between 2001 and 2008 to under 10 per cent per annum in recent years, exports as a driver of growth have substantially slowed down. Consequently, the overall contribution of exports to growth has declined from 3 percentage points to about 1 percentage point. As a result, the contribution of net exports has become negligible, at most. At the same time, domestic consumption as a share of GDP began to rise in 2013, after it had stabilized since 2008, due to the comparatively higher rise in investment spending financed by the government’s stimulus packages. Retail consumption behaved very differently across provinces; it held steady especially in Guangdong, which is also the country’s largest provincial market.

In the first half of 2014, services accounted for more than half of the country’s growth. It seems that China has passed the turning point of the inverse U curve of manufacturing widely observed for advanced countries in their earlier days (e.g., the United States in the late 1950s, Japan in the early 1970s). Both employment and output in the manufacturing sector as a share of the national total began to decline in 2013, when manufacturing output was smaller than service output for the first time.

Investment as a share of GDP is likely to decline, but it will probably take a decade for it to drop below 40 per cent, during which time capital stock can still maintain a reasonable growth rate. On top of that, China's innovation capacity is being strengthened. In addition to improvements in human capital, China's spending on research and development (R&D) is accelerating. By 2015, R&D spending will reach 2.2 per cent of GDP, moving close to the ratios prevailing in advanced economies.

A useful contribution to the discussion about what the world should reasonably expect from China's growth has been made by economists and international organizations, both suggesting that China's new normal will entail growth rates in the range of 6 per cent to 7 per cent or even lower in the next 10 years. A useful exercise done by Cai Fang⁶ is to use the international experience to predict China's future growth. Fang calculated China's potential growth rates over 1985-2011 and then predicted China's potential growth rates for the 2014-2023 period. The data show that "the Chinese economy outperformed its potential growth rates in two periods, the 1990s before the Asian financial crisis and the years around the global financial crisis. In between, the Chinese economy experienced deflation and its actual growth rates were below its potential growth rates. China's potential growth rates in the next 10 years are predicted to be in the range of 6.9 to 7.6 per cent, with an average of 7.27 per cent. This is indeed much lower than the 9.4 per cent average in the period 1988-2013".

3.5 Implications for the rest of the world

Despite the slowdown in recent years, China has led world growth since the beginning of the recent financial crisis. The domino effect will be significant. According to the Organisation for Economic Co-operation and Development (OECD), a reduction in

⁶ R. Garnaut, Cai Fang, Ligang Song, *China: A New Model for Growth and Development*, ANU E Press, 2013.

the growth of Chinese demand by 2 percentage points for two years would reduce global GDP by 0.3 percentage points per year. The countries most linked to China as importer will be most damaged, particularly Japan (its main supplier of capital goods), while the United States and Europe will suffer relatively less.

Because one of the most important drivers of growth worldwide is exports, the decline in China's imports and exports will likely contribute substantially to a global slowdown. In 2014 the value of China's imports rose by just 0.5 per cent, marking a substantial slowdown from the 7.3 per cent rise in 2013 and an even bigger departure from the average annual increases of 22.6 per cent in 2002-2011. The value of merchandise imports will continue to increase, by 9.3 per cent a year on average in 2015-2019, according to *The Economist Intelligence Unit's* forecasts. The country's move away from its investment-led growth model is already having a big negative impact on the demand for commodities used by the construction sector, therefore imports from many markets have already declined. This trend also extends to other primary commodities, e.g. imports from Brazil, dominated by soya beans and iron ore, dropped by 4.8 per cent last year. Other big suppliers of commodities in Asia and Africa enjoyed much the same experience. Imports from Australia dropped by 1.2 per cent, from South Africa by 7.8 per cent. Unlike the outlook for commodity-exporting countries, the picture is rosy for countries that specialize in selling consumer goods, technology items and equipment. Chinese demand for consumption goods has become more sophisticated and the mechanization of China's manufacturing sector is also spurring an increase in technology-intensive imports, driven partly by a need to increase productivity as wages increase.

According to some recent research⁷, the slowdown of global trade since 2012 is not just due to cyclical factors (i.e. declining demand), but also to structural factors, namely to a reduction in the elasticity of trade to world GDP. Among the most important

⁷ C. Constantinescu, A. Dennis, A. Mattoo, M. Ruta, *What Lies Behind the Global Trade Slowdown, Global Economic Prospects*, Washington D.C., World Bank, 2015.

reasons for this is the deceleration of China's trade, which in turn reflects the contraction of global value chains⁸. More specifically, the international fragmentation of production processes has spurred world trade over the 2000s, but the global crisis put a halt to this phenomenon, mainly due to the fact that China's exports are increasingly less intensive in imported parts and components, but instead embed more local inputs.

Compared to China, the rest of Asia as a whole will not grow as much, and despite the possibility that it will become a location attractive to investors, it will never be an equally attractive market. China's GDP in 2015 will grow by \$1.2 billion, and will contribute 30 per cent to global GDP growth. The United States will contribute only 22 per cent. Even assuming a significant slowdown, the Chinese economy will remain the engine of global growth in the near future. It is now time for businesses to look at China as a multi-faceted and multi-centered country, with many potential markets in the inland provinces, often with the most promising opportunities in other neighboring countries.

Conclusions

As downward pressures on the Chinese economy are intensifying, and President Xi Jinping announced that the country will have to switch from focussing on the speed to focussing on the quality of growth, the composition of Chinese demand for goods will likely change more rapidly to a more sophisticated consumption model. European producers of both consumption and capital goods will benefit from the new Chinese demand for high-quality goods. However, market access is still cumbersome in a number of sectors due to complex and numerous regulations. Consequently, EU trade policies towards China are likely to benefit from a strategic shift from raising issues of exchange rate misalignments – an argument which is invariably raised by the U.S. – towards

⁸ F. Lemoine, D. Ünal, *Mutations du commerce extérieur chinois*, Lettre du CEPII, no. 352, March 2015.

market access concerns. Since the decision by the EU to open negotiations on a bilateral investment treaty (BIT) in 2013, the EU has intensified its efforts to address problems related to market access in China in some sectors such as cosmetics and medical devices, as well as licensing and market access issues in the area of financial and telecommunication services. Moreover, the slowdown of economic growth and the impact of Xi's anti-corruption campaigns will likely have a negative impact on foreign as well as domestic firms, as the slowdown could be accompanied by the adoption of stricter regulations for foreign invested enterprises. Therefore, continued efforts to increase dialogue on investment access and enforcement of intellectual property rights in China will contribute to balance out the impact on European firms investing and operating in the country.

4. The Irreversible Rise. A New Foreign Policy for a Stronger China

Gudrun Wacker

Two and a half years after the leadership change in Beijing took place, the contours, concepts and priorities of China's foreign policy under Xi Jinping have become clearer. While under the previous leadership the country was officially characterised as being in the phase of 'peace and development' or – somewhat bolder – 'rising peacefully', the rise of China is now treated as an irreversible fact. Deng Xiaoping's dictum of China's foreign policy of "keeping a low profile" which had been valid for several decades has quietly disappeared from the official vocabulary. A more pro-active foreign policy is taking shape as demonstrated by a series of new concepts and initiatives launched at the highest political level. As in other areas of China's politics, Xi Jinping has personally taken the lead in promoting this new pro-active approach.

4.1 General vision – old and new guidelines

As indicated in previous chapters, Xi Jinping's overall vision for his country is encapsulated in the 'China Dream' (*Zhongguo meng* – 中国梦)¹. This vision of China's national rejuvenation also has a

¹ *Zhongguo meng* can also be translated as "Chinese dream", but in order to make clear it is different from the American Dream, "China dream" or "China's dream" seems more appropriate. The question is whether China's dream is indeed identical with the Chinese dream.

foreign policy dimension since it foresees a stronger and more pro-active role of China in the world (*fenfa youwei* – 奋发有为 striving for achievement). While Deng Xiaoping's guideline for foreign policy – “to keep a low profile” (*taoguang yanghui* – 韬光养晦) - has not officially been given up, it seems to have been put quietly to rest. China's foreign policy and diplomacy seems to be shifting from passively adapting to changes in the external environment to actively shaping the external environment. In other words, there is a shift from “responsive diplomacy” (*fanying shi waijiao* 反应式外交) to ‘proactive diplomacy’ (*zhudong shi waijiao* 主动式外交). Wang Yi, in reviewing China's foreign policy in 2013, has repeatedly used the phrase ‘great power (or major power) diplomacy with Chinese characteristics’ (*you Zhongguo tese de daguo waijiao* 有中国特色的大国外交). In contrast to the previous leadership generation, the new generation is apparently now ready to openly call China a ‘great’ or ‘major power’. That notwithstanding, , describing China as a ‘developing country’ has not disappeared from official speeches abroad: for example when Xi Jinping visited Europe in March 2014, he pointed out that China will remain the biggest developing country for some time to come².

4.2 Four pillars of China's foreign policy

China's new foreign policy consists of four pillars³, which can be summarised as follows: relationships with (other) major powers,

²See “Rede des Staatspräsidenten der Volksrepublik China Xi Jinping in der Körber-Stiftung”, *Internationale Politik*, 28 March 2014, <http://www.koerber-stiftung.de/internationale-politik/schwerpunkt-neuer-osten/xi-jinping-2014/rede-xi-jinping.html> [last retrieved on 2 March 2015].

³ Wang Yi: “Zhidao xin xingshi xia Zhongguo waijiao de qiangda sixiang wuqi” [Strong intellectual weapon for guiding China's foreign policy in a new situation], *Zhongguo Gongchandang Xinwenwang*, 12 February 2015, <http://theory.people.com.cn/n/2015/0212/c40531-26552481.html>.

neighbourhood policy, relations with developing countries, and multilateral diplomacy.

Relations with major powers

Even before Xi Jinping took office, when visiting the U.S. in February 2012, he started talking about a ‘new type (or new model) of major power relationship’ (*xinxing daguo guanxi* 新型大国关系) between China and the United States⁴. Its purpose is to avoid the danger of a conflict between the rising (China) and the established power (U.S.) similar to the historical conflicts when Germany and Japan were on the rise – the so-called ‘Thucydides trap’. The main features of such a relationship, according to Xi Jinping, are: 1) no conflict or confrontation, through emphasizing dialogue and treating each other’s strategic intentions objectively; 2) mutual respect, including for each other’s core interests and major concerns; and 3) mutually beneficial cooperation, by abandoning the zero-sum game mentality and advancing areas of mutual interest⁵.

This proposal initiated a debate within China on whether the ‘new type’ of relationship would apply exclusively to the U.S. or also to other ‘major powers’. While some scholars argued that Sino-Russian relations were actually a model version for this new type of relationship, others that the concept could apply to the EU as well, to other emerging powers like Brazil and India, or even Japan. In Chinese foreign policy speeches, the U.S., Russia and the EU are usually listed in one category (‘major power rela-

⁴ Xi Jinping first suggested the ‘new type’ in February 2012 when he met with President Obama in Washington and brought it up again at the informal meeting in Sunnylands in June 2013. U.S. officials (and the President) prefer to speak of a ‘new model’ of major power relations. See P. Haenle, “What Does a New Type of Major-Power Relations Mean for the United States and China?”, *Phoenix Weekly*, 15 January 2014, <http://carnegietsinghua.org/publications/?fa=54202> [last retrieved on 27 February 2015].

⁵ Cheng Li, Lucy Xu, “Chinese Enthusiasm and American Cynicism Over the ‘New Type of Great Power Relations’”, *Brookings China-US Focus*, 4 December 2014, <http://www.brookings.edu/research/opinions/2014/12/05-chinese-pessimism-american-cynicism-great-power-li-xu> [last retrieved on 27 February 2015].

tions'). However, it has become clear that if the focus is on avoiding conflict between rising and established powers, then the "new type" of relations is really about China and the U.S. only.

Other countries, especially in Asia, could be reminded by the 'new type of major power relationship' of the idea of a 'G-2' suggested shortly after Barack Obama was elected U.S. President in 2008⁶. Indeed, when Obama made his first official visit to China in November 2009 he suggested a broad agenda for bilateral cooperation, but China was obviously not ready for such an idea. Many scholars in China saw the 'G-2' as a trap which would lure China into taking over more international responsibility and spending resources which could be better spent on domestic development. Now, a few years later, the situation seems to be almost reversed: the U.S. has responded very lukewarmly to the Chinese proposal. Accepting the "new type of major power relations" has been called by American commentators – ironically – a trap⁷. If the new type of relationship between China and the U.S. is perceived as a code word for dividing the Pacific into two spheres of influence, this will certainly be a source of concern for other countries in the region, especially for Japan.

Despite the continued 'strategic mistrust' between both countries, U.S.-China relations seem to have improved in some areas over the last years. Both sides have a plethora of dialogue fora, their military exchanges have increased, and Obama and Xi have both committed to cooperating on climate change.

Russia and the European Union are usually also dealt with in Chinese foreign policy speeches and documents as 'major powers'. Both relationships are called 'strategic partnerships', but differ greatly in major respects.

While one can argue whether China and Russia maintain a 'new type' of relationship or even the 'model' for it or not, they

⁶ Originally, the G-2 was a proposal for the economic relationship by Fred Bergsten in 2005 and later taken up by others, like former U.S. security adviser Zbigniew Brzezinski, in 2009.

⁷ A.S. Erickson, A.P. Liff, "Not-So-Empty Talk. The Danger of China's 'New Type of Great-Power Relations' Slogan", *Foreign Affairs*, 9 October 2014.

have been moving closer together as a result of the Ukraine crisis and Western sanctions against Russia. Putin has been seeking China's support, and Beijing has to some degree expressed understanding of Russia's annexation of Crimea and its stance on Ukraine. Furthermore, Beijing and Moscow share concerns about Western 'infiltration' and Western plans to 'instigate' colour revolutions and other domestic protest movements. So in terms of ideology and core national interests, both countries have similar views. But as economic partner, Russia's importance has traditionally been limited to the energy and arms sectors. Cooperation in the financial sector might also grow due to Western sanctions on Russia. However, China's increasing economic and political weight in the world has reversed the traditional relationship and so, from Moscow's perspective, Russia would like to diversify its connections and strengthen relations with other countries in Northeast and Southeast Asia. Beijing, on the other hand, has remained very cautious in its support for Putin against the West, at least officially – the U.S. and the EU are still China's biggest markets and remain indispensable for its modernisation goals.

With respect to the European Union, some steps were taken by the new leadership. When Xi Jinping visited the institutions in Brussels in March 2014, this was a first for a Chinese President and secretary general of the Communist Party (contacts with the EU have been traditionally handled by the Prime Minister). Moreover, China's Ministry of Foreign Affairs published a second EU policy paper⁸ in April 2014. Nevertheless, there is more continuity than change in China's relations with the EU. Despite the European debt crisis, the EU remains the most important market for China. Germany is considered as the major partner within the EU, thanks to its economic strength and the technology supplied by German companies. The so-called 16+1 format, consisting of 16 Central and Eastern European countries and

⁸ Full text of the paper: "China's Policy Paper on the EU", 2 April 2014, http://news.xinhuanet.com/english/china/2014-04/02/c_133230788.htm [last retrieved on 26 February 2015].

China and initiated under the previous leadership, has been continued with annual summit meetings, which has raised some concerns in Brussels. It remains to be seen what impact the new Silk Road initiatives (see below) will have on EU-China relations as well as on Sino-Russian.

In conclusion, among the 'major powers', the relationship with the U.S. remains of paramount importance to China. Beijing's attitude is characterized by a contradiction: on the one hand, more or less open criticism of the U.S. role in the Asia-Pacific, especially the maintenance of its military alliances and 'interference' in the territorial issues in the region, has become an omnipresent element in the Chinese discourse; on the other hand, China seems to pursue a 'special relationship', alluding to the possibility of reaching a 'grand bargain' by agreeing on two spheres of interest in the Pacific.

(Greater) neighbourhood

The second pillar or focus is neighbouring countries. China's 'neighbourhood policy' (*zhoubian waijiao* 周边外交) was the topic of a work conference of the CCP's Central Committee in late October 2013. Xi Jinping gave a speech and brought up the concept of 'greater neighbourhood'. This points to a new and much broader definition of what constitutes China's neighbourhood. In this context, the main initiatives, which aim at closer economic and infrastructure integration, are the new Silk Roads, namely the "Economic Belt Silk Road" and the "Maritime Silk Road", in short 'one belt, one road' *yi dai yi lu* 一带一路). With the two "Silk Roads", Xi Jinping has provided a vision for linking Asia and Europe, but this vision also has a strong domestic dimension, with Chinese provinces competing for projects under this broad framework. China announced setting up a "Silk Road Fund" with \$40 billion for investments in infrastructure, resources and industries and financial cooperation⁹. The "Silk Road Fund",

⁹ "China to establish \$40 billion Silk Road infrastructure fund", *Reuters*, 8 November 2014,

as well as the new Asian Infrastructure Investment Bank¹⁰, launched in October 2014, are also part of China's new multilateral economic diplomacy.

These initiatives, which raise the issue of 'connectivity' in the region, no doubt also aim at improving China's image in the region. China's reputation suffered after 2008 due to its assertive – and some would say aggressive – behaviour in the East and South China Seas: challenging Japan's control of the Senkaku/Diaoyu Islands, unilaterally declaring an Air Defense Identification Zone (ADIZ) over the East China Sea, placing an oil-rig in waters claimed by Vietnam, making incursions into areas and building structures on islets and reefs claimed by the Philippines. Therefore economic initiatives do not signal that China has changed its position on its territorial claims. Instead, Beijing made it very clear that it is not willing to compromise on these claims, especially in the East and South China Seas. It is also quite clear that China still insists on bilateral solutions for territorial disputes and is not willing to address them within a multilateral framework or by seeking international arbitration. Chinese Foreign Minister Wang Yi's proposal, made after the Association of Southeast Asian Nations (ASEAN)-China Foreign Ministers' meeting in Myanmar in August 2014, for a 'dual track' approach to the South China Sea issue confirmed, rather than modified this stance¹¹.

By being mainly oriented towards China's western and southern neighbours and aiming at connecting Asia and Europe, 'one road, one belt' is a vision that sort of de-links the U.S. from China's concept of wider neighbourhood, ignoring the fact that the

<http://www.reuters.com/article/2014/11/08/us-china-diplomacy-idUSKBN0IS0BQ20141108> [last retrieved on 26 February 2015].

¹⁰ D. Rodney, Ong Junio: "Asian Infrastructure Investment Bank: An Idea Whose Time Has Come?", *The Diplomat*, 4 December 2014, <http://thediplomat.com/2014/12/asian-infrastructure-investment-bank-an-idea-whose-time-has-come/> [last retrieved on 26 February 2014].

¹¹ Wang Yi, "Handle the South China Sea issue through the 'dual-track' approach", 9 August 2014, http://www.fmprc.gov.cn/mfa_eng/zxxx_662805/t1181523.shtml [last retrieved on 26 February 2015].

U.S. considers itself and is by most countries welcomed as a 'resident power' in the Asia-Pacific region.

In a recent article in the Chinese edition of the *Global Times*, Tsinghua University professor Yan Xuetong argued that the neighbourhood policy is more important and should be given priority over the relationship with the U.S., since all that China can achieve with respect to the U.S. is to reduce the latter's resistance to China's rise, while it can and actually needs to win the support of neighbouring countries¹². Indeed, in the 2014 Report on the Work of the Government, neighbourhood diplomacy was listed first, followed by developing countries. Major power relations only made position 3 on the list. Xi Jinping underlined the importance of a pro-active neighbourhood policy (that also builds up China's soft power) again in November 2014 at a Central Foreign Affairs Work Conference, attended by all members of the Standing Committee of the Politburo¹³.

Relations with emerging and developing countries

A third focus of Xi Jinping's foreign policy is relations with emerging and developing countries all over the world. This focus is not new – China has continuously tried to project its image as a member of the developing countries and as the voice of the developing world. Beijing's new activism can mainly be seen within the grouping of BRICS – Brazil, Russia, India, China and South Africa – as part of the global South. These emerging countries started to hold separate summit meetings since 2008.

While over the last ten years, China has become an important provider of aid to developing countries and is now ranking among the ten biggest donor countries in the world, it operates outside the

¹² Yan Xuetong: "Zhongguo waijiao 'zhoubian' bi Meiguo geng zhongyao" 阎学通: 中国外交“周边”比美国更重要 [In China's foreign policy, 'neighbours' are more important than the U.S.], *Huanqiu Shibao*, 13 January 2015.

¹³ For a short analysis of Xi's speech see C.K. Johnson, "Xi Jinping Unveils his Foreign Policy Vision: Peace through Strength", CSIS Freeman Chair Newsletter December 2014; "Xi eyes more enabling int'l environment for China's peaceful development", *Xinhuanet*, 30 November 2014.

framework agreed on by the Organisation for Economic Co-operation and Development (OECD) countries. The main difference from the OECD rules is that China usually does not attach any conditions (on anti-corruption etc.) to its soft loans and aid packages. China's foreign aid has been met with criticism in the West also because of its lack of transparency. In July 2014, the Chinese government published its second *White Paper on Foreign Aid*¹⁴, which provided some more information on the scope and distribution of funding than its predecessor¹⁵.

Under the new leadership, China has taken steps to set up some new institutions focused on infrastructure development¹⁶ in cooperation with other partners. One major step that was taken in July 2014 at the BRICS summit in Fortaleza (Brazil) was when the BRICS development bank, named New Development Bank (NDB), and a reserve currency fund, the Contingent Reserve Arrangement (CRA) were established. The NDB's focus will be on "infrastructure and sustainable development"; the CRA is intended to provide the BRICS countries with protection against short-term balance of payment pressures¹⁷.

Multilateral diplomacy

The fourth pillar is the multilateral arena. China will invest more energy in multilateral organisations and formats – mainly in those organisations where the U.S. is not a member and where China is therefore in a better position to control and shape the agenda. The

¹⁴ Information Office of the State Council, *China's Foreign Aid (2014)*, July 2014, <http://www.scio.gov.cn/zxbd/wz/Document/1374915/1374915.htm> [last retrieved on 28 February 2015]. The first such white paper had been published in 2011, but just gave aggregated figures.

¹⁵ For a short analysis of the White Paper, see Zhou Taidong: "China's Second White Paper on Foreign Aid Signals Key Shift in Aid Delivery Strategy", The Asia Foundation, 23 July 2014, <http://asiafoundation.org/in-asia/2014/07/23/chinas-second-white-paper-on-foreign-aid-signals-key-shift-in-aid-delivery-strategy/> [last retrieved on 28 February 2015].

¹⁶ Infrastructure development is one of the areas where China has gathered a lot of experience and has the additional advantage that China can export its overcapacities in the construction sector.

¹⁷ See official website of the 6th BRICS summit at <http://brics6.itamaraty.gov.br/>.

multilateral diplomacy mainly manifests itself in so-called 'host diplomacy': China actively offers to host international meetings, thus underlining its positive and constructive international role. Most of these activities are centred on Asia, so they also fall under the pillar of China's neighbourhood policy.

One example of this 'host diplomacy' was the summit of the 'Conference on Interaction and Confidence Building in Asia' (CICA), a little-known organisation of mainly Central and West Asian countries initiated by Kazakh President Nursultan Nazarbaev in the early 1990s. The summit was held in Shanghai in June 2014 and combined the two pillars of 'greater neighbourhood' and multilateralism/'host diplomacy'. Xi Jinping proposed in his speech a new Asian security concept. He argued that Asian security should be dealt with by Asians themselves and not by outsiders (meaning the U.S.)¹⁸. In view of the very diverse membership of CICA, the practical implications of Xi's 'new security concept' and CICA as an organisation remain to be seen.

Also in the domain of security, it was decided that the Xiangshan Forum (*Xiangshan luntan* 香山论坛), a track-2 conference organised by the China Association for Military Science (*Zhongguo junshi kexueyuan* 中国军事科学院) bi-annually in Beijing, would be upgraded to an annual event with the participation of Foreign Defence Ministers and delegates from the military. The first upgraded dialogue was held in November 2014. It is clear that China wants this meeting to become an equivalent to the Shangri-La Dialogue, which takes place every year in Singapore and brings together Foreign and Defence Ministers, high officials and scholars from Asia, the U.S. and some European countries¹⁹.

There are other examples where China used multilateral frameworks as platforms for presenting new initiatives. The Asia-Pacific Economic Cooperation (APEC) summit was hosted by

¹⁸ See Xi Jinping: "New Approach for Asian Security Cooperation" (speech held on May, 21, 2014), in: Xi Jinping, "The Governance of China", *Beijing*, 2014, pp. 389-96, 392.

¹⁹ E. Teo: "China defends military expansion; Minister calls for open and inclusive Asia-Pacific security architecture", *The Straits Times*, 22 November 2014.

China in November 2014 and was used to promote an APEC-wide Free Trade Agreement (Free Trade Area of the Asia-Pacific [FTAAP]). This can be interpreted as a response to the Trans-Pacific Partnership (TPP) FTA, a project from which China had initially been explicitly excluded, but also has not officially declared an interest in joining.

A month before the APEC summit, the signing ceremony had been held in Beijing for the Asian Infrastructure Investment Bank (AIIB) with 21 countries. China had announced this project in October 2013 in Indonesia before the APEC summit (from which President Obama was absent due to the government shut-down). Several regional countries – Japan, South Korea, Australia and Indonesia – have not pledged cooperation with the AIIB, apparently under pressure from the U.S.²⁰. However, they might reconsider their position. The concerns raised by the U.S. are related to the rules and standards (environment, labour...) that will be applied by the bank in future. But these issues are not yet cast in iron and can be addressed by members. By opposing the bank one can only make sure of having no influence on its operating principles²¹. Moreover, by using its influence to prevent other countries from joining the bank, the U.S. feeds suspicions that it wants to prevent China's rise or contain it.

While China argues that projects like the BRICS Development Bank and the AIIB will complement the existing financial institutions²², they can also be understood as a manifestation of China's and other emerging countries' frustration with the lack of progress in these established institutions: International Monetary

²⁰ "Why China is creating a new 'World Bank' for Asia", *The Economist*, 11 November 2014, <http://www.economist.com/node/21632027> [last retrieved on 20 February 2015].

²¹ The debate has recently shifted in this direction, see for example E. Feigenbaum: "The New Asian Order. And How the United States Fits In", *Foreign Affairs*, 2 February 2015; T. Kikuchi, T. Masutomo: "Japan should influence China from within the AIIB", *The Straits Times*, 3 February 2015.

²² According to calculations of the Asian Development Bank, investment needed in Asia for infrastructure 2010-2020 is 8 trillion US-\$. Yu Yongding, D. Lombardi: "China's G-20 Moment", *Project Syndicate*, 4 February 2015.

Fund (IMF) and World Bank reforms to accommodate the growing economic weight of the emerging countries were announced by the two institutions in spring 2010, but implementation has been held up by the U.S. Congress, protecting U.S. and also Western European interests²³. In absence of the promised redistribution of voting rights, it is not surprising that China and other emerging countries have begun to pursue alternative options that give them more say and more room to manoeuvre. An additional advantage for China is that if projects are funded through these banks they will be more acceptable and might create less public criticism and resistance in the recipient countries.

However, setting up its own institutions does not mean that China's participation in the existing multilateral institutions and organisations has weakened: China will also take over the G-20 presidency in 2016 and host the summit meeting²⁴.

Conclusions

Usually, comments of foreign observers point out that there is a major gap between China's peace rhetoric and its actual behaviour. However, official speeches by China's new leaders are quite straightforward in underlining that China will not tolerate being pushed around and will not make any compromise on its territorial claims. Therefore, China seems to actively pursue a parallel strategy of positive, mainly economic, initiatives (like the two Silk Roads) and small steps to advance China's position on the territorial issues. And this double strategy is also reflected in major policy speeches.

It is too early to tell whether the positive signals that Xi Jinping sent at the APEC summit - cautious steps to rebuild the relationship with Japan, shaking hands with Prime Minister Abe, signing a Memorandum of Understanding with the U.S. on encounters at sea

²³ Ibid.

²⁴ Ibid.

and in the air, climate deal with the U.S. - are tactical moves or first signs of a change in strategy.

In sum, however, there is a noticeable change in China's foreign policy towards more activism and more clarity (in a positive and negative sense). While the focus of this new activism is on China's periphery (albeit an extended understanding of this periphery), it is unclear whether China has realized just how much concern it has created over the last five years, especially among its neighbours. The fact that Xi Jinping has started to underline the importance of soft power as an instrument of China's foreign policy *vis-à-vis* the region indicates that there is some awareness of the loss of good reputation. With the new initiatives launched by Beijing, China tries to actively shape an environment that is beneficial to its interests and to limit the influence of the U.S.²⁵. Again, Beijing pursues two avenues in parallel by setting up new multilateral institutions where China can play a stronger role while at the same time staying active in existing institutions, traditionally dominated by the West, like the United Nations or the G-20.

²⁵ See Zheng Wang, "China's Alternative Diplomacy", *The Diplomat*, 30 January 2015.

5. EU and China: Making Room for Result-oriented Dialogue

Axel Berkofsky

Since 2003 the EU and China have referred to each other as ‘strategic partners.’ As an expression of that partnership, Brussels and Beijing have over the last decade established more than 50 bilateral so-called ‘sectoral dialogues’ covering 24 areas, including competition policy, civil aviation, market access, intellectual property rights, nuclear energy, food safety, environment, regulatory and industrial policy, trade policy etc. While the intense institutional exchanges suggest that Brussels and Beijing both assign great importance above all to bilateral trade investment ties, many of the problems and disagreements covered by many of the ‘sectoral dialogues’ have been dealt with for years without any results and progress to show for it. The dialogues dealing with issues related to trade and investment, such as the ones on market access, government procurement and intellectual property rights in particular, deal with issues European business investing in China has been complaining about for years. In fact, the list of complaints about the obstacles European investors and investments in China are confronted with has remained – at least as far as the Beijing-based EU Chamber of Commerce is concerned – (very) long and indeed identical over the years.

Problems on the bilateral trade and investment agenda notwithstanding, in 2013 the EU and China again confirmed their ‘strategic partnership’ by adopting the “EU-China 2020 Strategic Agenda for Cooperation”. Sino-European cooperation in international politics and security (under the headline ‘Peace and Security’) will – at least according to that policy paper – feature

prominently on the EU-China policy agenda in the years ahead¹. The number of areas and issues Brussels and Beijing envision to be jointly dealing with is big and includes areas such as nuclear security, the international non-proliferation regime and related export control arrangements, transnational organised crime, cyber-crime, anti-terrorism, maritime security as well Asian security in the framework of the below-cited “EU-China High Level Strategic Dialogue”. The “EU-China 2020 Strategic Agenda for Cooperation” also announced that it would “raise the level of EU-China dialogue and cooperation on defence and security, advancing towards more practical cooperation”. While this sounds promising on paper, the move towards more ‘practical security cooperation’ (i.e. the adoption of joint security policies) is very unlikely to take place any time soon (if ever). EU policymakers are without a doubt aware of the limits of concrete EU-Chinese security cooperation on (Asian) ground and know that the aspiration to move towards practical cooperation, i.e. joint EU-China security policies in Asia and elsewhere, will in the years ahead realistically continue to remain a case of wishful-thinking. Indeed, the EU and China continue to have very different positions on most (if not all) current issues on the regional and international security agendas, be it the crisis in Ukraine, the Middle East (e.g. Iran or Syria), and the so-called ‘rogue regimes’ in North Korea or Sudan – hardly the basis for moving towards practical cooperation on security in Asia (or elsewhere). The recent years of EU-Chinese consultations and dialogues on regional and global security have shown that the EU’s influence on actual Chinese foreign and security policy behaviour and policies must be described as very limited, if at all existent. In other words, Beijing will realistically not alter the quality of its regional foreign and security policies in response to European advice or requests to do so. China denying others the right to ‘interfere’ in any of what China refers to as its ‘internal affairs’ is (very) deeply embedded in Chinese foreign and security

¹ European External Action Service, EU-China 2020 Strategic Agenda for Cooperation, http://www.eeas.europa.eu/china/docs/20131123_agenda_2020__en.pdf.

policy thinking and Beijing will continue to take on board only the kind of advice on its foreign and security policies that comes nowhere near to resembling ‘interference’. In fact, since China’s leadership transition in 2012, Chinese policymakers as well as Chinese scholars interacting with European counterparts tend to become very defensive very quickly when ‘smelling’ anything that might be in the slightest way interpretable as ‘interference’ in Chinese domestic affairs from the outside. This is not to judge whether this is right or wrong or acceptable when dealing with European counterparts (officials as well as scholars), but it is – at least from this author’s perspective – the reality of European-Chinese exchanges and interactions on the quality and conduct of Chinese foreign and security policies. China is arguably in a phase of seeking to define its identity, role and reach as regional and global security policy actor and it will cooperate with the EU on security if such cooperation does not – at least from a Chinese perspective – obstruct the process of developing the kind of foreign and security policy identity developed in Beijing (as opposed to in Brussels or Washington).

5.1 Unwanted outside ‘interference’

Even if often-repeated official rhetoric speaking of EU-Chinese ‘mutual understanding’ and ‘shared values’, or ‘common interests’ might suggest otherwise, the history of European colonialism in Asia in general and China in particular is still very present in China’s historical memory and it is fair to point out that any European opinion on Chinese domestic and foreign policies that could be interpreted as unwanted ‘interference’ is in today’s China almost inevitably associated with European colonialism and China’s so-called ‘Century of Humiliation’, i.e. the roughly 100 years from the first ‘Opium War’ (1839) to the founding of the People’s Republic of China (PRC) in 1949. Furthermore, in order to be able to understand current Chinese foreign policy behaviour (and reactions to other countries’ foreign policies towards China), it is necessary to call attention to the fact that China’s President Xi

Jinping has over the last two years in his speeches on domestic and foreign policies numerous times called on the Chinese people to remember China's past of European colonialism and imperialism when outlining his vision of the so-called "China Dream" to the Chinese people. (For details on Xi's "China Dream" and what is referred to as 'National Revival' see Professor Zhao's contribution to this volume). The 'induction' of national self-confidence (accompanied by patriotism and at times strong nationalism) through Xi's "China Dream" has without a doubt had an impact on how much outside advice and opinions (or 'interference' from a Chinese perspective) Chinese foreign policymakers are willing to accept. Indeed, an economically rapidly growing China governed by a political leader and leadership determined to encourage the Chinese people to exercise Chinese economic and political patriotism probably feels less than ever inclined to endorse outside advice which in turn within China could be interpreted as a sign of weakness. The analyses of China's 'national psyche' taking into account Chinese history of the 18th and 19th Centuries have over recent years sought to explain current Chinese foreign policy rhetoric and more importantly foreign policy behaviour. Among others, scholars concluded that Chinese foreign policy approaches and policies are – at least up to a point – the result of a mix between an 'inferiority complex' (as a remnant of the aforesaid 'Century of Humiliation') and a growing 'national self-confidence' (as a result of China's phenomenal economic growth and development over the last 30 years)². Such – at least from a European perspective – contradictory elements making up and defining China's 'national psyche' produce policies that in the West are at times or indeed often perceived as nationalistic and driven by the motivation and determination to conduct policies independent and free from Western pressure and lecturing. The scope and limits of China's cooperation with the EU and Europe

² See e.g. Zheng Wang, *Never Forget National Humiliation*, Columbia University Press, New York, 2012 and W.A. Callahan, *China: The Pessimist Nation*, Oxford University Press, New York, 2012.

in international politics and security has to be understood and analysed against that background.

States usually only do what they have to do and China is certainly no exception. The recent years of Chinese domestic and foreign policies have provided plenty of evidence that giving in to European requests to make its political and governance system more 'European' or more 'Western' is not – put bluntly – one of the things China's policymakers feel that they have to do. China is referring to itself as a 'great power' and Xi Jinping's foreign policy rhetoric and his earlier cited determination to induce the concept of China's so-called 'National Revival' into the Chinese psyche is making sure that China's policymakers in case of doubt opt for 'interference'. In fact, in the current political atmosphere and the ongoing phase of Xi's campaigns and policies of consolidating his power in China, opting for categorically referring to any outside opinion on Chinese domestic and foreign policy as unwanted 'interference' has become the 'safe option' as it makes Chinese policymakers less vulnerable to inter-Chinese accusations of being 'weak' towards the West. To be sure, the jury is still out on whether such an approach is sustainable in the long-term and whether China might – against the background of China's rapidly growing economy and global investments – find out that the 'principle of non-interference' and the *de facto* refusal to accept outside advice on its foreign and foreign economic policies could become unsustainable³. According to U.S. China scholar David Shambaugh, China's determination to insist on the 'principle of non-interference' in defence of Beijing's foreign policy independence from outside pressure has already led to Beijing being short of 'friends' and without any close allies – a 'lonely power' as Shambaugh calls China⁴.

³ For the pros and cons of the 'principle of non-interference' from Chinese perspectives see "The End of Non-Interference", European Council on Foreign Relations 24 October 2013, http://www.ecfr.eu/page/-/China_Analysis_The_End_of_Non_interference_October2013.pdf.

⁴ D. Shambaugh, *The Illusion of Chinese Power*, Brookings Institution 25 June 2014, <http://www.brookings.edu/research/opinions/2014/06/23-chinese-power-shambaugh>; Shambaugh calling China a 'lonely power' in mid-2014 has created a

As far as Chinese trade and business interests with and in Europe are – at least for now – concerned, China's reluctance to endorse EU advice and input on its domestic and foreign policies does not have an impact on its ability to get from Europe what it wants most: market access, technical assistance, know-how and the expansion of trade and investment ties in general. Chinese policymakers are clearly aware and take advantage of the fact that European policymakers have over the last two years become very reluctant to criticize Chinese domestic and foreign policy conduct so as to avoid jeopardizing business and trade ties with China. The recent past has shown that Beijing does not hesitate to threaten its trade and investment partners with economic and trade retaliation in the case of unwanted 'interference' in what China refers to as strictly 'internal affairs'. Past Chinese reactions to European and EU opinions on human rights, freedom of speech and expression, freedom of religion Tibet and Taiwan are cases in point.

5.2 Not (fully) trusting the EU...

Chinese policymakers are undoubtedly aware that the EU and the big EU member states would side with the U.S. on Asian security issues in the case of a U.S.-Chinese controversy if the conflict in question also affected European interests. Beijing has probably very few illusions about European preparedness to side with China and not the U.S., should Washington's security interests in the region be affected by China's regional security policies. When China in the early 2000s – during Washington's unilateral moment in international politics and the invasion of Iraq in 2003 – asked Europe to endorse the concept of a 'multipolar world' to counter U.S. unilateralism, the European reaction (perhaps with the exception of France and Germany, which refused to participate in the invasion and later occupation of Iraq) was not enthusiastic, to say the very least. There are few illusions in Beijing about the fact

very vivid and indeed controversial debate on China outside but also inside of China on the state and quality of Chinese diplomacy and foreign policies.

that the EU's political and security ties with Washington are much deeper than the ones with Beijing, which have led Beijing's policymakers not to fully trust European counterparts to adopt policies which would run counter to or are fully independent from U.S. policies. In fact, there are numerous scholars and also policymakers in China who argue that high-sounding EU-China statements on the quality and scope of bilateral EU-Chinese security cooperation do not change anything about the fact that Europe continues to be an 'agent' of U.S. interests in the region.

5.3 ... because it backs U.S. containment, Beijing fears

When the U.S. administration announced its 'pivot to Asia' in 2011, accompanied by increased U.S. involvement in Asian security through the strengthening of existing military alliances with Japan and South Korea and the establishment of new defence ties with countries such as Australia, India, the Philippines, and Vietnam, Beijing immediately concluded that Washington's Asia 'pivot' was aimed at containing China. Beijing policymakers argued then (and still do) that the U.S. 'pivot' and the expansion of U.S. defence ties in the region accompanying it are aimed at 'encircling' China and continuing to ensure U.S. regional military hegemony, deterring China's rapid economic and military rise. While to date Washington continues to argue that its Asia 'pivot' is in no way intended to 'encircle' China, China continues to insist that it does just that. Furthermore, from China's perspective the 'pivot' is a U.S. attempt to convince other Asian countries to join Washington to deter China's economic and political rise and that Europe will – again from a Chinese perspective – sooner or later be pressured into actively supporting China's containment. European scholars on the other hand argue that the expansion of the EU's economic and political engagement in Asia in general and with China in particular over the last decade can be referred to

as a EU 'pivot' to Asia⁵. To be sure, not a 'pivot' with the expansion of military ties and alliances at the centre but instead one with policies aimed at engaging China economically and politically as much as possible.

When in July 2012 Catherine Ashton, then EU High Representative for Foreign Affairs and Security Policy and Hillary Clinton, then U.S. Secretary of State adopted⁶ the "U.S.-EU Statement on the Asia-Pacific Region"⁷, EU policymakers found themselves under pressure to explain to Chinese counterparts why the joint U.S.-EU statement on Asian security does not mean the EU allying itself with U.S.-led China containment policies. Beijing on the other hand maintained back then that the Clinton-Ashton joint statement sounded like the EU preparing itself to get involved in a U.S.-driven containment policy strategy towards China even if such a conclusion does not at all reflect the realities of EU foreign and security policies towards Asia in general and China in particular.

5.4 Fundamentally different

The debate on the scope and quality of EU-Chinese cooperation in international politics tends to neglect the fundamental question of whether and to what extent cooperation between democratic and non-democratic countries in international politics and security beyond informal consultations is at all feasible and able to produce actual results in the form of measurable joint policies.

While it is from a policymaker's point of view understandable – understandable since a policymaker is expected to produce on

⁵ N. Casarini, *The European 'Pivot'*, Issue Alert EU Institute for Security Studies (Euiss), Paris, March 2013,

http://www.iss.europa.eu/uploads/media/Alert_Asia.pdf;

J. Parello-Plesner, *Europe's Pivot to Asia*, East Asia Forum, 12 November 2012, www.eastasiaforum.org/2012/11/12/europes-pivot-to-Asia/.

⁶ See U.S. Department of State July 12, 2012, U.S.-EU Statement on the Asia-Pacific Region; <http://www.state.gov/r/pa/prs/ps/2012/07/194896.htm>

⁷ On the side-lines of the Asean Regional Forum (ARF) in Phnom Penh, Cambodia.

paper commitments from counterparts to demonstrate on paper preparedness to cooperate— to publicly ignore the question of the feasibility and prospects of actual results as regards cooperation, the absence of actual joint EU-Chinese policies provides evidence that different forms and systems of governance matter and have an impact on whether joint policies are at all realistic. In fact, it is accurate to conclude that Chinese regional and global foreign and security policies over the last two to three years have more than anything else demonstrated that Chinese approaches towards regional and global politics and security are fundamentally different from European approaches and policies. Furthermore, EU-Chinese bilateral consultations and dialogues on human rights, governance, democracy, freedom of speech and expression, terrorism and arguably many other issues have made it very clear that Beijing and Brussels often do not even agree on shared definitions of concepts such as human rights, democracy and terrorism. While policymakers in both Europe and China tend – at least on the official record – to play down the differences as regards differing definitions standing in the way of going beyond agreeing to disagree – scholars and analysts like this author cannot but conclude that the absence of the aforesaid jointly shared definitions a priori limit and indeed nullify the possibilities of actual meaningful cooperation. Against the background of China’s previously cited determination to defend itself against any form of ‘interference’ in its internal and foreign policies, there should be few illusions that European policymakers are able to ‘impose’ their definitions and concepts on Chinese counterparts.

5.5 “EU-China High Level Strategic Dialogue”

Doubts about the potential impact of European concerns and advice on Chinese regional and global security policy notwithstanding, in 2010 the EU and China set up an annual dialogue on Asian security. The most recent annual “EU-China High Level Strategic Dialogue” was held in January 2014 and Brussels among others hoped that the dialogue would encourage Beijing to become

more transparent about its defence expenditures and military equipment procurement and sales policies. However, that is clearly a case of European wishful-thinking as China will not make any more information on its arms procurement policies available simply because the EU is requesting just that in a bilateral dialogue. When analysts (like this author) argue that the EU-China strategic dialogue on Asian security is more than anything else an annual window-dressing event as opposed to a dialogue that produces real results, let alone joint Asian security policies, EU policymakers typically point out that the dialogue's objective is not the adoption of joint policies but rather a platform to informally consult with each other on Asian security issues. While dialogue and consultations are positive as such, the *raison d'être* of such a dialogue must be – at least from an analyst's perspective – put in doubt if European advice and input on Chinese regional security policy conduct such as Beijing's (very) assertive policies related to territorial claims in the East and South China Seas are quite simply ignored in Beijing. Indeed, the reality of Chinese regional security policy conduct and policies has shown that Beijing's preparedness to consult with the EU on security issues which fall under what Beijing refers to as its 'core interests' – the Taiwan and Tibet 'questions' and what Beijing refers to as 'territorial integrity' in Asia's disputed territorial waters – is very limited, if at all existent. If that is accurate and if European views and advice on Chinese security policies in Asia are only endorsed during official encounters as opposed to in the 'real' world, then it is fair to question whether the dialogue on Asian security with China is an efficient use of EU resources and political capital.

Brussels' reluctance to get involved in Asian territorial conflicts that involve China beyond urging involved parties to solve conflicts peacefully, have undoubtedly led Beijing policymakers to conclude that Brussels does not pose a 'danger' as regards 'interference' in China's regional security policies. While such reluctance has undoubtedly facilitated the establishment of the aforesaid EU-China dialogue on Asian security, it has also ensured that the EU's credibility as a coherent and unified foreign and

security policymaker is perceived as (very) limited in Beijing. To be sure, while Beijing on the official record complains about the Europe's inability to formulate and adopt joint foreign and security policies, such inability makes sure that the EU is probably just the kind of institution China wants the EU to be: an institution with a foreign policy apparatus that is not equipped with the instruments and the authority to formulate policies towards China that cannot be undermined by individual EU member states when and how they see fit. In other words: an European External Action Service (EEAS) that can be ignored if and when it adopts policies towards China which China in turn perceives as threatening its interests or as unwanted 'interference' in its internal affairs.

5.6 Putting EU scepticism on paper

It is noteworthy that a significant part of the EU's 'Guidelines on the EU's Foreign and Security Policy in East Asia' adopted in June 2012⁸ deal with China and the limits, problems and possibilities of EU-China cooperation in regional politics and security. Noteworthy because the guidelines display an arguably fairly negative EU assessment of the quality of Chinese domestic and foreign policies by listing a number of issues of China's domestic and regional foreign and security policy agendas which from an EU perspective China needs to address. Such issues include human rights, the – from an EU perspective – insufficiently developed application of the rule of law in China and the lack of progress as regards fundamental freedoms in the country. In that context, the guidelines lament that China is in Europe's view not sufficiently included in regional and global structures of economic and political governance (which is another way of saying that China does not abide by and/or adopt globally acknowledged and applicable rules of economic and political governance). Finally,

⁸ See Guidelines on the EU's Foreign and Security Policy in East Asia; Council of the European Union, General Secretariat, 15 June 2012, http://eeas.europa.eu/asia/docs/guidelines_eu_foreign_sec_pol_east_asia_en.pdf.

the guidelines urge China to become more transparent about its defence spending. Realistically, however, Europe criticizing Chinese domestic and foreign policies in general and calling for more transparency in China's defence spending in particular will, like in the past, be ignored in Beijing. The long list of problematic issues the guidelines list concerning Chinese approaches to the rule of law, governance, international politics and (many) other issues suggest that, from Brussels' perspective, the EU and China have in terms of governance and approaches towards international politics and security far too little in common to base any joint policies on.

Conclusions

China, François Godement concludes, is a realist power that does not in any way feel obliged to take European foreign policy opinions and criticism into account when implementing its foreign and security policies in Asia and elsewhere. "As a realist power, China has neither the inclination to consider Europe's geopolitical influence at a time when Europe is struggling with an ongoing economic and political crisis, nor the incentive to favour a more united and empowered Europe that would also be a more effective negotiator with China"⁹. As long as individual EU member states opt for adopting their own China policies when it suits their interests, Godement goes on to conclude, China will reserve the right to consider the EU a 'support actor' and not a protagonist in international politics and security. "National shortcuts are very tempting, but they will weaken the EU's hand as a whole, and if such an approach is pursued Europe will never receive the kind of recognition from China that a united continent of 500 million people can expect to command".

⁹ F. Godement, *Key Issues of China's Leadership Succession*, in N. Casarini, *Brussels-Beijing: Changing the Game*; Report no.14, European Institute for Security Studies (Euiss), Paris, February 2013, http://www.iss.europa.eu/uploads/media/Report__14.pdf.

A European role promoting European models and modes of security multilateralism, some European scholars and (many) EU policymakers argue, is endorsed in Asia, including in China¹⁰. However, as was sought to show above, such an assessment does clearly not reflect the realities of Chinese regional security policies. Insisting on the aforesaid ‘principle of non-interference’, there is a near-consensus among independent China scholars and analysts that Beijing will continue to remain opposed to meaningfully multilateralizing its regional security policies. Indeed, unless there is a fundamental shift in Chinese foreign policy thinking and making (which is very unlikely), Chinese policymakers will continue to pursue what can be referred to as ‘multilateralism *à la carte*’ and Beijing will continue to turn to individual EU member states if does not – to put it bluntly – get what it wants from EU institutions. The problem of course does not lie with China alone. The three biggest EU member states – Germany, France and the UK – will continue to formulate and adopt their very own policies towards China, which will continue to have a negative impact on the EU’s ability to ‘have’ one set of European economic, political and security policies towards China. Numerous times in the past these three EU countries adopted their own foreign policies towards China without in any way feeling obliged to consult with the European External Action Service (EEAS). Unless there is a fundamental shift in how the EU’s big member states conduct their respective foreign and security policies and unless they are prepared to assign more authority and competencies to the EEAS at the expense of the ability to adopt individual policies towards China, Beijing will continue to be able to exploit the lack of European unity for its own benefit. While China is not the only country and actor exploiting insufficient European foreign and security policy coherence, it is – viewed against the background of Europe’s trade and investment ties and interests with and in China

¹⁰ S. Peyrouse, *Europe’s Involvement in East Asian Security-How to Engage China*, Fridre Analysis, October 2012, <http://www.fridre.org/publication/1058/europe’s-involvement-in-east-asian-security>.

– probably the country in a position to exploit the lack of inner-EU unity most successfully.

All of this is not to say that China does not take the EU seriously at all as a foreign policy actor. Just not as seriously as the country with 100,000 troops stationed in the region and spending \$700,000 billion on its armed forces annually: the United States.

6. China's "New Silk Road": A Case Study in EU-China Relations

Wang Yiwei

In September 2013, China's President Xi Jinping made a visit to the Republic of Kazakhstan and gave a keynote speech at Nazarbaev University, titled "Promote Friendship between Our Peoples and Work Together to Create a Bright Future". In his speech, Xi pointed out that "to forge closer economic ties, deepen cooperation and expand space for development in the Eurasian region, we should take an innovative approach and join hands in building an 'economic belt along the Silk Road'. We may start with work in individual areas and link them up over time to cover the whole region". This was the first time the strategic conception of "Silk Road Economic Belt" had been proposed.

In October 2013, while attending the APEC (Asia Pacific Economic Co-operation) Economic Leaders Meeting, Xi remarked that the Southeast Asia region has served as an important hub for the "Maritime Silk Road" since ancient times, and that China is willing to strengthen maritime cooperation with The Association of Southeast Asian Nations (Asean) by making good use of the China-Asean Maritime Cooperation Fund set up by the Chinese government and establishing a sound maritime partnership for the purpose of jointly building the 21st Century "Maritime Silk Road"¹.

¹ "Jointly Writing a New Chapter of China-Indonesian Relations and Working Together to Create a Better Future of China-Asean Community of Common Destiny", *People's Daily*, 4 October 2013, 1st Edition.

The aim of this chapter is to present “One Belt One Road”, assessing its relevance for China-EU relationship providing Europe with a second opportunity with China.

6.1 What is “One Belt One Road”?

“Silk Road Economic Belt” and “Maritime Silk Road” constitute the new pattern of China’s all-round opening-up and new framework of China’s neighborhood diplomacy.

The two Silk Roads are, first of all, a transport network in the Eurasian area. It is a comprehensive network of transportation, consisting of railways, highways, air – and sea-ways, oil and gas pipelines, and transmission lines as well as communications networks. Services for these networks and important industrial clusters will gradually take shape along these traffic routes. Through industrial agglomeration and radiation effects, the construction industry, metallurgy, energy, finance, communications, logistics, tourism and the like will make up an integrated economic corridor. This transport network will link the Asia-Pacific area, the world’s economic engine, to the EU, altogether the world’s largest economy, creating new room for opportunities and leading to the formation of East Asia, West Asia and South Asia economic zones.

The proposal of two “Silk Roads” shows that China’s strategy of opening to the outside world has turned over a new leaf in history. Its major features are the following:

- **Content-wise:** from ‘bringing in’ to ‘going out’: a better combination of the two fosters new competitive edges of participating in and leading international economic cooperation, resulting in promoting reform through opening up.
- **Breadth-wise:** for the sake of development in China’s western area, westward and southward strategies are implemented to form a new pattern of all-round opening up.
- **Depth-wise:** Conforming to the global trend of regional economic integration and based on neighboring areas, free

trade zones are established to foster the free flow of goods, capital and labor.



Figure 6.1 - The map of "One Belt One Road" (*Xinhua* version)

To better facilitate trade and investment, deepen economic and technical cooperation and establish free trade zones, thus ultimately to formulate a large Eurasian market, constitutes the goal of constructing the two Silk Roads. China and the Silk Road nations will work to optimize the allocation of trade and production factors, promote regional economic integration and strive for synchronized economic and social development in the region.

The establishment of the Eurasian Continental FTA (Free Trade Area) or Eurasian big market will have significant impact on the current economic map of the world, promoting the formation of a new political and economic order.

6.2 Historical superiority of "One Belt One Road"

China is not the only country to propose the idea of building a new Silk Road. For example, Japan advocated Silk Road diplomacy in

1998 aiming at Central Asia; the United States proposed the “New Silk Road” aiming at South and Central Asia in 2011; India launched a “Mausam Project” designed to restore historical links with countries on the coasts of the Indian Ocean in 2014; Kazakhstan, Korea and many other countries had also presented similar plans. In comparison with these initiatives and programs mentioned above, the advantage and feature of China’s ‘One Belt One Road’ diplomacy is to promote the establishment of a development-oriented community of common destiny. On the one hand, China’s greatest edge in promoting the Maritime Silk Road lies not in China’s advantages in political, military, or geographical aspects, but in its close and cooperative relationship with the countries and regions along the route. On the other, the countries and regions along the line have strong desires to develop, intending to share China’s development dividends. In such a situation, China needs to give full play to its own advantages, not only regarding the Maritime Silk Road as a self-interest policy of promoting domestic industrial transfer and expanding overseas investment, but also treating the economic belt along the Maritime Silk Road and the Overland Silk Road as “a pair of wings to boost Asia’s economy”, thus promoting regional economic integration in depth. Moreover, compared with the political and security domain, when economic development is concerned it is easier to achieve a win-win situation without causing excessive strategic concerns. Specifically speaking, we can strengthen communication and coordination with the countries along the route with regard to their development planning so as to avoid blindly advancing projects in the manner of unrequited love, and bring the development aspirations of the countries along the route into the process of planning the Maritime Silk Road.

“One Belt One Road” emphasizes the principles of joint discussion, joint construction and sharing, and stresses the idea of openness and tolerance, mainly manifested in the following two aspects. Firstly, projects may be compatible with local existing co-operation frameworks, i.e. we try not to make a fresh start; secondly, extraterritorial powers such as Russia, the United States,

Europe and Japan shall be tolerated rather than excluded, so as to emphasize the public spirit of international cooperation and the attributes of public goods, making it not China's unilateral strategy. Indeed, "One Belt One Road" is literally practicing the idea that "China's dream is in common with the dream of the world's people to pursue a better life".² Sri Lanka's dream, Russia's revival dream, Indonesia's marine power dream, and the Mongolian dream are all interlinked with the Silk Road dream, fully turning Chinese opportunities into the world's opportunities and vice-versa. "One Belt One Road" will consolidate strategic cooperation partnerships with the countries and regions along the line, and lay solid foundations for a global partner network. For this purpose, China can propose the inclusive, open and sustainable "Silk Road Security Concept", release white papers about "One Belt One Road", and dispatch missions both at home and abroad to explain its intent and strategy as well as the benefits to be brought to local people. China can also stress the early contributions made by the United Nations Development Program (UNDP) and bring the "One Belt One Road" into the United Nations' Sustainable Development Agenda after 2015 to practice the 'Five-in-one' concept outlined in the report of the Eighteenth National People's Congress and to develop the 'five ways' of building "One Belt One Road", namely, policy communication, road interchange, unblocked trade, currency circulation, and shared understanding between peoples, into the "five communities", namely, a civilized community, a community with common interests, a community with shared responsibility, a security community, and a community with a common destiny.

The ancient Maritime and Overland Silk Roads used to be the "national roads" linking China with the East and the West, also seen as the bridge through which China, India, and Greece communicated their three leading cultures. Today, the Silk Road has revitalized, becoming an important strategic plan for China's reform and opening up to the outside world in the new era.

² 习近平奥巴马会晤“对接”中国梦与美国梦, 新华网, 2013年6月9日, <http://cpc.people.com.cn/pinglun/n/2013/0609/c241220-21802192.html>.

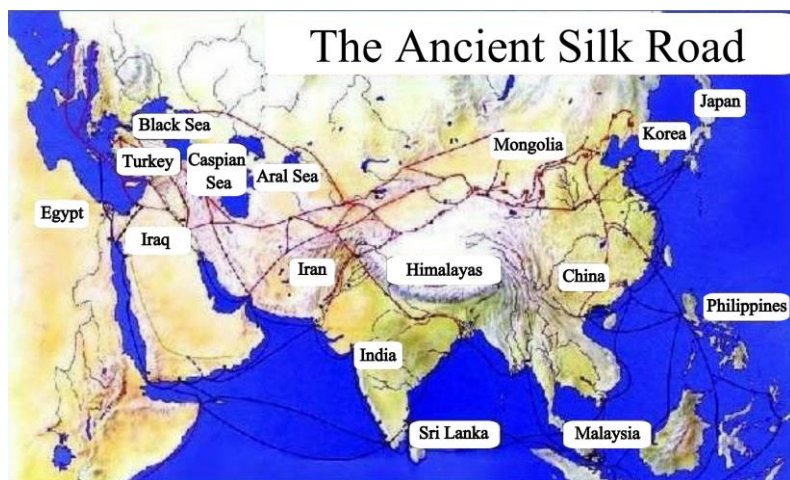


Figure 6.2 - The complete route map of ancient Silk Road

Along the “One Belt One Road” route, there are 65 countries from Central Asia, ASEAN, South Asia, Central and Eastern Europe, West Asia, and North Africa, home of 4.4 billion people with the disposable income of about 21 trillion dollars, accounting for 63 per cent (one belt) and 29 per cent (one road) of global capacity respectively. In 2013, China’s trade volume with the countries along the line exceeded \$1 trillion, making up one-fourth of China’s total foreign trade. Over the past 10 years, China’s trade with countries along the route has increased at the annual average rate of 19 per cent, which was 4 per cent higher than the annual average growth rate of foreign trade to China during the corresponding period. There is more room for growth in the future. The 13th Five-Year Plan is being devised, in which China is expected to import \$10 trillion worth of goods and invest more than \$500 billion abroad. Out-bound visitors are projected to be about 500 million. China’s neighboring countries as well as countries along the Silk Road will be the first to receive the benefits.

In summary, “One Belt One Road” is superior to the ancient Silk Road in three aspects:

- **Regionally speaking**, the current "One Belt One Road" reaches out to Moscow in the north, south Pacific countries in the south, Latin America in the east and Germany in the west, transcending the region of the ancient Silk Road.
- **Content-wise**, "One Belt One Road" no longer stands for a route for trading silk, tea, spices and chinaware, but represents interconnection in the 21st century. It links infrastructure, coordinates policies, promotes trade and commerce, circulates currency as well as connecting people's hearts and minds.
- **Significance-wise**, the Silk Road enabled Europeans to come to China and purchase silk, chinaware, spices and the like. China, in the eyes of the world, thus became the rich and mysterious place of *The Travels of Marco Polo*. In contrast, "One Belt One Road" is the fruit of China's all-around opening-up, actively signifying China's 'going out' policy. It would help shape a grand Eurasian market and a new pattern of globalization, thereby transcending the concepts of east-west trade channels and culture corridors.

In addition to its superiority over the ancient Silk Road, "One Belt One Road" surpasses similar strategies of other countries. Upon being proposed, "One Belt One Road" was dubbed "China's Marshall Plan"³. It is not surprising that people compare and contrast new things or ideas with those they know well, in memory or practice.

Following the Second World War, the United States put forward a plan to provide financial aid to Western European countries ravaged by the war and to participate in Europe's reconstruction. The United States also employed all sorts of forces to make sure these debtors dared not default. Such a plan created a

³ As early as January 5, 2009, the *New York Times* called China's 'going out' strategy the "Beijing Marshall Plan". After the strategy of "One Belt One Road" was proposed, the saying becomes even more popular, though "One Belt One Road" goes beyond the 'going out' strategy.

win-win situation for Europe and United States, under whose dominance the Bretton Woods System was soon established. The United States therefore ended up as the biggest beneficiary of the Marshall Plan.

Indeed, the “One Belt One Road” strategy and the Marshall Plan adopted by the United States to aid Western Europe are not without similarities. The impact in international opinion generated by the Marshall Plan as well as its vital role in enhancing America’s global image and influence are what China today wishes to achieve through “One Belt One Road”.

However, the similarities and differences between the “One Belt One Road” strategy and the Marshall Plan in terms of background, content, procedure and intent deserve closer attention:

Background: the Marshall Plan opened the prelude to the Cold War with a strong ideological tint. In other words, the Plan aimed at preventing the communist parties in Greece, Italy and other European countries from seizing power during the period of economic reconstruction and political chaos. In contrast, “One Belt One Road” carries no such background or ideology whatsoever. “One Belt One Road” originates from China, the engine of global economic growth, as Americanization and westernization lose ground, translates its own edges in production capacity, technology, capital, experience and model into advantages in market and cooperation. It is indeed the fruit of China’s all-around opening up.

Content: the Marshall Plan was officially named the European Recovery Program, an American initiative to provide economic support to the war-torn countries of Western Europe after the end of World War II to assist their reconstruction. Instead, “One Belt One Road” enables both China and countries along the Silk Road to share production capacity of high quality. The former was a one-way export, whereas the latter means jointly discussing investment projects, building infrastructure, and sharing the achievements of cooperation, e.g. the so-called ‘five-way’ connection comprised of smooth road interchange,

unblocked trade, currency circulation, policy communication, as well as connecting people's hearts and minds. That being said, "One Belt One Road" is planned to run a longer cycle and is much more comprehensive.

Procedure: the Marshall Plan was formally launched in July 1947, and lasted for four fiscal years. Throughout the period, Western European countries, by participating in the Organization for Economic Cooperation and Development (OECD), accepted a total of \$13 billion from the United States in various forms including but not limited to finance, technology and equipment. By comparison, the procedures taken by "One Belt One Road" stretch over a much longer term, which can basically be viewed as the extension of China's three-step development strategy. The interconnection network linking Europe, Asia and Africa will be gradually established by simultaneously carrying out such projects as economic corridors, industrial parks, and port construction from both onshore and offshore throughout Central Asia, the Middle East, Southeast Asia, South Asia and other routes.

Intention: the Marshall Plan was meant to assist Europe to recover its economy and to make it an important power and tool to contend with the Soviet Union, allowing the United States to dominate the European market more conveniently. When the Plan was put forward, the United States attached harsh political conditions and all pro-Soviet European countries were excluded. Even for the allied countries, the United States formulated standards and rules for all involved in the Plan, which the countries of Western Europe had no choice but to accept unconditionally. The Plan contributed to the split of Europe. Clearly showing America's strategic intent to intervene in Europe, the Plan shouldered the strategic mission of strengthening Europe to confront Soviet expansion, catalyzing the birth of NATO. "One Belt One Road" holds no strategic intent to control countries along the route – the vast geographical range as well as the large number of states involved make it impossible for any single country to dominate. Instead, it

aims to turn China's development opportunities into opportunities for the countries along the line, connecting the Chinese dream with the world dream. With emphasis on joint discussion, construction and sharing, "One Belt One Road" strives for the joint development of countries with different races, beliefs, and cultural backgrounds. Starting from interconnection and by advocating the establishment of a Silk Road Fund and Asian Infrastructure Investment Bank, "One Belt One Road" will provide more public goods for neighboring countries and regions. It stands for a new model of regional cooperation for South-South Cooperation.

6.3 Europe's second opportunity with China

In the 18th Century, a China fever swept across Europe. Even now, France still has the word *Chinoiserie*. The French Enlightenment leader Voltaire once wrote, "It is really a misfortune that we are not like the Chinese". German philosopher Leibniz, employing the 'Golden Apple' story in Greek mythology as metaphor, made his famous statement, "If a wise man is elected to decide which nation is the most prominent, rather than which goddess is most beautiful, then he will give the Golden Apple to the Chinese".

Today, Europe's opportunities with China once again return. When China proposed the plan of "One Belt One Road", the EU also announced the European New Silk Road Project, aiming to build a free trade zone from Lisbon to Vladivostok so that partners do not have to choose between Moscow and Brussels. This would make it possible for intercontinental cooperation between China and Europe to interlink. Both overland and maritime Silk Roads link Central Europe with Central Africa, and connect the Pacific Ocean, Indian Ocean, and Eastern Mediterranean, which would not only drive the joint rise of China and India and consolidate the rising momentum of Asia, but also create a more inclusive globalization. Because traditional globalization started from the sea, coastal areas were among the first to develop, whereas the interior has been less developed. A regional gap of wealth was

formed historically. "One Belt One Road" advocates and encourages opening to the West, and drives the development of western regions as well as Central Asia, Mongolia, and other landlocked countries, thereby implementing inclusive development philosophy.

In this way, Europe rediscovers China and the world. Transcending the West and discovering the world can be seen as Europe's second opportunity with China. In the era of globalization, China and Europe have again found each other and discovered the world, betokening a grand East-West integration.

To sum up, China's "One Belt One Road" offers seven great opportunities for Europe as follows:

First, it is an opportunity to build a greater Eurasian market and to revive European civilization: historically, the Eurasian continent has always been a center of world civilization, at least after the fall of Egyptian civilization. The two great civilizations of East and West were linked together through the historical Silk Road. It was not until the rise of Turkey's Ottoman Empire and the cut of the Silk Road by it (known as the "Ottoman wall") that Europe was forced to move towards the sea. Europe's movement to the sea had also benefited from the spread of China's great inventions such as the compass and gunpowder to Europe through Arabia. Europe's movement to the sea led to globalization via colonization and further resulted in the decline of the Silk Road, following which Eastern civilizations turned conservative and the world became Western-centered. Upon the rise of the United States, the center of the West shifted from Europe to America, and Europe soon declined, a decline unable to be reversed even through European integration. Today, Europe is faced with a historic opportunity to return to the center of the world, which may be called the revival of Eurasia. Halford Mackinder, a British expert in geopolitics, regards Eurasia as the 'world island', and believes that its integration will turn the United States back into an

‘isolated island’⁴ and allow Eurasia to return to the center of human civilization, thereby reshaping global geopolitics and landscape. The European interconnection plan, once linked with China’s “One Belt One Road” will enable ‘five-way’ connection in policy, trade, transportation, currency and people to mesh with China-Europe’s ‘four great partnerships’ of peace, growth, reform and civilization, allowing Eurasia to return to the center of human civilization while radiating to the African continent.

Secondly, it is an opportunity for Europe’s regional integration: for a long time, the European Union has not made a firm choice between “Eastern partnership” and “Mediterranean partnership” in terms of priority. Both have their respective problems in implementation. Now the Ukraine crisis is tearing Europe apart. It seems that in order to strengthen European integration, actions cannot be confined within Europe. Instead, even within Europe, there have got to be innovative ideas. The implementation of “One Belt One Road” turns Central and Eastern Europe into China’s new European portal; in particular, Poland, Greece, the Balkans, Hungary’s railway, the port of Piraeus have become competitive products in the “16 plus 1” cooperative projects as well as bridges to link overland and maritime Silk Roads. The inclusive development advocated by “One Belt One Road” can be seen as an opportunity for European integration, urging a dozen of Chinese provinces along the line, especially inland frontier provinces, to establish close economic partnerships and investment ties with European regions.

Thirdly, it is an opportunity for EU-Russian reconciliation: since the end of World War II and the establishment of NATO, “keeping Russia out” has been a clear strategic goal. The current Ukraine crisis is the very consequence of such a strategy. In fact, EU-Russian reconciliation lays the cornerstone of stability in Europe. “One Belt One Road”, going beyond the

⁴ Please refer to Z. Brzezinski, *The Grand Chessboard*, Basic Books, 1997.

Silk Road in ancient times, pays particular attention to containing Russia's development projects in the Far East, and to making organizations like the Eurasian Economic Union, Collective Security Organization of Commonwealth of Independent States and Shanghai Cooperation Organization compatible with each other via Moscow with the view to "keeping Russia in". German Chancellor Angela Merkel realized that, as we are unable to choose neighbors, we must interlink the Eurasian Economic Union with the EU as a wise choice to resolve the Ukraine crisis and seek for long-term peace and stability in Europe⁵. "One Belt One Road" opens up the opportunity for EU-Russian reconciliation.

Fourthly, it is an opportunity for the EU to participate more easily in Asia-Pacific Affairs. After the United States put forward the strategy of "returning to Asia", the EU expressed clear strategic anxiety about being marginalized. It then accelerated the promotion of FTA with Asian countries, yet with less than satisfactory progress. "One Belt One Road" allows Europe to interlink with Asia both by land and by sea, making it much easier for Europe to participate in Asia-Pacific Affairs, thus enhancing the EU's ability to seize the opportunity of Asia-Pacific development, and finally expand the EU's influence in the Asia-Pacific region.

Fifthly, it is an opportunity for the EU to enhance its global influence. As many of the countries along the route of "One Belt One Road" are Europe's former colonies, it is of vital importance to stress linkage with EU's peripheral strategy. These countries have the need to draw from European experience and practices in global and local governance. Under the framework of "One Belt One Road", there will be more opportunity for China and the EU to cooperatively develop and operate on third-party markets like West Africa, Indian Ocean and Central Asia countries and the like. Europe's experience,

⁵ "Merkel and Gabriel offer Russia free-trade agreement", *Die Welle*, January 23, 2015; "Merkel offers Russia trade talks olive branch", *Financial Times*, 26 November 2014.

standards, historical and cultural influence are valued by China. "One Belt One Road" upholds and promotes the spirit of the Silk Road, namely, solidarity, mutual trust, equality and mutual benefit, tolerance and learning from each other, and win-win cooperation. When the spirits of "One Belt One Road" are interlinked with the spirits of the EU and resonate with the normative power of the EU, China-Europe's global influence would be significantly upgraded.

Sixthly, it is an opportunity to transform and upgrade the China-EU comprehensive strategic partnership. China and the EU have enjoyed diplomatic relations for 40 years. During the past decade, since the establishment of the China-EU strategic partnership, China-EU relations have seen all-around, wide-ranging opportunities for cooperation, embodied in the Strategy and Plan of China-EU Cooperation 2020. Today, China and the EU are negotiating a Bilateral Investment Treaty (BIT). Both sides have even taken into consideration the feasibility of a China-EU FTA. "One Belt One Road" brings along greater dynamics, and the rail networks of Yu-Xin-Europe, (Chongqing-Xin Jiang-Europe) Zheng-Xin-Europe (Zheng-Xin Jiang-Europe) and Yi-Xin-Europe (Yiwu-Xin Jiang-Europe) increasingly interlink China and Europe together to jointly develop and further establish a new form of partnership with win-win cooperation.

Seventhly, it is an opportunity to balance the development of the trans-Atlantic relationship. Since the end of World War II, the EU has relied heavily on trans-Atlantic relations, but it has always found it hard to get out of an asymmetrical position in competition and cooperation with the United States. The hope of "speaking with one voice" has remained elusive and embarrassing. "One Belt One Road", in contrast, emphasizes openness and inclusiveness. In other words, it does not exclude any country, or seek any spheres of influence. Nor does it engage in any military expansion. It advocates to keep the US inclusive, which transcends the bilateral exclusivity of TTIP. In the process of implementation, "One Belt One Road" promotes

China-EU cooperation in preserving Silk Road safety, thus it may also contribute to scale-up the European position in the NATO, and ultimately help balance the development of trans-Atlantic relations.

6.4 Case study: Maritime cooperation with Central Europe

As the final stop of "One Belt One Road", Europe should feel happy about the project. The EU, however, is always slow. Coupled with the cancellation of the 17th China-EU leaders meeting, EU has not yet made a positive response. The situation should improve this year.

"One Belt One Road" consists of railways, highways and other form of infrastructure, as well as oil and gas pipelines, power grids, Internet networks, aviation routes, and so on. Being a diversified network, "One Belt One Road" is a key project to connect China with Europe and with the greater Eurasian market. In light of the fact that China and Europe enjoy extensive common ground in on naval issues and policy, EU-China maritime cooperation would become a new highlight in China-EU cooperation. In order to create four-dimensional cooperation as peaceful partners, growth partners, reform partners, and civilized partners, we should stress maritime cooperation. As for China-EU cooperation in maritime economic development, "One Belt One Road" also has important significance. China's strategy of "One Belt One Road" can be effectively integrated with the maritime strategies of the European Union as well as other countries in Europe. Greece, in particular, would become China's important gateway to Europe and a bridgehead in cooperation between China, Europe and Middle East. During the 3rd meeting of the leaders of the China-Middle East-Europe countries, China and the EU reached consensus to create a new channel for Asian-European sea-and-rail intermodal transportation built out of the Hungarian Railways and Greece's Piraeus port, proving once again that

Europe maintained a pivotal position in the construction of “One Belt One Road”

The great initiative of “One Belt One Road”, especially the 21st-century Maritime Silk Road, opens up a historic opportunity for maritime cooperation between China and Europe. Both share a wide range of similarities, common ground and mutual interests in maritime issues, policy and the maintenance of maritime security. Therefore, maritime cooperation would become a new highlight in China-EU cooperation. With marine development strategies of China and Europe linked with each other, China and the EU will make joint efforts to maintain the security of sea-ways. For instance, marine shipping and logistics centers need to be established, as shown in the anti-pirate action in Somalia. As shown in the port of Piraeus in Greece, the Strategy and Planning of China-Europe Cooperation 2020 should be put into practice. Once conditions mature, a Marine Cooperation Organization should be founded to commit to maintaining marine order and building a new version of Asia-Africa-Europe cooperation. Promoting bilateral and multilateral coordination, the complement of policies with concepts, along with effective control of differences, would prove a viable way for Sino-EU cooperation in the Maritime Silk Road.

Conclusions

The above analysis suggests that “One Belt One Road” is not a Chinese solo, but a symphony played by all countries along the route. It is, in particular, an ensemble of China and Europe joining hands in operating on the great Eurasian market.

The saying “those who have Europe have the world; those who get China get the world” vividly describes win-win cooperation between China and Europe. China-EU cooperation not only benefits people on both sides and helps them to achieve revival and rejuvenation; it also enhances potential for bilateral cooperation and world influence via joint development and operation of third-party markets, ultimately achieving regional integration and

globalized inclusive growth. Such are the shared expectations of both China and EU. Europe should grasp this second-round opportunity with China brought about by "One Belt One Road" so as to realize its own dream, one that is complementary to and reinforced by the Chinese dream.

Conclusions. Implications for the EU

This report analysed the first two years of Xi Jinping's rise to power in China. Xi's policy decisions and reforms are going to have a strong impact on what kind of economic and foreign policy actor the world's second biggest economy will be in the years ahead. In turn, this has relevant implications for EU's policies and policy attitudes towards China.

When defining the EU's policy responses to the ongoing major political and economic shifts in Beijing, it is worth noticing that Xi Jinping has made it clear over and over again he will pursue and adopt his domestic and foreign policies without any 'interference' from the outside. He will reserve the right to add the words 'Chinese-style' to Western terms and concepts such as 'democracy', 'freedom of speech', 'human rights', 'governance', etc. In particular, Xi Jinping's ruthless anti-corruption campaign and his determination to protect China from 'western values' resulted in a significant increase in the number of allegedly 'sensitive' issues on China's domestic and foreign policy agenda. Issues that foreigners are advised not to talk about, let alone criticize. Besides, Xi's determination to increase state control over the media and more importantly the Internet and his crusade against what he refers to as 'Western values' are arguably a sign of strength and an expression of Xi's ability to impose his policies on the Chinese society. Instead they seem more a sign of a deep-rooted sense of uncertainty between Xi and his close followers, who fear that their power base is far less secure than it might appear to the outside world.

By raising a number of issues in the conduct of Chinese domestic and foreign policy, this report draws key policy recommendations for the EU stance vis-à-vis China:

Shifting the spotlight from exchange rate misalignments to market access

As downward pressures on the Chinese economy are intensifying, Chinese President Xi Jinping announced that the country will have to switch focus from the speed to the quality of growth. This will have profound implications for Europe, a major trading partner for China, and the main origin of China's imports. More specifically, the composition of Chinese demand for goods will likely change rapidly to a more sophisticated consumption model. European producers of both consumption and capital goods will benefit from the new Chinese demand for high-quality goods. However, market access is still cumbersome in a number of sectors due to complex and numerous regulations. Consequently, EU trade policies towards China are likely to benefit from a strategic shift from raising issues of exchange rate misalignments – an argument which is invariably raised by the U.S. – towards market access improvement. Since the decision by the EU to open negotiations on a Bilateral Investment Treaty (BIT) in 2013, the EU has intensified its efforts to address problems related to market access in China in some sectors, as well as licensing and market access issues in the area of financial and telecommunication services. Given its overall trade surplus with Europe, the BIT is in the interest of China, which feels excluded from TTIP (Transatlantic Trade and Investment Partnership) and TPP (Trans-Pacific Partnership) and the EU's trade deals with its neighbours. However, by declaring its preference for an even broader free trade agreement, China may be trying to shift attention away from the requirements it needs to meet for the BIT. At the same time, the slowdown of economic growth and the impact of Xi's anti-corruption campaigns will likely have a negative impact on foreign as well as domestic firms, as the slowdown could be

accompanied by the adoption of stricter regulations for foreign invested enterprises. Therefore, continued efforts to increase dialogue on investment access and enforcement of intellectual property rights in China will contribute to balance out the impact on European firms investing and operating in the country.

Strengthening the “New Silk Road” through the Asian Investment Infrastructure Bank

As Europe is already today a major trade partner for China and a major destination for Chinese outbound direct investment (not considering those which are directed to tax havens), the strengthening of the Eurasian trade road through the development of the New Silk Road Economic Belt may contribute to further fostering trade and investment linkages between the two continents. The New Silk Road could help redirect the geopolitical center of gravity away from the US and back to Eurasia. In a sense, and quite optimistically, today's Europe may be faced with the historic opportunity to return to the center of the world, and this depends on the revival of Eurasia. In this perspective, Europe should consider contributing to strengthening Eurasian trade and investment, especially in terms of supporting new infrastructure building and other development projects. The very recent decision by the major European countries – France, Germany, Italy and the UK – to join the Asian Infrastructure Investment Bank (AIIB), a China-led development bank, goes in this direction and represents a major shift of European attitude towards Asia and China in particular, as it clearly departs from the U.S. position. Although this is mainly a geopolitical decision with potentially significant implications for other major Asian economies – such as South Korea, which might reconsider its decision to join the AIIB – important commercial considerations are going to play a role. The UK in particular hopes to become one of the main destinations for Chinese outbound investment (together with Germany, which already is a large recipient of Chinese FDIs). A bridge is progressively being built between China and Europe, which will

hopefully facilitate trade and investment policy dialogues, such as the ongoing EU-China negotiations for the Bilateral Investment Treaty.

Reducing the number of EU-China ‘sectoral dialogues’

The EU and China have established more than 50 EU-China ‘sectoral dialogues’ covering a wide range of areas and topics related to economic governance, trade, investment and industrial policies, environment etc. While the dialogues on economic and trade governance have produced mutually beneficial results, the ones covering issues related to Chinese domestic policy and inner-Chinese governance have not. In fact, as it turned out, the ‘sectoral dialogues’ have arguably not led to any measurable EU influence on inner-Chinese governance at all. Even if the political rhetoric might at times suggest otherwise, European influence on issues such as human rights, freedom of speech and expression and the rule of law will most likely continue to be absent. Indeed, the recent past has shown that Beijing continues to reserve itself the right to ‘cherry-pick’ domestic policy issues it allows others to criticize and to interrupt any kind of dialogue if outside ‘interference’ is considered excessive. Against the background of the lack of results, the EU should therefore consider whether or whether not to continue those ‘sectoral dialogues’. A reduction in the number of EU-China ‘sectoral dialogues’ could in turn enable both Brussels and Beijing to focus more efficiently on fewer issues on the bilateral agenda.

Making the “EU-China High Level Strategic Dialogue” result-oriented

The “EU-China 2020 Strategic Agenda for Cooperation” calls for “raising the level of EU-China dialogue and cooperation on defence and security, advancing towards more ‘practical cooperation’”. While this sounds good on paper, it remains yet to be seen how the “EU-China High Level Strategic Dialogue” will turn from

an informal dialogue to one able to formulate and adopt concrete EU-China security cooperation on the ground. So far, the EU-China strategic dialogue on Asian security is arguably more than anything else an annual window-dressing event as opposed to a dialogue that produces real results, let alone joint security policies. While EU policymakers typically point out that the dialogue's objective is not the adoption of joint policies but rather a platform to informally consult on Asian security issues, moving towards the above-mentioned 'practical cooperation' requires the dialogue to turn into more than an informal platform for discussions. However, in view of the Chinese principle of 'non-interference', it will continue to be very unlikely that the bilateral dialogue on security leads to concrete EU-China security cooperation on sensitive issues, such as the Taiwan and Tibet 'questions' as well as 'territorial integrity' in Asia's disputed territorial waters.

The EU and China should therefore identify areas and issues of security where dialogue could actually lead to 'practical cooperation' in Asia and beyond. Among others, these areas may include nuclear non-proliferation in North Korea and Iran, terrorism in the MENA region, Southeast Asia and Central Asia as well as joint confidence-building measures in East and Southeast Asia.

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