China’s Economic Outlook, Blinken in Vietnam, and the PRC’s Defense Posture

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TRANSCRIPT

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Wilson Shirley:

Hello and welcome back to the China Insider, a podcast from the China Center at Hudson Institute. It's Tuesday, April 18th, and we have three topics to go through today. The first is about China's grim economic reality as Q1 stats come out this week. The second is about Antony Blinken's recent visit to Vietnam and that country's role in countering China, and the third is about China's changing military posture, including new rules about military conscription and the Chinese defense minister's recent visit to Moscow. Miles, how are you doing?

Miles Yu:

Very good, Wilson.

Wilson Shirley:

So, Miles, our first topic today is the Chinese economy. There have been numbers coming in over the last couple of months. There are a couple of key economic data points that are coming out today, but I wanted to talk to you about some of the big questions that people are having about the Chinese economy after Q1 as it goes forward in the post-COVID zero era. So, can you give us a quick overview of where the Chinese economy is right now?

Miles Yu:

I think the Chinese economy, if not in total shambles, but is face severe challenges because reality is that the Chinese model of economy, particularly after COVID lockdowns is not working. I mean, I think you can see a lot of signs from the very top that the leadership is being spooked. On April 15th, for example, the Chinese Party's primary weekly magazine, Qiushi, published in an article, actually a speech that Xi Jinping gave back in January. He was talking about the one major theme that is how to stimulate what's called "domestic circulation." In other words, China is going to face this dire possibility of decoupling. In other words, Chinese economy would have to rely on its own domestic market. That means that the government doesn't really have any confidence in international investment. And so, just so happened that on the same day, the annual Spring Canton Fair opened.

This is one of the primary venues of international investment in China. This year, the situation is very grim. I mean virtually there's no major international corporation that goes to that fair. It's like 90% of the companies that showed up were actually domestic companies from China. On top of that, there were a lot of retail statistics that just came out last week. Over 70% of China's retail stores, major stores, lost dramatically in its profits. Some of them lost as much as 90%.

Wilson Shirley:

Wow.

Miles Yu:

So, this is just a really, really bad situation. Now, on top of that, many of China's major companies were facing international sanctions on account of human rights and Hong Kong regression, those things. For example, the world's leading surveillance electronic equipment maker, Hikvision, was sanctioned by the US government for its role in building up the
surveillance state all over China and particularly in Xinjiang. First-quarter profit dropped by 23% and that's a huge, huge drop.

So, all in all, Chinese economy is basically, you know, is in big trouble. At that Canton Fair, ¾ of the 40 foreign countries represented are from Belt and Road Initiative regions. Those are very poor, relatively poor countries. Western companies stayed away. And so, Xi Jinping in his article this week constantly talk about the problem of black swines and grey rhinos. Those are the Chinese Communist terms to designate major unforeseen catastrophic events. And that's black swine. Grey rhinos mean something that's already there, so obvious bad signs but are being ignored. So, this is something that really is at the bottom of Chinese economy because it is not doing very well.

Wilson Shirley:

And we've talked before on this podcast about problems with debt in China. We've talked about problems in the real estate sector. I saw some stats that investment in real estate was down 5.7% in January and February from a year ago. But I want to talk a little bit about the trends that you were speaking about. That is foreign companies that used to show up at events like this all the time but aren't anymore. So, we've seen a few stories over the last couple of weeks of tech companies like Apple looking to other parts of the world like India or Thailand to manufacture their products as they try to get supply chains out of China. So, as this trend continues, I think you talked about sort of domestic demand being how China is going to attempt to drive growth as this decoupling in certain sectors continues. How is that trend going to affect China's global posturing?

Miles Yu:

I don't know how many of you have recently visited Walmart and you can see there is substantial increase in products not made in China. You go to the clothing section, you go to the shoe section, you go to other furniture section even. That's because the supply chain has been, as you say, moved out of China. Not completely, but definitely, the trend is there. By the way, I have to say that decoupling has never been a state policy of either United States or any other country in Western Europe. It is happening anyway despite state policy and guidance. That's because every company has to look for one thing that is bottom line. And the bottom line tells you that in the investment environment like China, there is no policy consistency. There is no guarantee of property rights. There is a very severe control of currency. So, all the regulations were kind of, you know, ridiculous, and the Party is now infiltrating the economic operations of major corporations at every level. So, that's why decoupling is not a matter of policy, but a matter of reality.

Wilson Shirley:

And different countries talk about it in different ways. A couple weeks ago we talked about Ursula von der Leyen's speech. She didn't emphasize decoupling, she emphasized de-risking as kind of the European framework or the EU Commission's framework, which is an interesting way to talk about it. And I want to double down on this for a second though, Miles, because you talked about how decoupling, at least broadly speaking, has never been the explicit policy of Western governments. And a lot of people say that in fact, it's China that has been driving the
decoupling by driving towards this dual circulation model. Can you talk about what that means? Is China actually driving a lot of this decoupling itself and what is the strategy there?

Miles Yu:

I think that China benefits tremendously from engagement with the West. There's no question about that. But also, from the point of view of Chinese Communist Party, there's massive Chinese economic engagement with the West also poses a serious risk, that is if you have economic connection with the West, you would have to guarantee some degree of free flow of information because major corporations have to run on accurate economic data. And the truth and the free flow of information is something that would not be easily tolerated by the regime itself. So that's one problem. For example, major companies in China based out of US or Europe, they would have to use something called the VPN, right? VPN is a secure email communication and the Chinese government is very ambivalent about that. Right now, it has a national crackdown on VPN. That is, that's because you would also have to allow the Chinese nationals who are employed by these Western companies to use VPN to freely communicate and get information from outside. That's basically a political issue. So, it's not easy. So that's one reason why China has dramatically dialed up measures of decoupling on its own. When the United States government demanded that China opened its books of these companies listed in American capital markets like New York Stock Exchange for example, and just like anybody else, the Chinese government actually voluntarily withdrew some of the companies from the New York Stock Exchange.

Wilson Shirley:

And so, these were companies that Americans had invested in because they were on the New York Stock Exchange.

Miles Yu:

That's exactly right. It has a lot of American investors' money in there. So, once they get out the American capital market and China basically hopes that the risk of being audited by the Western market regulators will be mitigated. So, that's one of the reasons. So, there's a lot of political impetuses for China to facilitate decoupling. It's not what they really want for economic reason, but for political reason, they have to do that.

Wilson Shirley:

Yeah, so, I want to now pivot this conversation to one of the primary countries that Western companies are looking to move their supply chains towards, and that's Vietnam. So, the Secretary of State of the United States, Antony Blinken, was recently in Vietnam. He's finishing up a week-long trip that included a stop in Hanoi. He was there to mark the 10th anniversary of America's comprehensive partnership with Vietnam. And this is not the first high-level visit from the administration to Vietnam. Vice President Harris was there, Secretary of Defense Austin, the Trade Representative, USAID Administrator. So, Miles, what's your takeaway away from Antony Blinken's visit to Vietnam and why is Vietnam so important in America's strategy in the Indo-Pacific?

Miles Yu:
Well, Vietnam is the linchpin of resistance against Chinese aggression mostly because of history, because of geographic location, also because of the potential Vietnam as a check against Chinese aggression in not only East Asia but also most importantly in Southeast Asia. No country has been engaged in military confrontations with China on a massive scale so frequently as Vietnam. Vietnam since 1970s has fought at least 5 major battles with China on land and at sea, and including the all-out invasion of Vietnam by the Chinese in 1979. Therefore, Vietnam’s resolve to resist China's further aggression has been strongest in the region. Vietnam is also one of the most important countries in Southeast Asia. So, Vietnam's resolve to resist Chinese aggression actually would have a chain reaction and contagious impact upon the nations of ASEAN. So, that's very important. Secondly, Vietnam and the United States have resolved its unprecedented past, have become strategic partners.

The United States during Obama administration lifted all the existing arms embargo against Vietnam. So, Vietnam has purchased a lot of weapons from the United States. Vietnam has become a very strong partner with the US and some other countries that similarly threatened by China, particularly India and Japan. But there's also a very important angle here that people often ignore, that is Vietnam is Russia's strongest traditional ally in the region, in Asia, and Vietnamese as a result of the Cold War politics forged an alliance with the then Soviet Union. And Russia continues to be very friendly with Vietnam. As a matter of fact, one of the most important reasons that China invaded Vietnam in February 1979 was because 3 months before that, Vietnam and Soviet Union signed a mutual defense pact. And that's why, that's something China could not tolerate on top of the fact that Vietnamese Communists toppled China's puppet state in Cambodia, Khmer Rouge regime.

But for the West, for the sort of China perspective, there's one thing that's very unique about Vietnam. Vietnam and China are both communist countries and they are all the children of Marxism-Leninism, and the Vietnamese know the Chinese playbook more than anybody else. It knows its command structure, knows its traditional tactics, and knows its weapons. So, Vietnam knows how to deal with China better than anybody in the region. So, that's why Vietnam is strategically important, not only for the region but also for America’s global strategy. That's one reason why Secretary Blinken and you mentioned about all the other key members of this government have constantly going to Vietnam.

**Wilson Shirley:**

And this cooperation is taking on really tangible forms as well. So, while Blinken was there, he broke ground on a new embassy compound. He finalized the transfer of a 3rd Coast Guard cutter to Vietnam. And one of the most important issues that I think about in terms of Vietnam-PRC relations today is the South China Sea. So, China right now is claiming territory in the South China Sea that is Vietnamese territory as well. So, can you give us a quick overview of what's happening in the South China Sea today?

**Miles Yu:**

Well, China claim pretty much the entire South China Sea as its own and.

**Wilson Shirley:**

Through what they call the nine-dash line, right?
Miles Yu:
The nine-dash line is essentially, it is the 11-dash line, but then China gave Ho Chi Minh, doing Ho Chi Minh a favor. So, they cut off two of them, so it become nine when Ho Chi Minh was still alive. Probably, this is probably China's most outrageous claim. Really in violation of international law, the Permanent Court of Arbitration in the Hague ruled in 2016, China's claim in this area of sovereign rights had no basis. The Philippines.

Wilson Shirley:
Yeah, and that's the United Nations Convention on the Law of the Sea, right?

Miles Yu:
That's right. So, the Philippines basically is a very unique country because Philippines is a member of the ASEAN. On the other hand, Philippines is 1 of the 3 treaty allies of United States.

Wilson Shirley:
Yeah, and we just reached a basing agreement with them recently.

Miles Yu:
That's right. And Philippines is the closest to Taiwan in terms of operational soundness. Basing in the Philippines is going to be crucial. And that's exactly what's going on. The United States obviously has treaty obligation to defend the Philippines, and we have been granted basing rights in many of the key forward-deployed regions. And I think in recently we added 4 more and those were very close to Taiwan. So, in a scenario of Taiwan exigency, Philippines going to play a very important role. On top of that, and in the northern flank of the Taiwan scenario, you would have Japan to rely on. So, in other words, the United States is beefing up its readiness for any Taiwan contingencies. So, when president of United States says, “If China invades Taiwan, US will have military intervention,” he's not kidding. And we're getting ready for that.

Wilson Shirley:
Thanks for that, Miles, because you set us up perfectly for the 3rd topic of the conversation, which is the issue of defense. And I want to flip it to the other side to talk about China's military posturing because last week Beijing announced that it was revising its conscription policy saying that “if there's a war, it would conscript veterans and educated college students.” And China, it's my understanding, typically draws members of the PLA from the countryside. So, what's driving this change and why does it matter?

Miles Yu:
I mean, we have to look at China's policies from a historical perspective so that we don't easily get freaked out. First of all, China has the world's largest armed force. It has 2.3 million active-duty personnel. I don't think China really needs to big, to get bigger. As a matter of fact, one of the main, China's main problem consistently for decades is the overweight of its military personnel. So, try to trim it and year after year after year. So, I will not take really this kind of
drafting seriously. It is puffing and puffing and puffing and puffing, you know. There’s another reason why they do it because veterans of Chinese military have been one of the most destabilizing elements in Chinese society. They serve in the military and retire and then they’re out of jobs, many of them, and all there are sort of an inadequately compensated.

So, if you look at the groups of the protestors, one of the consistent groups were actually veterans, right? So, they showed up in uniform and they demand more treat, sort of welfare treatment. And this is one of the reasons why you have to really include them. This happened in modern Chinese history all the time. When Chiang Kai-shek unified China, you have a lot of veterans of the war, even during the Warlord Period, he had to organize them into some kind of fashion. This is a similar situation. After the Korean War, China faced something like 4 to 5 million military personnel size. They have to trim them. So, they have to deal with those people who are veterans. So, I think this is one of the reasons why they’re doing this, to what extent those soldiers and veterans can really handle modern warfare in a scenario over Taiwan Strait or beyond. And I am very doubtful.

Wilson Shirley:
Okay, so the second big issue on the defense front from China last week came with a visit to Moscow. So last week, Russian President Vladimir Putin and China’s Defense Minister, a man named Li Shangfu, a man who is sanctioned by the United States met in Moscow. And the two had a follow-up to the conversations that Xi Jinping and Putin had last month. So, let’s just elaborate a little bit more and drill down on the defense side of cooperation between China and Russia. What happened at that meeting, where they said that they were going to “deepen military mutual trust?”

Miles Yu:
General Li Shangfu’s visit to Moscow is a very interesting one because has rarely happened before. A defense minister visiting a foreign country without Xi Jinping grabbing all the spotlight, which is kind of very rare. So, therefore, there must be something very substantial to discuss between him and the Russians. However, I’m doubtful that there will be any substantial discussion about any joint military action either in Asia-Pacific or in Europe. I think that they’re going to discuss some of, to reconcile some of the Chinese promises, open or secrets, promises of supplying lethal weapons to Russia and what China actually is willing to do and in what fashion. So, those issues are not very easy. China has dug a diplomatic hole of its health, of itself and it basically promised the unlimited capacity of friendship with Russia. On the other hand, China also is severely hampered by what it can do without suffering wrath of the international community, particularly when it comes to warfare in Ukraine and in Taiwan. So, China knows very well everything that it takes in terms of defense and providing material assistance to Russia must be of severe consequences. I think Li’s visit to Moscow is dealing with those issue, ½ defense, ½ diplomacy.

Wilson Shirley:
Sure, and to your point, Ukraine, obviously what everyone’s talking about right now, but it wasn’t mentioned in either side’s official readout of the meeting, even though it certainly was discussed. So, I want to close out with one last question for you Miles, and it's something that I meant to ask you about in either last week's episode or the episode before, which was if you
could elaborate a little bit on the dynamics between Russia and China today. So, most of the
time I've seen Western analysts describe the dynamics as Russia being China's junior partner
or words to that effect. When you've been talking, you've discussed a little bit of leverage that
Russia has over China right now though. So, I don't know if I am understanding you correctly
there, but could you talk a little bit more about the power dynamics between these two
countries?

Miles Yu:
I think that Russia right now, obviously, is the bully of the world on kind of the war in Ukraine,
and looks like the world, the West is united in resisting Russia and Russia has become a pariah
state. That's reality number 1. Reality number 2 is that Russia's war in Ukraine has been a
disaster. So, it looks like you going to drag Russia down. If Russia for some reason either
collapsed or retreated or even defeated in Ukraine, the West would have all the energy united to
deal with China, which has been regarded as the systemic rivalry for Europeans and the
national security threat number 1 for the United States. So, China does not want to see that
happen. So, what China has been doing is that China wants to make sure that it will do
everything to make sure Russia does not collapse or Russia.

Wilson Shirley:
Including buying oil from it at discounted prices.

Miles Yu:
That's right. So, China wants to help Russia not to collapse, not to be defeated. So, but then
that also brings another dilemma, which we just talked a little bit earlier. So, it's in China's
interest to keep Russia emerging from the Ukraine War not defeated. I don't know what kind of
scenario that that's one of the reasons why China wants to propose this peace plan to give
Russia in face-saving exit, but Vladimir Putin right now is not necessarily in that mood. He does
not want to play junior partner of China. So, he still has a little bit of imperial pride in him. On the
other hand, and I think, you know, Russia also sincerely distrusted China's intention because
China wants to play both sides, right? So, China wants to play an active role in the
reconstruction of Ukraine and Russia is not really that happy. Russia also is not happy that
China has not been openly, openly at least rhetorically attack Ukraine yet. So, when you try to
play the middleman without any principle and without any credibility and you basically lose on
both sides.

Wilson Shirley:
Yeah, and we keep on waiting for that call between Zelensky and Xi Jinping, that still has not
happened even though it was reported on a couple of months ago as a possibility in the near
future. I think that's all that we have time for this week, Miles, thank you so much. Looking
forward to recording next week's episode with you.

Miles Yu:
Thank you, Wilson. I'm looking forward to next week too.
Wilson Shirley:
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