



Sigur Center for Asian Studies

THE GEORGE WASHINGTON UNIVERSITY

China at the Crossroads? Reform Challenges Ahead

China is at a series of junctures in its economic, social, political, environmental, and foreign policy realms. As the ruling party for over 60 years, the Chinese Communist Party (CCP) finds itself at a turning point, faced with numerous challenges on the road ahead. In a lecture entitled “[China at the Crossroads? Reform Challenges Ahead](#),” held at the Sigur Center for Asian Studies in April 2015, David Shambaugh, professor of political science and international affairs at the George Washington University, argued that diminishing returns have set in in a number of main areas of reform that China has enjoyed and benefited from over the last 35 years. These diminishing returns set in beginning around 2005 when the CCP started discussing a new wave of reforms. What are the issues the CCP faces in order to retain legitimacy? Ten reform challenges exist in China today, which, if not appropriately addressed, may cause the country to stagnate and lose momentum of growth.

Challenge 1: Economic Reforms

Perhaps the largest challenge, economic reforms in China encompass a wide array of issues. These include:

- *Stagnating Growth*—China faces a declining growth rate, down from the double-digit rates of several years past. While the CCP has defined a seven percent growth rate as the “new normal,” economists in and out of China believe that the growth rate in actuality is closer to 5-6 percent. This decline is a result of a number of factors, chiefly: property market bubble bursts in some cities, declining land sales, and the resulting declining tax revenues from lower land sales.

- *Macro Growth Model*- China needs to shift from the “old two”- domestic investments and exports- to the “new two” – domestic consumption and innovation- in order to move up the economic value chain and create a knowledge-based economy.
- *State Owned Enterprise (SOE) Reform*- The largest problem facing Chinese SOEs today is the monopoly these entities hold over various sectors of the economy. Introducing mixed ownership and competition is crucial to improve quality and foster innovation in these sectors.

Other economic reform challenges China will need to grapple with include reforming or relaxing its hukou laws to establish a national labor market, liberalizing the financial sector, and streamlining the Chinese regulatory system to address corruption. In the period since the Third Plenum, the CCP has made some progress on a number of these issues, but has encountered resistance in others.

Challenge 2: Fostering Innovation

If China hopes to achieve macro growth, it needs to address reform that encourages fostering innovation. While innovation has been seen in some sectors (namely, biotech and nanotech), the Chinese economy is still largely assembly and processing based. If it wants to move out of the “middle income trap,” China will need to innovate its way out. Those sectors that have seen the most progress in innovation have benefitted from top down R&D investment. In contrast, a bottom up approach to innovation necessitates that entrepreneurs and small businesses are able and willing to take risks and explore as they choose (without censorship or no-go zones). China’s education system needs to encourage this type of free thinking, but is ultimately subject to regulation by the political system. Innovation may also come from the outside in vis-à-vis external companies or individuals, but in order for innovation to take root via this route, China needs to provide a network linked globally with unfettered access to other countries and individuals.

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Challenge 3: Reducing Social Inequality and Instability

While many have prospered from China’s reforms, others have not felt the trickle down of wealth. Because university graduates do not hold the same opportunities as their predecessors, middle class aspirations are stagnating. Meanwhile, China’s wealthy have one foot out the door and are parking their personal assets,

children, relatives, and businesses abroad. This hedging type behavior demonstrates a lack of confidence in China's own system and future. Moreover, beyond the media's coverage of social unrest in Tibet, Xinjiang, and Hong Kong, China experiences 200,000 incidents of mass unrest per year.

Challenge 4: Aging

In upcoming years, the size of China's population age 60 and over will increase dramatically. The number of families with only one child underscores the challenge of the growing number of aging Chinese. This will in turn test the government's ability to offer benefits, healthcare, and social security.

Challenge 5: Corruption

Corruption is so systemic and endemic across the system that it has reached "epidemic proportions," according to Shambaugh. Serious efforts have been made in the current anti-corruption campaign, leading to investigations of a large number of officials. At the same time however, cadres in the system are fearful as a

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result of the campaign, freezing up their ability to conduct day-to-day work. The lack of grease on wheels—that is to say, corruption—is resulting in the system not functioning in the way it has in previous years. In order for the campaign to succeed, more attention needs to be given to the source of corruption within the Chinese system.

Challenge 6: Political and Legal Reforms

The Chinese political system cycles through periods of opening- or liberalization- and closing – or repression-, with typical openings lasting between five to seven years, and closings lasting two to three years. However, the current closing cycle is pushing seven years, and repression in China today is at its most severe point since the aftermath of the 1989 Tiananmen Square protests. The CCP has cracked down on Internet users, NGOs, social activists, ethnic groups, students, and across the board, revealing a profoundly insecure regime. The crackdown on Internet dissent, religion, ethnic unrest, and other activism greatly impedes the CCP's ability to make progress in the economic areas that it needs to focus on, and challenges the longevity of the Chinese system.

Challenge 7: Fostering Urbanization

The CCP's goal is to have 60% of the Chinese population living in urban areas by 2020. This requires moving 260 million rural inhabitants into urban areas, creating 110 million new jobs, and dealing with the 160 million migrants already living in urban areas. The push for urbanization places enormous pressure on municipal governments for all kinds of public goods, but if

successful, has the potential to stimulate consumer spending and create a new pool of labor.

Challenge 8: Improving the Environment

China faces a broad range of environmental problems including air pollution, deforestation, water pollution, and the resulting health implications of these issues. The CCP recognizes the importance of these problems and has released a series of anti-pollution measures since the Third Plenum. While these measures are a promising sign, the regulations are only as good as their implementation and enforcement.

Challenge 9: Improving China's Image and Soft Power

Since 2008, the CCP has invested a great deal of money into institutions and activities that operate abroad to build and improve China's international image. Polls show that China's global image is mixed (neither overwhelmingly positive nor negative). In order to build its global image, the Chinese government would do well to distinguish the difference between public diplomacy and soft power: public diplomacy is external propaganda at work, whereas soft power comes from a nation's society, culture, values, and political system. Soft power travels and has a magnetic effect; culture needs to have universal appeal. However, China does not possess a lot of universal appeal. The CCP spends a disproportionate amount of time telling the world how China is unique and different from the rest of the world, rather than discussing how China might generally appeal to others. Another problem in China's soft power campaign rests on the CCP's propensity to use slogans (such as "China Dream," "harmonious world," and "peaceful development", which are difficult for foreigners to understand and don't always necessarily match China's actions at home and abroad. Until China can understand soft power as distinct from external propaganda and public diplomacy, it will find building a positive international image challenging.

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Challenge 10: Managing Foreign Relations

Between 2007-2008 until 2011-2012, China faced a downturn

in foreign relations. However, its foreign relations have been on the uptake since 2014: relations with the United States have stabilized, and China conducted a series of highly successful trips in Europe last year. The confidence and proactivity that China displays in managing its foreign relations is in stark variance with the insecurity that China shows internally; this dichotomy remains a puzzle. Nonetheless, China's periphery still presents some ongoing territorial issues that strain its foreign policy. China will need to effectively address these issues by recognizing the problems and responding to them in a serious, pragmatic way.

Conclusion: China's Path Ahead

While the ten challenges discussed above are not insurmountable, they are unprecedentedly complex. The CCP's rule is at stake, and as Shambaugh argues, "the endgame has begun." While the current path China is following is reversible, the CCP undoubtedly needs to reform. Will the CCP's future be one of proactive and confident rule, or will it be reactive and insecure rule? Regardless of which path the CCP takes, it likely faces a rocky road ahead.

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