

SWALLOWING THE POISON FROG: IMPLICATIONS OF  
SINO-AMERICAN ECONOMIC STATECRAFT

A thesis presented to the Faculty of the U.S. Army  
Command and General Staff College in partial  
fulfillment of the requirements for the  
degree

MASTER OF MILITARY ART AND SCIENCE  
General Studies

by

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Fort Leavenworth, Kansas  
2022

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<b>REPORT DOCUMENTATION PAGE</b>			<i>Form Approved</i> <i>OMB No. 0704-0188</i>		
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<b>1. REPORT DATE (DD-MM-YYYY)</b> 10-06-2022		<b>2. REPORT TYPE</b> Master's Thesis		<b>3. DATES COVERED (From - To)</b> AUG 2021 – JUN 2022	
<b>4. TITLE AND SUBTITLE</b>  Swallowing the Poison Frog: Implications of Sino-American Economic Statecraft			<b>5a. CONTRACT NUMBER</b>		
			<b>5b. GRANT NUMBER</b>		
			<b>5c. PROGRAM ELEMENT NUMBER</b>		
<b>6. AUTHOR(S)</b>  MAJ Ryan J. Orsini			<b>5d. PROJECT NUMBER</b>		
			<b>5e. TASK NUMBER</b>		
			<b>5f. WORK UNIT NUMBER</b>		
<b>7. PERFORMING ORGANIZATION NAME(S) AND ADDRESS(ES)</b> U.S. Army Command and General Staff College ATTN: ATZL-SWD-GD Fort Leavenworth, KS 66027-2301			<b>8. PERFORMING ORG REPORT NUMBER</b>		
<b>9. SPONSORING / MONITORING AGENCY NAME(S) AND ADDRESS(ES)</b>			<b>10. SPONSOR/MONITOR'S ACRONYM(S)</b>		
			<b>11. SPONSOR/MONITOR'S REPORT NUMBER(S)</b>		
<b>12. DISTRIBUTION / AVAILABILITY STATEMENT</b> Approved for Public Release; Distribution is Unlimited					
<b>13. SUPPLEMENTARY NOTES</b>					
<b>14. ABSTRACT</b> China's economic rise challenges America's decades-long global preeminence with a rival conceptualization of economic ends, ways, and means. This study seeks to increase the contextual knowledge of the U.S.-Sino economic-security relationship. Based on a dataset of 193 countries between 2000 and 2018, this study econometrically evaluates the effects and determinants of 21st century Chinese economic statecraft, particularly bilateral debt financing. It finds that a ten percentage point increase in a state's Chinese debt stocks is associated with a two vote increase in a state's voting alignment with China in the UN General Assembly. This study then isolates state characteristics that predispose a country to Chinese economic influence, finding that the effect of Chinese economic statecraft is highly contingent to bilateral economic resiliencies and vulnerabilities. As a result, it proposes a bifurcated policy paradigm of selective economic denial and steady economic punishment to capitalize on the enduring but highly contextual impact of Chinese economic influence.					
<b>15. SUBJECT TERMS</b> Economic Statecraft, Geoeconomics, China					
<b>16. SECURITY CLASSIFICATION OF:</b>			<b>17. LIMITATION OF ABSTRACT</b>	<b>18. NUMBER OF PAGES</b>	<b>19a. NAME OF RESPONSIBLE PERSON</b>
<b>a. REPORT</b> (U)	<b>b. ABSTRACT</b> (U)	<b>c. THIS PAGE</b> (U)			<b>19b. PHONE NUMBER (include area code)</b>
			(U)	104	

MASTER OF MILITARY ART AND SCIENCE  
THESIS APPROVAL PAGE

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## ABSTRACT

SWALLOWING THE POISON FROG: IMPLICATIONS OF SINO-AMERICAN ECONOMIC STATECRAFT, by Ryan Orsini, 104 pages.

China's economic rise challenges America's decades-long global preeminence with a rival conceptualization of economic ends, ways, and means. This study seeks to increase the contextual knowledge of the U.S.-Sino economic-security relationship. Based on a dataset of 193 countries between 2000 and 2018, this study econometrically evaluates the effects and determinants of 21st century Chinese economic statecraft, particularly bilateral debt financing. It finds that a ten percentage point increase in a state's Chinese debt stocks is associated with a two vote increase in a state's voting alignment with China in the UN General Assembly. This study then isolates state characteristics that predispose a country to Chinese economic influence, finding that the effect of Chinese economic statecraft is highly contingent to bilateral economic resiliencies and vulnerabilities. As a result, it proposes a bifurcated policy paradigm of selective economic denial and steady economic punishment to capitalize on the enduring but highly contextual impact of Chinese economic influence.

## ACKNOWLEDGMENTS

To my wife, thank you for your unbridled support and belief in my personal mission. To those working to understand and inform U.S. policy, thank you for your objective expertise in the pursuit of a better peace.

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## ACRONYMS

AIIB	Asia Infrastructure Investment Bank
BRI	Belt and Road Initiative
CCP	Chinese Communist Party
IFDI	Inward Foreign Direct Investment
IFI	International Financial Institution
GDP	Gross Domestic Product
MDB	Multilateral Development Banks
OFDI	Outward Foreign Direct Investment
PBOC	People's Bank of China
PLA	People's Liberation Army
PRC	People's Republic of China
RDB	Regional Development Bank
RMB	Renminbi

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# CHAPTER 1

## INTRODUCTION

It is almost axiomatic in both the United States and China to use the phrase great power competition to define the international system.<sup>1</sup> However, the two sides understand this competition differently. The United States labels competition as a return—a set of incipient conditions that evolved beginning in the 2010s. However, Chinese thinkers conceive of competition as a constant—a continuous dynamic among states.<sup>2</sup> This is just one of many key dichotomies between U.S. and Chinese thought that will shape future outcomes of competition.<sup>3</sup>

History also shows that asymmetry of thought among potential adversaries can lead to strategic surprise.<sup>4</sup> This project dives into the heart of the economic asymmetry that defines the Sino-American relationship and attempts to use that discrepancy to improve U.S. policy outcomes. Specifically, this study seeks to increase the contextual

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<sup>1</sup> Graham Allison, *Destined for War: Can America and China Escape the Thucydides' Trap?* (New York: Houghton Mifflin Harcourt, 2017), xvi-xx.

<sup>2</sup> Thomas Wright, “The Return to Great-Power Rivalry Was Inevitable,” The Brookings Institution, September 12, 2018, <https://www.brookings.edu/opinions/the-return-to-great-power-rivalry-was-inevitable/>; Elbridge Colby and A. Wess Mitchell, “The Age of Great-Power Competition,” *Foreign Affairs* 99, no. 1 (January-February 2020): 118-130.

<sup>3</sup> Barry Watts and Andrew May, “Net Assessment After the Cold War,” in *Net Assessment and Military Strategy*, ed. Thomas Mahnken (New York: Cambria Press, 2020), 85-93.

<sup>4</sup> Mark Cancian, *Coping with Surprise in Great Power Competition* (Washington, DC: Center for Strategic and International Studies, February 2018), 30-37, <https://www.csis.org/analysis/coping-surprise-great-power-conflicts>.

knowledge of the U.S.-Sino economic-security relationship. It focuses on one aspect of the problem: Chinese financial statecraft. By examining the causes, effects, and mitigating factors of Chinese financial statecraft, this study aims to better inform a more effective and efficient U.S. strategy.

### Background

This chapter introduces the broad discrepancies in how the U.S. and China conceptualize economics for the purposes of national security, and in particular the existential ends and subordinated means of Chinese economics. It closes with a framework by which the United States can better understand their Chinese counterparts, by examining the variation in Chinese economic policy over time.

### China's Existential Ends

The first way Chinese and American security theory conceptualizes economics differently is the existentiality of economics toward desired ends. In the United States, economics is just one of several key sources of strength that when acted upon produce strategic effect.<sup>5</sup> As a result, Americans view wealth generation as a key means to soft and hard power influence. However, yearly variance in economic progress alters future

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<sup>5</sup> The Biden Administration's Interim National Security Strategic Guidance labels economics among other socio-political and security pillars as sources of strength that require continual nurturing. These factors, in turn, sustain a desirable international system and distribution of power. See U.S. President, *Interim National Security Strategic Guidance* (Washington, DC: The White House, March 2021), 9, <https://www.whitehouse.gov/wp-content/uploads/2021/03/NSC-1v2.pdf>.

political leadership but not the stability of the republic itself. Without an existential end state, U.S. economic interests often conflict with its national security priorities.<sup>6</sup>

In contrast, China views its economy as a decisive component to the development and stability required for its grand strategic end: national rejuvenation.<sup>7</sup> Referred to as the *China Dream*, this grand strategic goal envisions the resurgence of Chinese status and influence both domestically and internationally.<sup>8</sup> China assesses this rise as incompatible with the current political and military dominance of the U.S.-led international system. As a result, China leverages two mutually supporting pillars centered on economics.<sup>9</sup> First,

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<sup>6</sup> Hon. Steinberg describes this dilemma between American economic and security interests in the Sino-American relations. See James Steinberg, “What Went Wrong? U.S. China Relationships from Tiananmen to Trump,” *Texas National Security Review* 3, no. 1 (Winter 2019): 119-133; Gavin reviews this tension with respect to President Biden’s proposed foreign policy agenda. See Francis Gavin, “Economics and U.S. National Security,” *War on the Rocks*, June 29, 2021, <https://warontherocks.com/2021/06/economics-and-u-s-national-security>.

<sup>7</sup> Allison, *Destined for War*, 212.

<sup>8</sup> Economy presents the China Dream as the centerpiece of Chairman Xi’s vision. See Elizabeth Economy, *The Third Revolution: Xi Jinping and the New Chinese State* (New York: Oxford University Press, 2018), 2-5; Pu outlines the careful calibration of Chinese status seeking behavior, both to accrue influence and shirk responsibility, primary focused on domestic audience to advance economic and security interests. See Xiaoyu Pu, *Rebranding China: Contested Status Signaling in the Changing Global Order* (Stanford, CA: Stanford University Press, 2019), 99-103.

<sup>9</sup> Fewsmith argues that variation in Chinese foreign policy is driven by domestic government organization and domestic politics but increasingly broke from international norms as the CCP judged foreign diplomatic, security, economic, and societal pressures threatened Chinese core interests. See Joseph Fewsmith, *Rethinking Chinese Politics* (New York: Cambridge University Press, 2021), 177-182; Medeiros outlines the interrelationships of enduring Chinese policy priorities over time. See Evan Medeiros, “China’s International Behavior: Activism, Opportunism, and Diversification,” *Joint Forces Quarterly* 47, no. 4 (July 2007): 35. Or for Chinese objectives within their cultural worldview see Allison, *Destined for War*, 107-109.

China seeks economic development to grow the country's economic wealth and influence over time from a low-income to high-income country to counterbalance the political and economic weight of the U.S. and its allies. Under "Dual-Circulation," China seeks to utilize the synergistic effects of domestic and international consumption, investment, and trade to drive it to higher levels of national income.<sup>10</sup>

China's existential view of economics also centers on state stability. Stability refers both to the sovereign autonomy of the state and the centralized control of the Chinese Communist Party (CCP). Economic performance underlies the social contract of the CCP's legitimacy, promoting a vision of sustained societal benefit in exchange for centralized party control. It also generates the resources, in terms of both financial and political capital, to build critical capabilities such as a modernized military and burgeoning consumer market. In turn, these instruments simplify security problems and create economic opportunity over time.<sup>11</sup> Not only is Chinese economic policy intimately tied to state security interests, but it is also a central feature of overall strategy.<sup>12</sup>

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<sup>10</sup> Yifu and Wang argue Dual Circulation is primarily focused on facilitating a qualitative industrial leap necessary from middle income to high-income status. See Lin Justin Yifu and Xiabing Wang, "Dual Circulation: A New Structural Economics View of Development," *Journal of Chinese Economics and Business Studies* (August 2021): 1, <https://doi.org/10.1080/14765284.2021.1929793>.

<sup>11</sup> Both Fravel and Finklestein show the endogenous effects of Chinese economic and security gains, building over time to further goals of stability and development. See M. Taylor Fravel, *Active Defense: China's Military Strategy Since 1949* (Princeton, NJ: Princeton University Press, 2019), 276; See David Finklestein, "Breaking the Paradigm: Drivers behind the PLA's Current Period of Reform," in *Chairman Xi Remakes the PLA: Assessing Chinese Military Reforms*, ed. Phillip Saunders (Washington, DC: National Defense University Press, 2019), 47-54.

<sup>12</sup> Gompert, Cevallos, and Garafola argue that these twin pillars of stability and development, and the tight economic-security nexus apply to Chinese thinking in peace

## China's Subordinated Means

The second way U.S. and Chinese security theory views economics differently is the level of subordination of economic means to state control. In the United States, economic means are one component of a whole of government response that varies in the transition from peace to war.<sup>13</sup> While the U.S. government controls some aspects of its economy, particularly fiscal and monetary, the economic instrument of power associated with foreign influence is overwhelmingly executed by private profit-motivated firms and actors. U.S. economic intervention to coerce or deter is only a transient action before transitioning back to a more peaceful state defined by decentralized control.<sup>14</sup>

In contrast, China subordinates its economic means to higher degrees of state control. The Chinese see control as necessary given the nature of conflict between states. Unlike the United States, the Chinese see a continuous relationship between peace and war, where states use all available means in perpetual conflict.<sup>15</sup> In order to succeed in

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and war through the idea of “war control,” whereby military leaders must tailor conflict scope and scale of conflict in pursuit of these nonmilitary ends. See David Gompert, Astrid Cevallos, and Cristina Garafola, *War With China: Thinking Through the Unthinkable* (Santa Monica, CA: RAND Corporation, 2016), 14, [https://www.rand.org/pubs/research\\_reports/RR1140.html](https://www.rand.org/pubs/research_reports/RR1140.html).

<sup>13</sup> Office of the Chairman of the Joint Chiefs of Staff (CJCS), Joint Publication (JP) 3-0, *Joint Operations* (Washington, DC: Joint Chiefs of Staff, 2017), V-8, [https://www.jcs.mil/Portals/36/Documents/Doctrine/pubs/jp3\\_0ch1.pdf](https://www.jcs.mil/Portals/36/Documents/Doctrine/pubs/jp3_0ch1.pdf).

<sup>14</sup> David Baldwin, *Economic Statecraft*, 2nd ed. (Princeton, NJ: Princeton University Press: 2020), 385.

<sup>15</sup> This classic concept is known as “struggle.” Fravel notes that “...war is just the highest form of military struggle.” See Fravel, *Active Defense*, 67. Burke, et al. identify one core PLA operating concept as the notion that the “Combat space is shrinking, [the] war space is expanding” to reflect the expanded utilize of nonmilitary means. See Edmund Burke, Kristen Guinness, Cortex Cooper, and Mark Cozad, *People's Liberation*

perpetual conflict, states accrue and consolidate strategic position and advantage.<sup>16</sup> This calls for principles of manipulation, patience, indirect means, and extraction to influence adversaries.<sup>17</sup> As a result, China seeks to exploit the interrelationships between itself, its adversary, and the system or environment.<sup>18</sup>

Through this lens of conflict, China leverages a tremendous set of economic endowments. Its economy is largely mercantilist, harnessing market power to accrue additional wealth. Historic advantages of low labor cost, large consumer base, and strong licensing requirements attract high foreign export and investment demand, effectively subsidizing Chinese coffers and intellectual property development. Similarly, high savings rates, concentration of state-owned enterprises in strategic sectors, and strong capital controls enable China to surge investment to strategic domestic and international

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*Army Operational Concepts* (Santa Monica, CA: RAND Corporation, 2020), 13.  
[https://www.rand.org/pubs/research\\_reports/RRA394-1.html](https://www.rand.org/pubs/research_reports/RRA394-1.html).

<sup>16</sup> Known as Shi, this classic concept for strategic advantage dates back to the Warring States Period (475-221 BC), a time of Chinese internal struggle that has had an indelible impact on Chinese culture and strategy. See Henry Kissinger, *On China* (New York: Penguin Books, 2012), 7-13.

<sup>17</sup> Pillsbury shows the application of Shi in 20th and 21st century Chinese policy. See Michael Pillsbury, *The Hundred-Year Marathon: China's Secret Strategy to Replace America As the Global Superpower* (New York: St. Martin's Griffin, 2016), 35-51.

<sup>18</sup> Chinese military thought personifies the drive to cultivate and leverage strategic asymmetry, be it military or nonmilitary. "Three Warfares" leverages psychological war, opinion war, and legal war over an opponent. "Target-centric war" paralyzes adversary operating systems. "Intelligitization" leverages all available data, from terrain to society and economy, to optimize decision making through artificial intelligence and machine learning. Thomas identifies critical consistencies and deviations in military conceptual thought over last twenty years. See Timothy Thomas, *The Chinese Way of War: How Has It Changed?* (McLean, VA: Mitre, 2020), 42-51, <https://apps.dtic.mil/sti/pdfs/AD1114504.pdf>.

sectors.<sup>19</sup> In addition, China also increasingly uses geo-economics, or the use of state wealth to accrue influence. From its manipulation of Taiwanese politics to the isolation of the free Tibet movement, and retribution for COVID response, Chinese geo-economics exploits latent economic asymmetry to maximize policy outcome.<sup>20</sup>

### Opportunity in Chinese Economic Statecraft

Existential ends and subordinated means are two conceptual differences between the U.S. and China in the application of economics for national security. This variation presents an important prism to understand the determinants and vulnerabilities of Chinese economic tools. First, there is clear variation in the application of Chinese economic tools. As the CCP balances both stability and development, it appears trade-offs of short-run inefficiency for long-run ends occur.<sup>21</sup> Second, there is also mixed effectiveness. Today there is significant evidence of bandwagoning against Chinese policy, and various concerns over the country's future economic viability.<sup>22</sup> Given the core long-run

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<sup>19</sup> These are some critical resiliencies and asymmetries of the Chinese macroeconomic system. See Thomas Orlik, *China: The Bubble that Never Pops* (New York: Oxford University Press, 2020), 1-8.

<sup>20</sup> Blackwill and Harris anoint China as the international leader in geoeconomic endowment and use. See Robert Blackwill and Jennifer Harris, *War by Other Means: Geoeconomics and Statecraft* (Cambridge, MA: Harvard University Press, 2017), 93-151.

<sup>21</sup> Economy offers this behavior is not evidence of a lack of strategy, but rather tactical experimentation and an overwhelming will to achieve ends. See Economy, *The Third Revolution*, 15, 233.

<sup>22</sup> Yang and Liang review regional case studies of alleged extractive economic practices to differentiate Chinese tactics based on the target country. See Yi Edward Yang and Wei Liang, "Introduction to China's Economic Statecraft: Rising Influences, Mixed Results," *Journal of Chinese Political Science* 24, no. 1 (March 2019): 381-385, <https://doi.org/10.1007/s11366-019-09614-1>. Orlik explains long term Chinese viability

economic-security lens of Chinese strategy, this study proposes that variation in Chinese economic statecraft over time presents a key to best understand Chinese policy determinants and vulnerabilities.

### Problem Statement

The growing influence of U.S. liberalism over time has brought America into inevitable conflict with other actors in the international community seeking their own spheres of influence.<sup>23</sup> However, the U.S. now faces a novel task in its strategic competition with China. Never before in the modern era has the U.S. faced a country of similar economic stature and opposing economic theory. This economic contest challenges America's decades-long global economic preeminence, and holds at risk the beneficial access, growth, and influence the United States applied to domestic and geopolitical objectives over time. As a result, this study uses the following problem statement:

How does the United States contest modern Chinese economic statecraft, particularly China's sharp power financial tools, in order to maintain U.S. global economic hegemony?

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relies on economic reforms such as industrial transition, limited privatization of state-owned enterprises, consumption-based demand, and rightsizing the domestic debt-financing market. See Orlik, *China: The Bubble That Never Pops*, 202-203.

<sup>23</sup> This American hegemony is a condition of the international system and a function of the influence of U.S. liberalism. It contrasts with imperialism, where a state forces others into a desired sphere of influence. Robert Kagan argues it requires the U.S. to deliberately plan its statecraft around this inevitable conflict of influence. See Robert Kagan, "The Price of Hegemony: Can American Learn to Use its Power," *Foreign Affairs* 101, no. 3 (May/June 2022): 10-19.

### Purpose of the Study

This study seeks to increase the contextual knowledge of the U.S.-Sino economic-security relationship. It focuses on one aspect of the problem: Chinese financial statecraft. By examining the causes, effects, and mitigating factors of Chinese financial statecraft, this study aims to better inform a more effective and efficient U.S. strategy.

### Research Questions

This study focuses on the following primary and secondary research questions:

Primary Research Question: What are the effects of Chinese economic statecraft on U.S. partners and allies in the international system?

Secondary Research Question 1: What are the determinants of Chinese economic statecraft, particularly its sharp power financial statecraft?

Secondary Research Question 2: How does the U.S. utilize economic ways and means to better advance its interests vis-à-vis China during competition, and if necessary, during a pivot to crisis?

### Hypotheses

China uses a blend of domestic and international cues to formulate and adapt its economic statecraft. These cues will be specific not only to the resiliencies, vulnerabilities, and preferences of other countries, but also to the perceived costs and benefits of using various economic tools. This study's primary analytical focus is how China determines the objectives and allocation of financial outflows to influence the recipient countries toward its desired ends.

Ho: Increased use of Chinese financial statecraft leads to an increase in Chinese support by other states.

Both the countries China seeks to influence and the firms China leverages to implement its economic statecraft face various pressures that alter the effectiveness of state policy. Other countries have various grievances and incentives that push and pull them into China's orbit based off their domestic and international position. Similarly, despite the unprecedented level of control China retains over its economy due to its structure, size, and scale, Beijing is also constrained by factors influencing the will of firms that execute its economic policy. As a result, effective policy aligns the interests of public and private actors to foster bandwagoning and minimizes balancing in accordance with China's goals. This study theorizes that Chinese financial statecraft will effectively align these various push and pull factors of not only other countries, but also Chinese domestic actors with Beijing's interests.

#### Assumptions

This study makes two core assumptions about the nature of the PRC and its underlying economic data. First, the study assumes PRC control of the Chinese economy. In order for economic indicators to be a good proxy of sharp power economic policy, the PRC must have a reasonably high control over the entities of national and local government to align all state actors to economic goals, and the PRC must retain reasonably high control over domestic firms to align resources toward those goals. Second, the study assumes that the international reporting data used in the analytical methodology accurately reflects bilateral economic trends over time. While China is widely suspected of withholding or misreporting economic data, the study assumes that

any purposeful variation in the data is homogeneous across years and countries in the sample.

### Definition of Terms

Economic Statecraft, the use of economic instruments to promote and defend national interests, and to produce beneficial geopolitical and domestic results; and the effects of other nations' economic actions on a country's goals. This study will use economic statecraft and geo-economics interchangeably.<sup>24</sup>

Competition, a relationship between states with incompatible interests that is short of military conflict.<sup>25</sup>

Gray Zone War, a common set of tactics in the space between peace and war for the purposes of coercing another actor to alter the status quo but below a threshold that typically warrants direct military response.<sup>26</sup> Therefore, this study uses competition to describe a particular strategic relationship between states and gray zone as a common set of tactics used within that part of the conflict spectrum.

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<sup>24</sup> This adapts the definition of Blackwill and Harris, 2016. See Blackwill and Harris, *War By Other Means*.

<sup>25</sup> This adapts the definitions of the U.S. military. See Office of the Chairman of the Joint Chiefs of Staff (CJCS), *Joint Concept for Integrated Campaigning* (Washington, DC: Joint Chiefs of Staff, 2018), [https://www.jcs.mil/Portals/36/Documents/Doctrine/concepts/joint\\_concept\\_integrated\\_campaign.pdf?ver=2018-03-28-102833-257#:~:text=The%20JCIC%20defines%20integrated%20campaigning,and%20duration%20across%20multiple%20domains](https://www.jcs.mil/Portals/36/Documents/Doctrine/concepts/joint_concept_integrated_campaign.pdf?ver=2018-03-28-102833-257#:~:text=The%20JCIC%20defines%20integrated%20campaigning,and%20duration%20across%20multiple%20domains).

<sup>26</sup> This adapts the definition of Morris et al, 2019. See Lyle Morris, Michael Mazarr, Jeffrey Hornung, Stephanie Pezard, Anika Binnendijk, and Marta Keep, *Gaining Competitive Advantage in the Gray Zone* (Washington, DC: RAND Corporation, 2019), [https://www.rand.org/pubs/research\\_reports/RR2942.html](https://www.rand.org/pubs/research_reports/RR2942.html).

Foreign Direct Investment. a category of cross-border investment in which an investor resident in one country establishes a lasting interest and a significant degree of influence over an enterprise resident in another economy.<sup>27</sup>

Sharp Power. a method of leveraging state resources for influence by attempting to piece or penetrate the political, information, or economic environment of a target state in order to undermine a target country's institutions, legitimacy, and decision making. This is opposed to soft power and hard power, which typically seek influence through attraction and coercion, respectively.<sup>28</sup>

Belt and Road Initiative. a broad program of bilateral trade, finance, and investment by the People's Republic of China.

### Scope

China uses a blend of soft, sharp, and hard power policy instruments in pursuit of their goals. However, while this paper attempts to control for all types of economic tools, it will be principally focused on sharp power, and specifically the financial tools by which China attempts to manipulate the system of its FDI outflow recipients.

### Limitations and Delimitations

This study suffers from several key constraints. First, any inferential power is ultimately limited by the immeasurable nature of state coercion and deterrence—both of

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<sup>27</sup> Organisation for Economic Cooperation and Development (OECD), “Foreign Direct Investment,” OECDiLibrary, accessed October 27, 2021, <https://doi.org/10.1787/9a523b18-en>.

<sup>28</sup> This adapts the definition of Walker, 2018. See Christopher Walker, “What is Sharp Power,” *Journal of Democracy* 29, no. 3 (July): 9-23.

which are truly multifaceted phenomena. As a result, any conclusions are not generalizable to other state dyads, or to relatively more overt forms of policy tools such as trade or aid. Another key limitation comes from the nature of the data and estimation techniques. By modeling based on Chinese economic theory, the study suffers from reduced sample size, both in terms of total country-year observations and reduced country cluster. This study relies on yearly dyadic data and fixed effects estimation, common practices in the macroeconomic literature, and as a result loses key granularity be it by economic sector, technological change, and policy change over time.

Two delimitations also constrain this project. First, due to the restricted research period, this study focuses primarily on financial statecraft, just one subset of economic statecraft. Time constraints also delimit the project's scope to the post 1978-era of Sino-American economic relations following the so-called Chinese Reform and Opening Period.

### Significance of the Study

Now more than ever, the U.S. must reassess the underlying assumptions of its economic and security strategies vis-à-vis China. This study fills a gap in the body of knowledge by examining the quantitative determinants and effects of Chinese sharp power economic statecraft within the Sino-American strategic competition. While limited in its scope, this study uniquely contributes to that reassessment as a component of a larger center of gravity analysis on the Chinese economy. Sharp power-based financial statecraft, such as bilateral Foreign Direct Investment or debt stocks, are just critical requirements toward Chinese objectives with its own set of vulnerabilities and resiliencies. Chinese economic statecraft represents an asymmetric benefit over the

United States where the PRC gains strategic benefit below the threshold of armed conflict, and quite possibly, leverage irreparable and unforeseen damage during conflict. As a result, legacy theories of both the American way of pursuing economic prosperity and the American way of war might require reassessment.

### Summary

Locked into a struggle for influence with China for the foreseeable future, America's most important task in these early years is to analyze and understand.<sup>29</sup> While China's asymmetric ability vis-à-vis the United States to mobilize nonmilitary means into foreign policy is challenging, so too is the gap in strategic culture, modes of thinking, and increasingly, basic policy preferences and tactical actions.

Given the decisive nature of Chinese economic instruments in this new game, this project seeks to understand the determinants and effects of Chinese financial statecraft. The following section explores the body of knowledge on economic statecraft and Chinese actions in the international system.

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<sup>29</sup> Graham Allison, Robert Blackwill, and Ali Wyne, *Lee Kwan Yew: The Grand Master's Insights on China, the United States, and the World* (Cambridge, MA: MIT Press, 2020), 37-49.

## CHAPTER 2

### LITERATURE REVIEW

#### Introduction

In addition to broad strategic differences in how apply economics to national security, China and the United States also vary in the application of various economics ways and means over time. This literature review explores the existing field of study of the Sino-American competition, defining the various methodologies, endowments, and pressures during China's economic rise and their effect on the international system.

This review has four sections. The first section explores Chinese economic statecraft traditions, beginning with a short history from the Great Opening in 1978 to the economic endowments of modern China. The second section reviews various tools of China's financial statecraft: the state-owned enterprise, foreign direct investment, regulatory control, and alternative finance. The third section reviews the modern economic competition between China and the U.S. since 2017, including various domestic and international pressures that shape modern Chinese economic statecraft. The final section reviews key trends that will inform the study's methodology and analysis.

#### Chinese Economic Traditions (1978-2016)

##### Chinese Economic Statecraft (1978-2016)

Chinese economic evolution since 1978 is a story of balance between party goals, social cohesion, and development opportunity. In December 1978 at the Third Plenum of the 11st Central Committee, Deng Xiaoping, then General Secretary of the CCP, issued the first guidance of what became known colloquially as "Reform and Opening." The

results changed the world. Deng's policies ushered in a new era for the Chinese people of limited economic opening to foreign markets, effectively ending Maoist-era economic autarky. Kissinger argues it also ushered in a new dilemma for the party, forcing it to balance the sustainability and requirements of economy and society.<sup>30</sup> On one hand, Pillsbury argues the need for western-based science, technology, and capital for economic and military development drove rapid opening.<sup>31</sup> On the other hand, Orlik shows China paid a steep price for the rapid trade and investment inflows during the 1980s in terms of inflation, debt, and corruption. Unchecked economic reform and growth exposed China to undue social risk. As a result, China adopted so-called "soft-landing" practices, limit market access, and manage the rate of economic growth.<sup>32</sup> Baum identifies five cycles of *fang* (letting go) and *shou* (tightening up) during the 1980s alone as diverse political coalitions in the CCP competed for influence and the future of the Chinese economy.<sup>33</sup>

Three influential years, from 1989-1991, marked the next inflection point in modern China's economic evolution. Doshi finds that the Tiananmen Square crisis, the Gulf War, and the Soviet Union collapse exposed Chinese reliance and vulnerability to U.S.-led technological and capital investment. Going forward, Chinese economic ways

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<sup>30</sup> Kissinger, *On China*, 335.

<sup>31</sup> Michael Pillsbury, *The Hundred-Year Marathon: China's Secret Strategy to Replace America As the Global Superpower* (New York: St. Martin's Griffin, 2016), 69-79.

<sup>32</sup> Orlik, *China: The Bubble That Never Pops*, 52-56.

<sup>33</sup> Richard Baum, *Burying Mao: Chinese Politics in the Age of Deng Xiaoping* (Princeton, NJ: Princeton University Press, 1994), 6-7.

and means sought to preserve western market access through bilateral and multi-lateral action, both to avoid U.S. economic coercion and constrain U.S. freedom of action in regional or international bodies.<sup>34</sup> Deng Xiaoping’s 1990 maxim “Hide (your capabilities) and Bide (your time)” encapsulated this behavior and set forth years of growth based on foreign exports and investment through seemingly mutually beneficial economic cooperation.<sup>35</sup>

China’s gradualist approach to economic reform continued through the 1990s. Lardy argues reform of the era focused on rapid productivity gains and factor accumulation rather than more costly sociopolitical endeavors such as major SOE or banking transformation.<sup>36</sup> Ang argues that ultimately this process of coadoption between managed Chinese markets and weak government institutions during these years allowed the country to graduate to middle-income status.<sup>37</sup> Both Lardy and Sharma

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<sup>34</sup> Rush Doshi cites concern over expanding U.S. use of Section 301 trade investigations and sanctions to interfere with bilateral Most Favored Nation (MFN) status that would cripple China’s development goals. It actively worked within regional bodies such as the Asia-Pacific Economic Cooperation, Association of Southeast Nations, and the World Trade Organization to constrain U.S. actions. See Rush Doshi, *The Long Game: China’s Grand Strategy to Displace American Order* (New York: Oxford University Press, 2021), 47-66, 139-141.

<sup>35</sup> Zhao Xiaochun, “In Pursuit of a Shared Future: China’s Global Activism in Perspective,” *China Quarterly of International Strategic Studies* 4, no. 1 (2018): 29-30, <https://doi.org/10.1142/S2377740018500082>.

<sup>36</sup> China’s modern issues with public debt, particularly in the state-owned sector, and banking sector insolvency arguably begin in this era as a deliberate trade-off for short run social and political stability. See Nicholas Lardy, *China’s Unfinished Economic Revolution* (Washington, DC: Brookings Institution Press, 1998), 3-20.

<sup>37</sup> Yuen Yuen Ang, *How China Escaped the Poverty Trap* (Ithaca: Cornell University Press, 2016), 11-17.

find China's limited exposure to the global economy during the decade helped mitigate the effects of the Asian Financial Crisis.<sup>38</sup>

Partial liberalization accelerated in the 2000s under the so-called "Go Out" policy. China secured World Trade Organization membership and Permanent Normal Trading Relations with the U.S. along with limited domestic banking and SOE reform to fill Beijing's coffers with foreign reserves. Miller and Li both argue these actions maximized the FDI inflows and outflows so critical to China's growth.<sup>39</sup>

China faced another inflection point to balance economic and societal requirements in 2008 following the Global Financial Crisis. Tooze, Naughton, and Doshi all present an increasingly interventionist China, motivated both to seize global influence vacuum generated by U.S. financial troubles and bolster slowing domestic growth.<sup>40</sup> During this window China established policy and procedures such as the Belt and Road Initiative (BRI), Asia Infrastructure Investment Bank (AIIB), and Made in China 2025. This transition coincides with a conversion to more overtly offensive economic ways and

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<sup>38</sup> Nicholas Lardy, "The Case of China," in *Financial Liberalization and the Economic Crisis in Asia*, ed. Chung Lee (New York: Routledge, 2003), 150-170; Shalendra Sharma, "Why China Survived the Asian Financial Crisis?" *Brazilian Journal of Political Economy* 22, no. 2 (April-June 2002): 225-252, <https://doi.org/10.1590/0101-31572002-1235>.

<sup>39</sup> Xiaojun Li, "Regulating China's Inward FDI," in *To Get Rich is Glorious: Challenges Facing China's Economic Reform and Opening at Forty*, ed. Jacques deLisle and Avery Goldstein (Washington, DC: Brookings Institution Press, 2019), 203-232; Tom Miller, "Great Leap Outward: Chinese ODI and the Belt and Road Initiative," in *To Get Rich is Glorious*, 233-260.

<sup>40</sup> Adam Tooze, *Crashed: How a Decade of Financial Crisis Changed the World* (New York: Viking, 2018), 239-254; Barry Naughton, "China's Domestic Economy: From Enlivening to Steerage," in *To Get Rich is Glorious*, 29-54; Doshi, *The Long Game*, 159-160.

means. Reilly, Norris, and Blackwill, and Harris all note an increase in Chinese coercive bilateral trade and investment practices from Taiwan to Norway.<sup>41</sup>

### Chinese Economic Endowments

An increasing body of research examines the frameworks by which China mobilizes economic means into geopolitical or geo-economic outcomes. Blackwill and Harris use an international frame to describe four leading geo-economic endowments: the ability to control outbound investment, domestic market features, influence over energy flows, and centrality to the global financial system.<sup>42</sup> Norris takes a firm-level view. He proposes Chinese state control over commercial actors generates variance in economic outcome due to state-level bureaucratic unity, state-firm goal compatibility, commercial market structure, and resource-reporting relationships.<sup>43</sup> Doshi focuses on recipient

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<sup>41</sup> William Norris, *Chinese Economic Statecraft: Commercial Actors, Grand Strategy, and State Control* (London: Cornell University Press, 2016); Blackwill and Harris, *War By Other Means*, 93-128; James Reilly, “China’s Economic Statecraft: Turning Wealth into Power,” (Lowy Institute for International Policy, Sydney, Australia, November 2013), [https://www.lowyinstitute.org/publications/chinas-economic-statecraft-turning-wealth-power#:~:text=China%20today%20is%20using%20economic,economic%20statecraft%20has%20been%](https://www.lowyinstitute.org/publications/chinas-economic-statecraft-turning-wealth-power#:~:text=China%20today%20is%20using%20economic,economic%20statecraft%20has%20been%20)

<sup>42</sup> Blackwill and Harris argue control over outbound investment and domestic market features drive Chinese geoeconomic strength, and influence over energy and international financial markets describes Chinese future goals. See Blackwill and Harris, *War By Other Means*, 87-91.

<sup>43</sup> Using bilateral case studies of geoeconomic interaction, Norris argues that a perfect set of conditions for state control of firm-level actors is state-commercial unity of purpose, oligopoly market structure, and a state-driven resource and reporting structure. See Norris, *Chinese Economic Statecraft*, 26-43.

impacts noting Chinese economic leverage is principally relational, structural, and domestic in nature.<sup>44</sup>

As a result of these broad endowments, China can vary its methods to align the interests of the government and economic actors that both deliver and receive its economic means. Aggarwal and Reddie find Chinese industrial and regulatory policies enable it to vary the state and market forces it utilizes, often by the income status of the target country, to avert international attention based on the political context.<sup>45</sup> Yang and Liang identify that China varies its economic statecraft by recipient national income status, with trade, aid, and FDI going to developing countries and FDI and mergers and acquisitions in developed nations.<sup>46</sup>

In addition, economic endowments allow China to vary its public and private diplomacy by target audience. Custer et al. find infrastructure investment drives Beijing's financial diplomacy, and often occur in conjunction with elite political visits.<sup>47</sup> Publicly,

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<sup>44</sup> Relational leverage manipulates bilateral interdependency. Structural leverage manipulates international systems and frameworks. Finally, domestic leverages reshapes a target country's politics and preferences. See Doshi, *The Long Game*, 136.

<sup>45</sup> Aggarwal and Reddie suggest technological improvements are changing the way firms and governments establish effective economic statecraft, in particular industrial and regulatory policy. See Vinod Aggarwal and Andrew Reddie, "New Economic Statecraft: Industrial Policy in an Era of Strategic Competition," *Issues & Studies: A Social Science Quarterly on China, Taiwan, and East Asian Affairs* 56, no. 2 (June 2020): 7, <https://doi.org/10.1142/S1013251120400068>.

<sup>46</sup> Yang and Liang, "Introduction to China's Economic Statecraft," 383-384.

<sup>47</sup> Samantha Custer, Brooke Russell, Matthew DiLorenzo, Mengfan Cheng, Siddhartha Ghose, Harsh Desai, Jacob Sims and Jennifer Turner, *Ties That Bind: Quantifying China's Public Diplomacy and Its Good Neighbor Effect* (Williamsburg, VA: AidData, College of William & Mary, 2018), 7-20, <https://www.aiddata.org/publications/ties-that-bind>.

China can tout the positive externalities of its economic relations. For instance, Bluhm et al., Miao et al., and van der Kley find lower spatial inequality through connective finance, growth in recipient domestic investment markets, and stabilized regional labor markets, respectively.<sup>48</sup> Privately, Isaksson et al. show that Beijing can promote its ability to sideline trade unions or provide target elites with corrupt kickbacks.<sup>49</sup> In this process, Kern and Reinberg argue countries turn to China for a range of requirements from financial resources to elite kickbacks.<sup>50</sup>

### Chinese Financial Statecraft Toolkit

#### State-Owned Enterprises (SOE)

Among Chinese endowments, several tools of financial statecraft stand out in the literature. First, the state-owned enterprise allows Beijing to mass economic means and

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<sup>48</sup> Richard Bluhm, Axel Dreher, Andreas Fuchs, Bradley Parks, Austin Strange, and Michael Tierney, “Connective Financing: Chinese Infrastructure Projects and the Diffusion of Economic Activity in Developing Countries,” (Working Paper 64, AidData, College of William and Mary, September 2018), [http://docs.aiddata.org/ad4/pdfs/WPS64\\_Connective\\_Financing\\_Chinese\\_Infrastructure\\_Projects\\_and\\_the\\_Diffusion\\_of\\_Economic\\_Activity\\_in\\_Developing\\_Countries.pdf](http://docs.aiddata.org/ad4/pdfs/WPS64_Connective_Financing_Chinese_Infrastructure_Projects_and_the_Diffusion_of_Economic_Activity_in_Developing_Countries.pdf); Miao Miao, Dinkneh Borojo, Jiang Yushi, Tigist Desalegn, “The Impacts of Chinese FDI on Domestic Investment and Economic Growth for Africa,” *Cogent Business and Management* 8, no. 1 (2021), <https://doi.org/10.1080/23311975.2021.1886472>; Dirk van der Kley, “Chinese Companies’ Localization in Kyrgyzstan and Tajikistan,” *Problems of Post-Communism* 67, no. 3 (2020): 241-250, <https://doi.org/10.1080/10758216.2020.1755314>.

<sup>49</sup> Ann-Sofie Isaksson and Andreas Kotsadam, “Racing to the Bottom? Chinese Development Projects and Trade Union Involvement in Africa,” *World Development* 106 (June 2018): 284-298, <https://doi.org/10.1016/j.worlddev.2018.02.003>; Ann-Sofie Isaksson and Andreas Kotsadam, “Chinese Aid and Local Corruption,” *Journal of Public Economics* 159 (March 2018): 146-159, <https://doi.org/10.1016/j.jpubeco.2018.01.002>.

<sup>50</sup> Andreas Kern and Bernhard Reinsberg, “The Political Economy of Chinese Debt and IMF Conditionality,” (Paper, SSRN, October 27, 2021), 7-8, [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3951586](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3951586).

spread economic risk. On one hand, China presents many of the negative externalities of heavy SOE-reliance including overcapacity, corruption, and crowding-out of private finance.<sup>51</sup> As Borensztein and Ostry show, China also had a history of productivity increases during its era of macroeconomic liberalization.<sup>52</sup> As a result, it is popular in Western circles to pin China's stunted economic liberalization to Chairman Xi's tenure.<sup>53</sup> However, Mattlin finds the CCP pivot back toward large public ownership began as early as 2006 as a deliberate party decision based on the accrual and reinvestment of massed corporate profits, weak domestic investment markets, and strategic security imperatives.<sup>54</sup>

Many researchers have attempted to understand China's SOE-led development success. Irwin and Gallagher find that China innovated based on the experiences of other Asian Tiger national champions to use SOE-based Outward Foreign Direct Investment OFDI to subvert international rules, access markets, and gain resources without resorting

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<sup>51</sup> For the negative externalities of SOEs on the current Chinese economy see Orlik, *China: The Bubble That Never Pops*, 13-15.

<sup>52</sup> Borensztein and Ostry observe rises in total factor productivity (TFP) of Chinese labor markets when comparing pre-and post-SOE reform, but speculate on the viability of such TFP gains throughout the economy. See E. Borensztein and J. Ostry, "Accounting for China's Growth Performance," *American Economic Review* 86, no. 2 (May 1996): 224-228, <https://www.jstor.org/stable/2118127>.

<sup>53</sup> Daniel Rosen, "China's Economic Reckoning," *Foreign Affairs* 100, no. 4 (July/August 2021): 20-29; Jude Blanchette, "Xi's Gamble," *Foreign Affairs* 100, no. 4 (July/August 2021): 10-19.

<sup>54</sup> Mikael Mattlin, "The Chinese Government's New Approach to Ownership and Financial Control of Strategic State-Owned Enterprises," (BOFIT Discussion Paper No. 10, Bank of Finland, BOFIT, Institute for Economies Transition, Helsinki, 2007), 12-45, [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=1001617](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1001617).

to painful industrial adjustment.<sup>55</sup> In fact, Stone et al. find evidence that SOE-based OFDI follows the CCP's foreign policy guidance as compared to smaller Chinese firms.<sup>56</sup> Lin et al. point to another innovation in the evolution of Chinese SOEs. They find unique corporate governance structures based on formal and informal contracts, policies, and regulatory institutions that help align competing firm and party objectives.<sup>57</sup>

### Foreign Direct Investment (FDI)

As the world's top bilateral creditor, China's FDI is another key economic tool for the CCP of considerable scholarship. Horn et al. estimate that between 1949-2017 the world accumulated \$1.5 trillion in debt to China, exploiting a system of underreported loans and near market-level interest rates.<sup>58</sup> One common strand captures Chinese OFDI as a principle tool of so-called "Debt-Trap Diplomacy," whereby the PRC lures developing nations into fiscally unsustainable loans in order to gain political leverage or

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<sup>55</sup> Amos Irwin and Kevin Gallagher, "Exporting National Champions: China's OFDI Finance in Comparative Perspective," (GEGI Working Paper 6, Global Economic Governance Initiative, Boston University, June 2014), 14-15, <https://www.bu.edu/pardee/files/2014/06/Exporting-National-Champions-Working-Paper.pdf>.

<sup>56</sup> Randall Stone, Yu Wang, Shu Yu, "Chinese Power and the State-Owned Enterprise," *International Organization* (August 2021): 1-22, <https://doi.org/10.1017/S002081321000308>.

<sup>57</sup> Karen Lin, Xiaoyan Lu, Junsheng Zhang, and Ying Zheng, "State-Owned Enterprises in China: A Review of 40 Years of Research and Practice," *China Journal of Accounting Research* 13, no. 1 (February 2020): 1-25, <https://doi.org/10.1016/j.cjar.2019.12.001>.

<sup>58</sup> Sebastian Horn, Carmen Reinhart, and Christoph Trebesch, "How Much Money Does the World Owe China," *Harvard Business Review*, February 26, 2020, <https://hbr.org/2020/02/how-much-money-does-the-world-owe-china>.

reclaim collateralized physical property of value to China.<sup>59</sup> However, recent scholarship provides more nuance to this frame. Brautigam's case study analysis shows how the narrative of Chinese international involvement has been co-opted by various media and governments.<sup>60</sup> Alternatively, Carmody et al. represent another strand of the literature, describing Chinese OFDI and the larger Belt and Road Initiative as a means to utilize excess capacity of capital and material from China's domestic economy.<sup>61</sup> Another lens views Chinese OFDI as inherently more decentralized. Jones and Zeng argue that rather than a centrally driven geopolitical scheme, the BRI is a set of loosely associated projects subject to competing domestic interests.<sup>62</sup> Most recently, a new field of study identifies Chinese innovations in OFDI collateralization. Gelpern et al. review of Chinese debt

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<sup>59</sup> The debt-trap diplomacy frame of Chinese OFDI has become increasingly popular within the U.S. diplomatic and military communities. See Brahma Chellaney, "China's Debt Trap Diplomacy," Project Syndicate, January 23, 2017, <https://www.project-syndicate.org/commentary/china-one-belt-one-road-loans-debt-by-brahma-chellaney-2017-01>.

<sup>60</sup> Deborah Brautigam, "A Critical Look at Chinese Debt-Trap Diplomacy: The Rise of a Meme," *Area Development and Policy* 5, no. 1 (December 2019): 1-14, <https://doi.org/10.1080/23792949.2019.1689828>.

<sup>61</sup> This school of thought proposes that not only do BRI OFDI projects generate Chinese economic growth, they also preserve Chinese socioeconomic status by outsourcing risky Chinese debt requirements and delaying macroeconomic reform. See Pdraig Carmody, Ian Taylor, and Tim Zajontz, "China's Spatial Fix and 'Debt Diplomacy' in Africa: Constraining Belt or Road to Economic Transformation?" *Canadian Journal of African Studies* (February 8, 2021): 14-15, <https://doi.org/10.1080/00083968.2020.1868014>.

<sup>62</sup> This firm-level argument largely follows the work of William Norris that emphasizes that state control of economic actors is contingent upon a set of conditions. See Lee Jones and Jinghan Zeng, "Understanding China's Belt and Road Initiative: Beyond Grand Strategy to a State Transformation Analysis," *Third World Quarterly* 40, no. 8 (August 2019): 1415-1439, <https://doi.org/10.1080/01436597.2018.1559046>.

contracts with foreign governments reveals that China successfully navigates credit risk in the developing world through a combination of confidentiality, seniority, and policy contract requirements. Through these contractual stipulations, China can ensure they have financial non-disclosure, priority of payment over other creditors, and policy alignment.<sup>63</sup> Similarly, Malik et al. review of Chinese development projects shows not only the use of collateralization to mitigate developing state credit risk, but also a significant amount of Chinese lending off national balance sheets.<sup>64</sup>

### Regulatory Control

Regulatory control is another key Chinese economic tool. Although once discouraged in economic thought, high regulatory and capital controls are broadly acknowledged as an important component of both Chinese growth and developing country growth in general.<sup>65</sup>

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<sup>63</sup> Anna Gelpern, Sebastian Horn, Scott Morris, Brad Parks, and Cristoph Trebesch, “How China Lends: A Rare Look into 100 Debt Contracts with Foreign Governments,” (Working Paper 21-7, AidData, College of William & Mary, Williamsburg, VA, March 2021), 4-9, <https://www.aiddata.org/publications/how-china-lends>.

<sup>64</sup> Malik et al. review of Chinese debt structuring reveals perhaps the strongest evidence of profit-maximizing behavior by Chinese economic agents. See Ammar Malik, Bradley Parks, Brooke Russell, Joyce Lin, Katherine Walsh, Kyra Solomon, Sheng Zhang, Thai-Binh Elston, and Seth Goodman, *Banking on the Belt and Road: Insights from a New Global Dataset of 13,427 Chinese Development Projects* (Williamsburg, VA: AidData, College of William & Mary, September 2021), 1-6, <https://www.aiddata.org/publications/banking-on-the-belt-and-road>.

<sup>65</sup> Gallagher and Tian find that revised International Monetary Fund guidance and increasing capital flow risk after the 2008 Financial Crisis contributed to a rise in support capital flow regulation across the developing world. See Kevin Gallagher and Yuan Tian, “Regulating Capital Flows in Emerging Markets: The IMF and the Global Financial

However, recent scholarship points to the effects and determinants of Chinese regulatory controls. Sun and Li argue Beijing's current focus on capital controls is the product of iterative experimentation post-Global Financial Crisis to deal with excessive global liquidity. They argue in today's macroeconomic conditions that floating exchange rates are no longer sufficient for monetary policy autonomy.<sup>66</sup> Aggarwal and Reddie argue that China's regulatory policy successes throughout the 2010s to foster next-generation industrial bases created a new form of economic statecraft centered on industrial policy.<sup>67</sup>

One component to this success is China's asymmetry in regulatory control as compared to other states. Brown and Singh as well as Carbaugh and Wassell report that China induces forced technology transfer at a massive scale through a combination of joint ventures, special purpose vehicles, and mergers and acquisitions. Western firms are often required to share patented intellectual property as requirements for Chinese market access, exploiting individual profit maximizing behavior without the protection of

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Crisis," *Review of Development Finance* 7, no. 2 (2017): 95-106, <https://www.sciencedirect.com/science/article/pii/S1879933717300775?via%3Dihub>.

<sup>66</sup> Sun and Li, writing on behalf of the People's Bank of China, propose a capital control-focused revision to the customary equilateral triangle representing the "Impossible Trilemma" in standard macroeconomic theory. See Guofeng Sun and Li Wenzhe, "Monetary Policy, Exchange Rate, and Capital Flow: From 'Equilateral Triangle' to 'Scalene Triangle'," (The People's Bank of China Working Paper Series, No. 3, Beijing, March 30, 2017), [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2949307](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2949307).

<sup>67</sup> Aggarwal and Reddie in particular highlight the effects of the 2011 Chinese National Review Process for mergers and acquisitions as well as the 2015 Chinese National Security Law. See Aggarwal and Reddie, "New Economic Statecraft," 6-8.

governmental regulatory controls.<sup>68</sup> Further, Chinese regulatory controls are also highly responsive to emerging CCP policy preferences. For example, Yazar finds that the China Banking Regulatory Commission (CBRC) consistently yields to CCP preferences on important policy issues ranging from small-medium enterprises, local government debt, and consumer protection measures.<sup>69</sup> Finally, regulatory controls facilitate future offensive tools. Steil and Litan argue that control of individual outbound private investment, normally guided by profit motive, will increasingly determine the effectiveness of financial sanction.<sup>70</sup> This suggests that over time China will be able to garner more policy influence as its currency rises in strength relative to the U.S. dollar.

#### Alternative Finance

A final key Chinese economic tool are its various alternative finance regimes. One method of alternative finance is to supplant the U.S. dollar with the Chinese

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<sup>68</sup> Michael Brown and Pavneet Singh, *China's Technology Transfer Strategy: How Chinese Investments In Emerging Technology Enable a Strategic Competitor to Access the Crown Jewels of the U.S. Innovation* (Mountain View, CA: Defense Innovation Unit Experimental, January 2018), 6-8, [https://admin.govexec.com/media/diux\\_chinatechnologytransferstudy\\_jan\\_2018\\_\(1\).pdf](https://admin.govexec.com/media/diux_chinatechnologytransferstudy_jan_2018_(1).pdf); Bob Carbaugh and Chad Wassell, "Forced Technology Transfer and China," *Economic Affairs* 39, no. 3 (2019): 306-319.

<sup>69</sup> The CBRC regulates the Chinese banking industry which dominates China's underdeveloped financial market. Yazar's case study concludes that the CBRC is not a truly independent authority. See Orhan Yazar, "Regulation with Chinese Characteristics: Deciphering Banking Regulation in China," *Journal of Current Chinese Affairs* 44, no. 2 (2015): 135-166.

<sup>70</sup> Steil and Litan argue that the inability to control outbound investment by private citizens has rendered most U.S. financial sanction ineffective despite America's dominant position in international markets. See Benn Steil and Robert Litan, *Financial Statecraft: The Role of Financial Markets in American Foreign Policy* (New Haven: Yale University Press, 2006), 159-162.

Renminbi (RMB). Cohen argues currencies have a lifecycle that is a function of the country's geopolitical ambition, and for nearly ten years China has actively promoted its rising currency.<sup>71</sup> RMB internationalization was once seen as ultimately limited to the Asian region.<sup>72</sup> However, RMB use has grown due to the BRI, and most participants project increased use over time.<sup>73</sup> Peters et al. argue the latest version of China's currency promotion is its Digital Currency Electronic Payment (DCEP), known colloquially as the digital Yuan, which promises to overcome many current RMB limitations as a first mover among central bank digital currencies.<sup>74</sup>

Doshi argues that Chinese alternative finance efforts over the last decade also included various replacement methods to mainstream rating and payments systems.<sup>75</sup> Similarly, Ly argues that RMB internationalization is also supported by the push for

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<sup>71</sup> Countries who choose to promote their currency typically do so to accrue a series of benefits such as increased seigniorage, macroeconomic flexibility, political leverage, and international reputation. See Benjamin Cohen, *Currency Statecraft: Monetary Rivalry and Geopolitical Ambition* (Chicago: University of Chicago Press, 2019), 44-64.

<sup>72</sup> Hyoung-kyu Chey, "Can the Renminbi Rise as a Global Currency?" *Asian Survey* 53, no. 2 (March-April 2013): 348-368, <https://doi.org/10.1525/as.2013.53.2.348>.

<sup>73</sup> Bank of China, "White Paper on RMB Internationalization: RMB Along the Belt and Road," (Beijing, 2015), 14, <https://pic.bankofchina.com/bocappd/rareport/201511/P020151109382840816047.pdf>.

<sup>74</sup> Michael Peters, Benjamin Green, Melissa Yang, "Cryptocurrencies, China's Sovereign Digital Currency (DCEP), and the US Dollar System," *Educational Philosophy and Theory* (August 2020): 1-7, <https://doi.org/10.1080/00131857.2020.1801146>.

<sup>75</sup> Doshi introduces China's efforts to replace the U.S. Dollar as global reserve currency, global SWIFT financial messaging system, and the big three American credit rating agencies. See Doshi, *The Long Game*, 246-58.

Chinese Cross-Border Interbank Payment System (CIPS) to replace the SWIFT.<sup>76</sup> In addition, Chen's examination of Chinese official development finance practices reveals various methods of alternative credit schemes such as fiscal guarantees, government-backed collateral, and commodity-based repayments.<sup>77</sup> These practices effectively generate a modern-day alternative to standard international financial institution practices, particularly for developing nations. Niczyporuk and Urpelainen find that Chinese financial alternatives attract state partners with high credit risk.<sup>78</sup>

China also focuses on influencing international and multinational financial organizations. China's formal governance role in Bretton Woods institutions such as the World Bank and International Monetary Fund is not proportional to its current economic standing. As a result, Morris et al. show China's growing influence in IFIs through mid- and senior-grade leadership positions, contract accrual, and discretionary investment focus.<sup>79</sup> Humphrey and Chen investigate Chinese emphasis on multilateral and regional

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<sup>76</sup> Bora Ly, "The Nexus of BRI and Internationalization of Renminbi (RMB)," *Cogent Business & Management* 7, no. 1 (August 2020), <https://doi.org/10.1080/23311975.2020.1808399>.

<sup>77</sup> Muyang Chen, "Beyond Donation: China's Policy Banks and the Reshaping of Development Finance," *Studies in Comparative International Development* 55 (August 2020): 436-459, <https://doi.org/10.1007/s12116-020-09310-9>.

<sup>78</sup> Hanna Niczyporuk and Johannes Urpelainen, "Taking a Gamble: Chinese Overseas Energy Finance and Country Risk," *Journal of Cleaner Production* 281 (January 2021): 10, <https://doi.org/10.1016/j.jclepro.2020.124993>.

<sup>79</sup> Morris et al. find that China augments its formal IFI governance role with mid and senior level leadership positions, disproportionate of contract accrual by Chinese firms, and by focusing IFI loans on Chinese development goals such as infrastructure and agriculture. See Scott Morris, Rowan Rockafellow, and Sarah Rose, "Mapping China's Multilateralism: A Data Survey of China's Participation in Multilateral Development Institutions and Funds," (Policy Paper No. 241, Center for Global Development,

development banks (MDB, RDB) such as the Asian Infrastructure Investment Bank or Caribbean Development Bank. They find growing Chinese influence in the form of large direct shareholding as a means to diversify state borrowing and crediting, drive regional consensus, and promote its views on economic development.<sup>80</sup>

Ultimately, while the RMB is not postured to overtake the U.S. dollar as global reserve currency in the near term, the CCP is preparing for the opportunity. Falcone charts the expansion of PBOC operations, identifying its growth largely mirrors the capabilities of the U.S. Federal Reserve and U.S. Treasury Department over time to enable a more aggressive policy as the Reminbi grows in strength relative to the dollar.<sup>81</sup> Kumar and Rosenbach argue that a successful Digital Yuan, in conjunction with all China's other alternative finance mechanisms, would promise China the panopticon view of global finance that the U.S. has enjoyed for decades.<sup>82</sup>

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Washington, DC, November 2021), 57-58, <https://www.cgdev.org/sites/default/files/mapping-chinas-multilateralism-data-survey.pdf>.

<sup>80</sup> Chris Humphrey and Yunnan Chen, *China in the Multilateral Development Banks: Evolving Strategies of a New Power* (London: Overseas Development Institute, September 2021), 30-31, [https://cdn.odi.org/media/documents/ODI\\_Report\\_-\\_China\\_MDB\\_Octoberupdate.pdf](https://cdn.odi.org/media/documents/ODI_Report_-_China_MDB_Octoberupdate.pdf).

<sup>81</sup> Falcone notes that despite the PBOC's increasingly offensive posture, global trust in the Renminbi continues to be too low to bifurcate the global financial system. This stems from China's weak financial markets and low currency reserve status. See Jonathan Falcone, "The People's Bank of China's Monetary Armament: Capabilities and Limitations of Evolving Institutional Power," *Military Review* 100, no. 4 (July-August 2020): 68-85.

<sup>82</sup> Aditi Kumar and Eric Rosenbach, "Could China's Digital Currency Unseat the Dollar?" *Foreign Affairs*, May 20, 2020, <https://www.foreignaffairs.com/articles/china/2020-05-20/could-chinas-digital-currency-unseat-dollar>.

## Chinese Hierarchy Management (2017-Present)

As China attempted to maintain its global economic position over time, its economic interactions since 2017 increasingly resemble a multi-dimensional contest of politics, society, and narrative as much as economics itself. This section of the literature identifies the various domestic and international forces simultaneously shaping modern Chinese economic statecraft.

### Chinese Domestic Pressures

#### Market

China faces a series of market pressures stemming from decades of partial economic liberalization and socialization. Dollar as well as Economy and Levi argue that Western market structures are perhaps the biggest constraint on CCP decision making.<sup>83</sup> Among these market structures, both Shih and Huang speculate that the inadequate corporate bond and equity markets will constrain its rise.<sup>84</sup>

Further, expansionary Chinese fiscal policy since the Global Financial Crisis combined with an immature financial system to metastasize an excessive domestic debt.

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<sup>83</sup> Dollar partially refutes the current mainstream thought that American-led economic engagement with China failed. See David Dollar, “Four Decades of Reforming Chian’s International Economic Role,” in *To Get Rich Is Glorious*, 165-167; Economy and Levi refute the narrative of Chinese global resource extraction, and identify that private actor reliance in commodity markets moderate Chinese policy. See Elizabeth Economy and Michael Levi, *By All Means Necessary: How Chinas Resource Quest is Changing the World* (New York: Oxford University Press, 2014), 191-195.

<sup>84</sup> Victor Shih, “Financial Repression Still: Policy Concerns and Stagnation in China’s Corporate Bond Market,” in *To Get Rich is Glorious*, 113-138; Yukon Huang, “China’s Emergence as a Trading Power and Tensions with the West,” in *To Get Rich is Glorious*, 197-198.

Both McCormick and Bai et al. argue that inefficient Chinese capital allocation concentrated risk within particular financial mechanisms such as off-balance sheet lending and in certain sectors such as real estate.<sup>85</sup> It is estimated that local government and corporate debt alone is approximately 50% and 200% of GDP, respectively.<sup>86</sup>

While increasing national debt stocks typify many wealthy countries, China might have become too overleveraged before it gained the productivity necessary to sustain its growth. Ding and Li point to a lack of Total Factor Productivity growth during China's decades of rapid rise as issues to future economic viability as other comparative advantages such as labor rate and labor supply decrease without proper social safety nets to support worker displacement.<sup>87</sup>

Nonetheless, China retains great resilience to these market pressures. As Tooze, Orlik, and Kratz et al. all show, Chinese officials have an excellent track record responding effectively to financial modern crisis, to include the macroeconomic strains of the COVID pandemic.<sup>88</sup> However, China's lack of institutionalization may drive a

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<sup>85</sup> Dinny McMahon, *China's Great Wall of Debt: Shadow Banks, Ghost Cities, Massive Loans, and the End of the Chinese Miracle* (New York: Houghton Mifflin Harcourt, 2018), 36-44; Chon Bai, Chang-Tai Hsieh, and Zheng Song, "The Long Shadow of China's Fiscal Expansion," *Brookings Papers of Economic Activity* (Fall 2016): 129.

<sup>86</sup> Orlik, *China: The Bubble That Never Pops*, 11-21.

<sup>87</sup> Chun Ding and Junyang Li, "Analysis Over Factors of Innovation in China's Fast Economic Growth Since its Beginning of Reform and Opening Up," *AI and Society* 29, no 3 (August 2014): 377-386, <https://doi.org/10.1007/s00146-013-0465-z>.

<sup>88</sup> For COVID-era macroeconomic resilience see Adam Tooze, *Shutdown: How COVID Shook the World's Economy* (New York: Penguin, 2021); for COVID-era overseas debt resilience see Agatha Kratz, Matthew Mingey, and Drew D'Alelio, "Seeking Relief: China's Overseas Debt After COVID-19," (Rhodium Group LLC, New

growing gap between Chinese economic ambitions and actual capability. Fewsmith finds that power-based factionalism and abuse within the CCP ultimately impedes its strong governance structures.<sup>89</sup> Beckly and Brands argue that Beijing has not been able to cope with global counterbalancing against it to include increasing economic encirclement that will accelerate its slowing growth.<sup>90</sup>

## Social

China also continues to balance societal change with its economic challenges. Zhang identifies that China most recently exemplifies this behavior in the ongoing “Great Reversal,” a new state program of conservative societal reform that targets China’s burgeoning tech sector and upper class.<sup>91</sup> These social reforms will continue to impact China’s digital development. Gallagher and Miller examine China’s social media repression, identifying an increasing focus on viral online content due to inherent

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York, October 8, 2020), [https://rhg.com/wp-content/uploads/2020/10/RHG\\_SeekingRelief\\_8Oct2020\\_Final.pdf](https://rhg.com/wp-content/uploads/2020/10/RHG_SeekingRelief_8Oct2020_Final.pdf); for macroeconomic resilience in the 2010s such as 2008 Financial Crisis, 2012 Wenzhou Crisis, 2013 money market crisis, and 2015 equity market crash, see Orlik, *China: The Bubble That Never Pops*, 183-185.

<sup>89</sup> Fewsmith, *Rethinking Chinese Politics*, 3-8.

<sup>90</sup> Michael Beckley and Hal Brands, “The End of China’s Rise: Beijing Is Running Out of Time to Remake the World,” *Foreign Affairs*, October 1, 2021, <https://www.foreignaffairs.com/articles/china/2021-10-01/end-chinas-rise>.

<sup>91</sup> Zhang explores the determinants of the Great Reversal, ongoing since October 2020, to identify the regulatory uncertainty that accompany authoritarian regimes. See Angela Zhang, “Agility Over Stability: China’s Great Reversal in Regulating the Platform Economy,” *Harvard International Law Journal* 63, no. 2 (2022): 54-55, [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3892642](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3892642).

limitations in the party's digital control.<sup>92</sup> Social reforms such as anti-corruption campaigns may impact the economy. Bai et al. argue that local government corruption serves an important role in the Chinese economy, adding needed innovation and competition to overcoming existing extractive institutions.<sup>93</sup> This research suggests that China's attempts to shield its society as part of economic reform will continue to enact short-run and long-run efficiency costs.

### Chinese International Pressures

#### U.S.

The American-led counterbalance to Chinese economic statecraft is a central feature of modern geopolitics. The literature broadly captures these trends in two areas: the failure to adapt U.S. economic hegemony to a rising China and the associated resurgence of U.S. protectionist measures.

One dominant narrative emerging in the literature is the failure to adapt U.S. economic practices to a world dominated by Chinese interests. Until recently, the U.S. largely championed economic liberalization both domestically and internationally. This view combines Cold War-era paradigms of commercial activity and interdependence,

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<sup>92</sup> Mary Gallagher and Blake Miller, "Who Not What: The Logic of China's Information Control Strategy," *The China Quarterly* 248, no. 1 (December 2021): 1031-1032, <https://doi.org/10.1017/S0305741021000345>.

<sup>93</sup> Bai et al. find significant variation in economic gain based on local government autonomy. They argue local government corruption counterintuitively drives growth by aligning incentives and balancing extractive policies. Chong-En Bai, Chang-Tai Hsieh, and Zheng Song, "Special Deals with Chinese Characteristics," (Working Paper 25839, National Bureau of Economic Research, Cambridge, MA, May 2019), 2-6, <https://www.nber.org/papers/w25839>.

such as those expressed by Keohane and Nye as well as and Gilpin, with rising financial leverage absorbed by the U.S. in the 1980s, 1990s, and 2000s.<sup>94</sup> This conception of American economic statecraft translated well into objectives against non-state actors and economically small state actors according to both Zarate and Farrell and Newman.<sup>95</sup> However, as McCormick et al. argue, it has proved less resilient in utilizing economic interdependence against state actors in a time of rapid technological change.<sup>96</sup> Further, as Aggarwal and Reddie and Irwin and Gallagher identify, Chinese economic statecraft innovation has in many ways seized strategic asymmetry.<sup>97</sup>

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<sup>94</sup> Under this view of liberalization, the U.S. government and commercial actors are separate entities in world affairs, and the U.S. government is responsible to set conditions for American MNC overseas. Steil and Litan argue that U.S. financial leverage began to skyrocket in the 1980s due to U.S. equity and bond market innovations. Robert Keohane and Joseph Nye, "Power and Interdependence," *Survival* 15, no. 4 (1973): 158-165; Robert Gilpin, "The Political Economic of the Multinational Corporation: Three Contrasting Perspectives," *American Political Science Review* 70, no. 1 (March 1976): 184-191; Steil and Litan, *Financial Statecraft*, 6.

<sup>95</sup> Zarate describes the evolution of U.S. financial coercion in the post 9/11 era. Farrell and Newman describe how globalization gave rise to a U.S. strategic asymmetry over global economics and information. Juan Zarate, *Treasury's War: The Unleashing of a New Era of Financial Warfare* (New York: Public Affairs, 2013); Henry Farrell and Abraham Newman, "Weaponized Interdependence: How Global Economic Networks Shape State Coercion," *International Security* 44, no. 1 (Summer 2019): 42-79.

<sup>96</sup> McCormick's, Luftig's, and Cunningham's recommendations for how the U.S. government must organize and act to develop future economic strength calls into question many core American assumptions about the relationship between government and commercial actors. David McCormick, Charles Luftig, and James Cunningham, "Economic Might, National Security, and the Future of American Statecraft," *Texas National Security Review* 3, no. 3 (Autumn 2020): 50-75.

<sup>97</sup> Irwin and Gallagher focus on the innovations of Chinese OFDI to sustain its rise in today's era while Aggarwal and Reddie identify Chinese advantages in industrial policy. Irwin and Gallagher, "Exporting National Champions," 20-22; Aggarwal and Reddie, "New Economic Statecraft," 5-6.

As a result, much of U.S.-led pressure on Chinese economic statecraft is an ineffective protectionist response. Lack of efficacy begins with domestic economic hardship. Li et al. project current U.S. trade restriction packages will only decrease domestic manufacturing employment due to large substitution and retaliation effects.<sup>98</sup> Fajgelbaum et al. conclude that U.S. tariff measures present negative real income loss, especially in manufacturing-heavy regions.<sup>99</sup> Further, U.S. efforts have not mobilized collective action of its firms to induce economic pain on China. Vorthrems and Zhang find that U.S. and allied firm participation in Chinese markets is driven by their resources and governing institutions, not U.S. policy guidance.<sup>100</sup> Nye concludes that desired decoupling varies widely by economic sector and could ultimately constrain future U.S. ability to coerce and deter as global interdependencies decrease.<sup>101</sup>

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<sup>98</sup> Chunding Li, Jing Wang, and John Whalley, “Trade Protectionism and U.S. Manufacturing Employment,” (Working Paper 25860, National Bureau of Economic Research, Cambridge, MA, May 2019), 24-25, <https://www.nber.org/papers/w25860>.

<sup>99</sup> Pablo Fajgelbaum, Pinelopi Goldberg, Patrick Kennedy, and Amit Khandelwal, “The Return to Protectionism,” *Quarterly Journal of Economics* 135, no. 1 (February 2020): 1-55, <https://doi.org/10.1093/qje/qjz036>.

<sup>100</sup> Vorthrems and Zhang show that while U.S. trade policies increase overall firm exit from the Chinese market, it does not drive U.S. exit as compared to other nations. They argue the resources available and sunk costs in the Chinese market inhibit large firm exit. This suggests larger hardship on small and rising firms while MNCs largely remain entrenched in overseas markets—both damaging to U.S. policy initiatives. Samantha Vorthrems and Jack Zhang, “Political Risk and Firm Exit: Evidence from the US-China Trade War,” (21st Century China Center Research Paper 2021-09, University of California San Diego, September 2021), 29-34, [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3916186](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3916186).

<sup>101</sup> Nye argues that the U.S. protectionist measures are too crude to carefully manage its asymmetric interdependencies with the world, and as a result risk its long-term influence. Joseph Nye, “Power and Independence with China,” *The Washington*

## International

China's economic statecraft also increasingly impacts the international community around it. These effects can largely be summarized by developing nations, developed nations, and International Financial Institution (IFI). Much like the United States, developed nations show the most balancing behavior against Chinese economic statecraft. Chiu identifies that the epicenter for discontent with Chinese statecraft lies in the socio-political structures of the developed West.<sup>102</sup> Hooijmaaijers' case study analysis of Chinese investment on European Union countries reveals rising OFDI generated not only competition amongst members states, but also collective regulatory controls.<sup>103</sup> Blading identifies similar backlash among democratic countries.<sup>104</sup> Increasingly, balancing behavior by developed countries becomes a self-sustaining narrative. As Chin notes, China is increasingly labelled as an economic revisionist, particularly among the developed world.<sup>105</sup> Economy notes that these narratives are impediments to China's soft

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*Quarterly* 43, no. 1 (Spring 2020): 7-21, <https://doi.org/10.1080/0163660x.2020.1734303>.

<sup>102</sup> Joanna Chiu, *China Unbound: A New World Disorder* (Ontario: Anansi Press, 2021).

<sup>103</sup> Bas Hooijmaaijers, "Blackening Skies for Chinese Investment in the EU?" *Journal of Chinese Political Science* 24, no. 1 (February 2019): 451-470, <https://doi.org/10.1007/s11366-019-09611-4>.

<sup>104</sup> Christopher Blading, "Why Democracies Are Turning Against Belt and Road," *Foreign Affairs*, October 24, 2018, <https://www.foreignaffairs.com/articles/china/2018-10-24/why-democracies-are-turning-against-belt-and-road>.

<sup>105</sup> Gregory Chin, "True Revisionist: China and the Global Monetary System," in *China's Global Engagement: Cooperation, Competition, and Influence in the 21st Century*, ed. Jacques Delisle and Avery Goldstein (Washington, DC: Brookings Institution Press, 2017), 35-66.

power efforts, and force China to augment their international influence by other means, such as cultural conditioning, which also disrupt Chinese perceptions.<sup>106</sup> However, as Brautigam et al find, these same perceptions can also lead the developed to unintentionally overestimate Chinese intention and actions.<sup>107</sup>

Another vector of pressure on Chinese economic statecraft comes from the developed world. Pu reveals China's long history of contradictory signals to both claim and shirk informal leadership of the developing world.<sup>108</sup> China has a similar conflicting relationship with the developing world. Much of the pushback to Chinese economic development comes from negative externalities within low and middle income countries. Morgan for example, observes that Africans view elements of Chinese economic statecraft with varying levels of skepticism, favoring investment and aid while opposing trade.<sup>109</sup> Wegenast et al. find that Chinese mining projects decrease local employment.<sup>110</sup>

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<sup>106</sup> Economy, *The Third Revolution*, 219.

<sup>107</sup> Deborah Brautigam, Yufan Huang, and Kevin Acker, "Risky Business: New Data on Chinese Loans and Africa's Debt Problem," (Briefing Paper no. 3, China Africa Research Initiative, Johns Hopkins University School of Advanced International Studies, Baltimore, MD, 2020), 11-12, <https://static1.squarespace.com/static/5652847de4b033f56d2bdc29/t/6033fadb7ba591794b0a9dff/1614019291794/BP+3+-+Brautigam%2C+Huang%2C+Acker+-+Chinese+Loans+African+Debt.pdf>.

<sup>108</sup> Pu, *Rebranding China*, 3-6.

<sup>109</sup> Morgan concludes that African perceptions largely support China's desired win-win narratives despite Western views of Chinese influence. Pippa Morgan, "Can China's Economic Statecraft Win Soft Power in Africa? Unpacking Trade, Investment, and Aid," *Journal of Chinese Political Science* 24 (December 2018): 387-409, <https://doi.org/10.1007/s11366-018-09592-w>.

<sup>110</sup> Wegenast et al. theorize that Chinese comparative advantages in labor skill will make them less likely to support regional employment. Tim Wegenast, Mario Krauser, Georg Struver, and Juliane Giesen, "At Africa's Expense? Disaggregating the

The literature also finds that broad narratives such as “Debt Trap Diplomacy” do not accurately capture the casual effects of Chinese influence in the developing world, and ultimately inhibit understanding. Were refutes the Debt Trap narrative through an investigation of Sino-African debts and concludes that it detracts from the agency and necessary reform of African countries.<sup>111</sup> Singh concludes that unfounded concerns over Chinese financial influence ultimately reflect Western preservation concerns and not the welfare of the developing world.<sup>112</sup>

China also yields a large but underappreciated economic impact on International Financial Institutions (IFI). Srinivasan argues that the international community, particularly developing nation leaders such as China, have long called for IFI governance reform.<sup>113</sup> Broze et al. show that the top grievance for BRI-supporting nations is IFI

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Employment Effects of Chinese Mining Operations in Sub-Saharan Africa,” *World Development* 118 (June 2019): 39-51, <https://doi.org/10.1016/j.worlddev.2019.02.007>.

<sup>111</sup> Anzette Were, “Debt Trap? Chinese Loans and Africa’s Development Options,” (Policy Insights 66, South African Institute of International Affairs, Johannesburg, August 2018), 9-10, <https://www.africaportal.org/publications/debt-trap-chinese-loans-and-africas-development-options/>.

<sup>112</sup> Singh finds that Chinese influence does not drive individual country debt-burden or that it coincides with larger Chinese interventionist practices. Ajit Singh, “The Myth of ‘Debt-Trap Diplomacy’ and Realities of Chinese Development Finance,” *Third World Quarterly* 42, no. 2 (August 2020): 250-251, <https://doi.org/10.1080/01436597.2020.1807318>.

<sup>113</sup> T. N. Srinivasan, “Trends and Impacts of Real and Financial Globalization in the People’s Republic of China and India Since the 1980s,” *Asian Development Review* 30 (2013): 1-30, [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2259530](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2259530).

reform and stability.<sup>114</sup> China then leverages grievance over IFI reform into a larger influence over those IFI structures. Kern and Reinberg find that countries are driven to International Monetary Fund (IMF) loans based on their Chinese debt status and external shock events.<sup>115</sup> Sundquist also finds Chinese loans crowd-out IMF lending.<sup>116</sup> Both Hernandez and Qian et al. find a similar effect in World Bank projects based on Chinese funding and loan allocation.<sup>117</sup> This evidence suggests that not only are IFI governance structures unable to keep up with the rate of change in the global economy, but that the responsiveness of Chinese alternative finance exacerbates IFI holes in a self-reinforcing cycle

### Summary and Trends

The evolution of Chinese economic statecraft brings Beijing on a journey from a bipolar Cold War-era contestation, to a unipolar international facilitation, and

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<sup>114</sup> J. Lawrence Broz, Zhiwen Zhang, and Gaoyang Wang, “Explaining Foreign Support for China’s Global Economic Leadership,” *International Organization* 74, no. 3 (2020): 450, <https://doi.org/10.1017/S0020818320000120>.

<sup>115</sup> Kern and Reinberg, “The Political Economy of Chinese Debt and IMF Conditionality,” 24-25.

<sup>116</sup> James Sundquist, “Bailouts from Beijing: How China Functions as an Alternative to the IMF,” (GCI Working Paper 15, Global Development Policy Center, Boston University, February 2021), 3, [https://www.bu.edu/gdp/files/2021/03/GCI\\_WP\\_015\\_Sundquist\\_Mar.pdf](https://www.bu.edu/gdp/files/2021/03/GCI_WP_015_Sundquist_Mar.pdf).

<sup>117</sup> Diego Hernandez, “Are New Donors Challenging World Bank Conditionality,” *World Development* 96 (August 2017): 529-549, <https://doi.org/10.1016/j.worlddev.2017.03.035>; Jing Qian, James Raymond Vreeland, Zetao Wu, and Jianzhi Zhao, “Compete or Complement? How the World Bank Responds to the Establishment of the AIIB,” (Working Paper, February 18, 2021), 16, [https://www.peio.me/wp-content/uploads/2021/papers/PEIOo21\\_paper\\_47.pdf](https://www.peio.me/wp-content/uploads/2021/papers/PEIOo21_paper_47.pdf).

increasingly back to bipolar competition. China's economic rise and modern statecraft is a story of balance between growth and disruption, both domestically and internationally.

Today, three key tensions inform not only the current state of Sino-American economic competition, but also this research project. First, global financial flows are increasingly central to international relations. Global monetary liquidity skyrocketed since the 2008 Great Financial Crisis, leaving government and private entities experimenting with new solutions. As a result, states and institutions historically central to global economic power such as the United States or IFIs are increasingly in competition for status and leverage as they attempt to keep pace with the rate of change in financial flows. This phenomena continues to alter the economic-security relationship between states. It also creates new opportunities for state and non-state actors alike to exploit financial governance norms for both individual and state ends. In this increasingly dynamic market, risk comes in the form of unstainable financial exposure and manipulation.

Second, the relationship between private and public entities is changing. Economic rivalry generates urgency for different methods of centralized economic planning in both China and the U.S. While domestic narratives such as the Community of Common Destiny or Debt-Trap Diplomacy may be helpful in motivating and galvanizing behavior of economic actors, they can also inhibit true understanding and inflict internal costs. Private and public innovations will continue to reshape this relationship, from new forms of public policy to digital financial vehicles.

Finally, China continues its concerted effort to balance both economic growth and social stability. This management manifests cyclically over time. While influenced by

international pressures, these cycles appear to be primarily driven by domestic political considerations. During this time, Beijing both secures its access in Western markets while minimizing its exposure to Western economic coercion. In so doing, China has innovated numerous tactics of financial statecraft, generating economic asymmetries over time that it can leverage for geopolitical gain.

This body of knowledge on economic statecraft and Chinese actions in the international system form a basis for the conceptual methodology to follow.

## CHAPTER 3

### RESEARCH METHODOLOGY

#### Introduction

This research methodology introduces the intended methods of data collection and analysis. Background research on China’s economic strategy, development history, and geo-economic toolkit introduced a broad concept to quantify the causes, effects, and mitigating factors of Chinese financial ways and means on the international system. As a result, this project models the ability of Chinese financial flows to influence the foreign and domestic policies of other countries over time.

#### Method

Ultimately, China varies its foreign policy geographically and over time. Given a set of means, China adapts its ways and means toward its desired ends. This action, in general, represents a constrained maximization problem that this study uses as a theoretical framework:

$$\begin{aligned} & \textit{Maximize Statecraft}_{it} = f(\textit{HardPower}, \textit{SoftPower}, \textit{SharpPower}); \\ \textit{S.T. } & Y_t = \textit{HardPower} * P_{\textit{HardPower}_{it}} + \textit{SoftPower} * P_{\textit{SoftPower}_{it}} + \textit{SharpPower} * P_{\textit{SharpPower}_{it}} \end{aligned}$$

whereby Beijing allocates some combination of foreign policy instruments, hard, soft, and sharp power, to achieve a desired level of influence through its statecraft for a specific country, *i* at a specific time, *t*. This represents maximizing a country’s ways toward its ends. However, this allocation is ultimately limited by determinant means of power, *Y*, such as various human, financial, political, and physical capital at a given time, *t*. This constraint is subject to “prices” of hard, soft, and sharp power that vary by country

and across time as certain instruments are more or less effective based off a country's internal resiliencies, vulnerabilities, and preferences. Thus, relative costs and benefits constrain ways given available means. Chinese strategy, then, is about maximizing its ways to achieve desired ends given a set of means for a set of countries over time.<sup>118</sup>

As a result, this study proceeds as a quantitative analysis in order to capture the effect of variation in Chinese bilateral financial flows. Below is a draft mathematical model to capture the determinants and effects of Chinese economic statecraft over time:

$$Effect_{it} = \beta_0 + \beta_1 Soft_{it} + \beta_2 Sharp_{it} + \beta_3 Hard_{it} + \beta_4 Control_{it} + a_{it} + \mu_{it}$$

*Effect<sub>it</sub>* is a dependent variable capturing bilateral Chinese influence over time such as UN General Assembly voting proximity to China or the United States.

*Soft<sub>it</sub>* is a vector of soft power economic statecraft measures such as the total bilateral Chinese trade or total bilateral Chinese aid.

*Sharp<sub>it</sub>* is the vector of interest reflecting Chinese sharp power measures such as outstanding Chinese loans or FDI inflows.

*Hard<sub>it</sub>* is a vector of hard power economic statecraft such as bilateral foreign military sales or PLA military capacity index.

*Control<sub>it</sub>* is a vector of control variables proxying for state resilience and vulnerabilities that could predispose or dissuade a state from Chinese financial statecraft. Some examples include: state domestic stability (measured by GDP per capita, Freedom House democracy strength index, Chinn-Ito capital control index) or resource constraints

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<sup>118</sup> For application of this theory to modern Russian foreign policy, see Ryan Orsini, "Guns, Butter, and Tweets: The Effectiveness of Modern Russian Statecraft," (Masters Thesis, Georgetown University, 2020), 12-14.

(total resource rents as share of GDP, Chinese steel production, or total outstanding IFI loans).

### Data Collection

Due to the compressed research period, this study will utilize existing data sets from international organizations and researchers to create the novel model grounded in the theory of Chinese statecraft outlined above. In particular, the project will utilize UNGA Ideal Point data set of Bailey et al. as a dependent variable for the effects of Chinese financial statecraft.<sup>119</sup> This project will also use the bilateral Chinese loan data by Horn et al. to capture the primary independent variable of interest, Chinese financial sharp power.<sup>120</sup> Overall, this data collection methodology allows the researcher to investigate all necessary aspects of Chinese statecraft: factors that influence Beijing's allocation of resources, the bilateral effects of Chinese tools, and ways in which the U.S.

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<sup>119</sup> UN General Assembly voting is one common proxy of state authority and hierarchy, both due to its availability over time and its non-binding voting structure. Theoretically, UNGA voting incentivizes states to reveal a truer approximation of its actual foreign policy preferences. Bailey, Strezhnev, and Voeten "Ideal-Point" UNGA estimator uses a spatial model that weighs votes by past state voting preferences, yielding a better approximation of state foreign policy preference variation than dyadic similarity "S-score" indicators to measure the degree of policy alignment between states. S-scores value votes (yay, nay, or abstentions) consistently over time and policy agendas. See Michael Bailey, Anton Strezhnev, and Erik Voeten, "Estimating Dynamic State Preferences from United Nations Voting Data," *Journal of Conflict Resolution* 61, no. 2 (2017): 436, <https://doi.org/10.1177/0022002715595700>.

<sup>120</sup> Horn, Reinhart, and Trebesch capture debt stocks owed to China for 107 countries from 2000 to 2017. See Sebastian Horn, Carmen Reinhart, and Christoph Trebesch, "China's Overseas Lending," (Working Paper 26050, National Bureau of Economic Research, Cambridge, MA, May 2020), <https://doi.org/10.3386/w26050>.

can more effectively and efficiently utilize economic ways and means to better advance its interests vis-à-vis China.

### Data Analysis

This study will estimate outcomes using Ordinary Least Squares (OLS) with Fixed Effects (FE) estimation. Fixed effects eliminate bias created by unobserved but constant state-level heterogeneity. This state effect represents all factors affecting voting alignment that do not change over time such as geographical features and cultural perspectives. Also included in this measure are other factors that might be approximately constant over the panel period such as a population's entrenched attitudes or predispositions to leaders and other states. This study will also utilize quantile regression. This estimation technique will enable investigation of effects within a particular subset, or quantile, of the data distribution. For example, quantile regression can examine if Chinese economic statecraft draws disproportion effect on high or low incoming countries. All results will be presented in statistical tables upon research completion.

### Ethical Considerations

This project will assess the bilateral effects of Chinese economic influence on other states using available macroeconomic data and generate associated U.S. policy recommendations. It is careful, however, not to make normative judgements to critique the agency of other states who apply their own policy optimization when deciding to participate in economic relations with China. There are no ethical considerations related to human subjects in this project.

### Summary

This study proposes a quantitative study of Chinese economic statecraft. It will be based on a country-year panel data set of various Chinese soft, sharp, and hard power economic statecraft measures. Using fixed effects and quantile regression, this study intends to isolate both the determinants and effects of Chinese financial statecraft over time as well as possible areas of U.S. policy reform.

## CHAPTER 4

### DATA FINDINGS AND ANALYSIS

#### Introduction

Chapter four addresses this project's core issues and questions in five primary sections, followed by chapter summary. First, a data description introduces all variables used in econometric modeling to include their research origins and units of analysis. Next, descriptive statistics focus on the distributions and correlations of primary independent and dependent variables of interest within the sample. Then, baseline and sub-analysis econometric modeling presents quantitative inference to the project's research questions. It uses fixed effects regression to determine the effect of Chinese economic statecraft on the international system, this project's primary research question. Subsequent quantile regression analysis then assesses the study's secondary research questions, identifying the determinants of Chinese economic outlays and possible areas of U.S. vulnerabilities and resiliencies.

#### Data Description

##### Dependent Variable: Country Vote Share

This study's primary outcome of interest measures the policy effect of various Chinese financial instruments through voting in the UN General Assembly. If Chinese influence is successful, then an increase in bilateral financial instruments should increase the UNGA voting alignment with China and decrease it with the United States. Figure 1 below shows voting alignment using Bailey et al.'s Ideal Point Estimator. It reveals the density of country voting in proximity to U.S. over time. States with similar voting

preferences appear near zero, such as Israel. Those with the most dissimilar voting behavior appear closest to five, such as North Korea and Iran. Voting proximity with the United States is strongly correlated with developed nation status. Most highly developed nations falling between one and two, and most middle or low income countries between two and four.

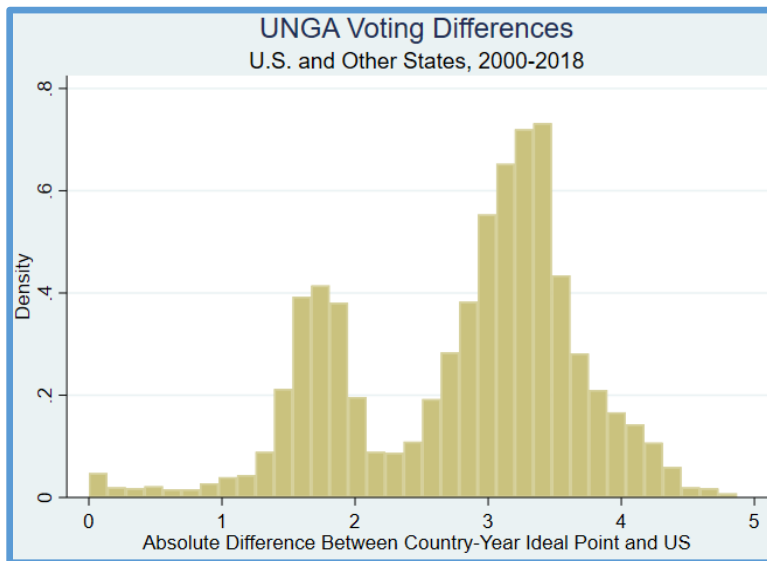


Figure 1. Histogram of Dyadic Voting Difference, U.S. and UNGA

*Source:* Created by author using Michael Bailey, Anton Strezhnev, and Erik Voeten. “Estimating Dynamic State Preferences from United Nations Voting Data,” *Journal of Conflict Resolution* 61, no. 2 (2017): 430-456. <https://doi.org/10.1177/0022002715595700>.

Independent Variables: Soft, Sharp, and Hard Financial Power

Soft Power: Bilateral Chinese Imports

Soft Power is controlled by total bilateral Chinese imports from the World Bank World Integrated Trade Solution (WITS) database. This study utilizes two

transformations of bilateral Chinese imports: logged and as a share of overall recipient country GDP. All else equal, as Chinese imports increase so should UNGA voting alignment with Chinese interests.

#### Sharp Power: Bilateral Chinese Debt Stock

Sharp power is measured by the total bilateral debt stocks owed to China. This includes by both private and public entities to Chinese state-owned creditors from direct loans based on the work of Horn et al.. It is represented in two transformations: logged and as a share of recipient country GDP. All else equal, as Chinese debt stocks increase, so will a target country's UNGA voting alignment with Chinese interests.

#### Hard Power: Bilateral Chinese Military Sales

Hard financial power is measured by bilateral foreign military sales from China to a recipient country based on the Stockholm International Peace Research Institute (SIPRI) database. It is also represented in both logged and GDP share transformations. Chinese voting alignment should increase, all else equal, as Chinese military sales rise.

#### Control Variables

This study uses three vectors of variables to control for other factors that might attract or dissuade Chinese financial influence. First, a batch of variables control for target state resilience: GDP per capita from the World Bank to capture a country's relative development growth, Freedom House's Democracy Index to control for regime similarity democracy index, and Correlates of War's national military capability index. Second, a set of variables control for Chinese interests in a target country. These include World Bank World Development Indicator for natural resource rents as share of state

GDP, Correlates of War's yearly steel production in thousand-tons, and Correlates of War's net energy consumption, measured in thousand coal-ton equivalents.

### Descriptive Statistics

Summary statistics reported in Table 5 show UN General Assembly member voting and bilateral economic tools from 2000-2018. In addition, Figure 2 shows voting alignment of the U.S. and China over the same time period using mean voting alignment. On average, UNGA voting is more aligned with China over the study's time period, and current year voting is highly consistent with past voting behavior. As shown in Table 6, bivariate correlations of available economic tools, Chinese voting proximity is most correlated with bilateral trade across independent variables.

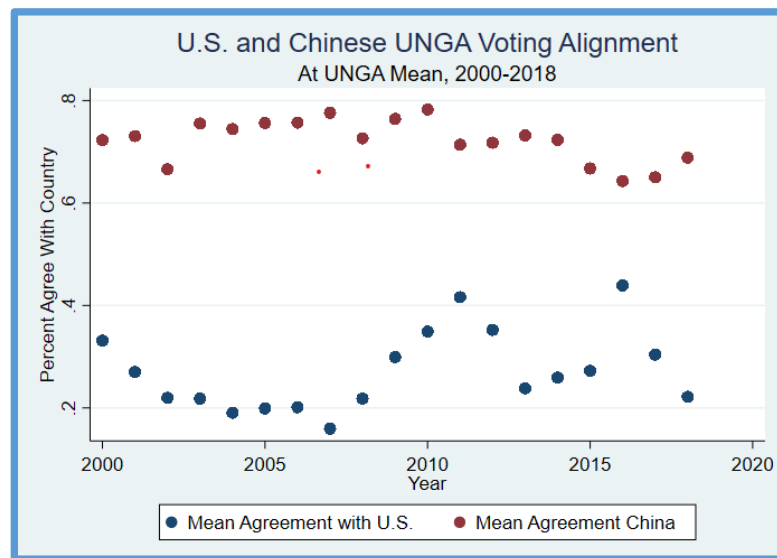


Figure 2. Line Chart of Dyadic Voting, U.S. and China

Source: Created by author using Michael Bailey, Anton Strezhnev, and Erik Voeten. "Estimating Dynamic State Preferences from United Nations Voting Data," *Journal of Conflict Resolution* 61, no. 2 (2017): 430-456. <https://doi.org/10.1177/0022002715595700>.

Figure 3 shows bilateral trade, debt, and military sales by year at sample mean. It reveals a precipitous spike in both soft power bilateral trade and sharp power debt over time, particularly between 2005 and 2015. Each of these variables shows a skewed distribution over time as Chinese financial influence is concentrated in a subset of states. As a result, all variables are scaled by logarithmic or share in order to minimize the effect of outliers within the data.

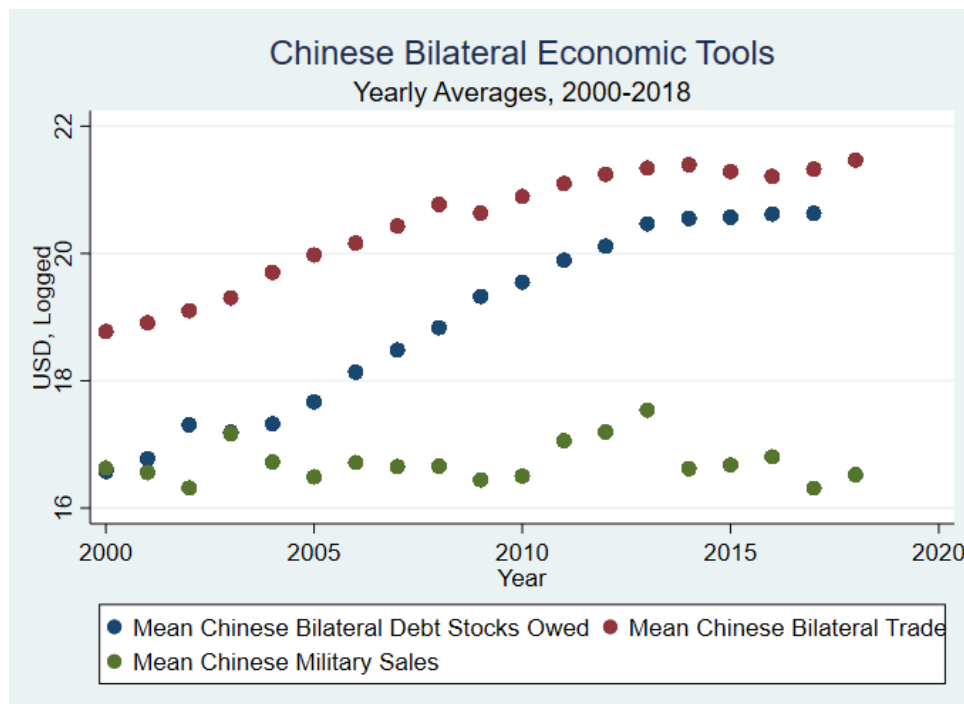


Figure 3. Scatter Plot Chart of Bilateral Chinese Economic Influence

*Source:* Created by author using Sebastian Horn, Carmen Reinhart, and Christoph Trebesch, “China’s Overseas Lending,” (Working Paper 26050, National Bureau of Economic Research, Cambridge, MA, May 2020), <https://doi.org/10.3386/w26050>; “SIPRI Arms Industry Database,” Stockholm International Peace Research Institute, accessed January 28, 2022, <https://www.sipri.org/databases/armsindustry>; “World Integrated Trade Solution Database,” World Trade Organization, accessed February 27, 2022, <https://wits.worldbank.org/>.

### Baseline Analysis

Table 1 reports OLS and FE regression by power type and country vote share. The key relationship of note is between *Bilateral Debt Share*, or total direct country debt stocks owed to China as a share of total country GDP, on UNGA voting. A 10-percentage point increase in the bilateral debt share of a country is on average associated with a 2-percentage point increase in voting alignment with China. This estimate captures the direct effect of a target country's debt owed to China on its voting changes. Noticeably, there is no significant impact on U.S. voting by any Chinese financial statecraft tool.

Table 1. Regression Baseline Estimates: Ordinary Least Squares and Fixed Effects

VARIABLES	(1) OLS Chinese Vote	(2) OLS U.S. Vote	(3) FE Chinese Vote	(4) FE U.S. Vote
Bilateral Trade (ln)	-0.007 (0.003)	0.009* (0.004)	0.0040 (0.0045)	0.0023 (0.0056)
Bilateral Debt Share	-0.0005 (0.0008)	0.002* (0.001)	0.0021*** (0.0007)	0.0006 (0.0008)
Bilateral FMS Share	0.0044 (0.046)	-0.067 (0.053)	0.0037 (0.0313)	0.0190 (0.0336)
Constant	0.557 (0.077)	0.0271 (0.088)	0.766 (0.123)	0.320 (0.107)
Observations	234	234	234	234
R-squared	0.408	0.408	0.470	0.488
Countries			51	51
Country FE			YES	YES
Year FE			YES	YES
Controls	YES	YES	YES	YES

*Source:* Created by author using Michael Bailey, Anton Strezhnev, and Erik Voeten. “Estimating Dynamic State Preferences from United Nations Voting Data,” *Journal of Conflict Resolution* 61, no. 2 (2017): 430-456, <https://doi.org/10.1177/0022002715595700>; Sebastian Horn, Carmen Reinhart, and Christoph Trebesch, “China’s Overseas Lending,” (Working Paper 26050, National Bureau of Economic Research, Cambridge, MA, May 2020), <https://doi.org/10.3386/w26050>; “SIPRI Arms Industry Database,” Stockholm International Peace Research Institute, accessed January 28, 2022, <https://www.sipri.org/databases/armsindustry>; “World Integrated Trade Solution Database,” World Trade Organization, accessed February 27, 2022, <https://wits.worldbank.org/>.

NOTE:

OLS and Fixed Effects Specifications by Power Type, 2000-2018

Dependent Variables, Share of U.S. and Chinese Votes

\*\*\* p<0.01, \*\* p<0.05, \* p<0.1

Robust standard errors in parenthesis

U.S. and Chinese UNGA voting not included in regression outputs

The practical significance of this estimate is assessed using the sample mean of Chinese voting alignment (0.76), median debt stocks (4.67 million USD), and one standard deviation in UNGA votes per year (55-81). The 2-percentage point vote

different accounts for approximately 2 more votes per year in favor of China. In 2017, this difference in voting alignment is similar to the gap between Argentina and Russia or Costa Rica and Djibouti. Among smaller economies, such as Guyana or Malawi, this increase in debt would be relatively small, at 18 and 28 million USD, respectively. Among large debtor countries, such as Ukraine, this magnitude of debt change is appreciably larger, approximately 520 million USD.

Within specifications 3 and 4, two relationships emerge among control variables. Net energy consumption and steel production, which control for country natural resource vulnerability, report as statistically significant determinants of country vote share for both the U.S. and China. These effects are of little practical significance.<sup>121</sup>

#### Sub-Analysis

Further analysis, outlined in Tables 2 and 3, use variations of quantile regression to identify determinants when Chinese instruments may be disproportionately effective vis-à-vis the United States.

#### GDP Per Capita and Chinese Voting Proximity

Table 2 presents regression estimates for Chinese vote share by power type and GDP per capita quantile. The second quantile of voting differences appears particularly sensitive to Chinese instruments of financial statecraft. In 2017, the GDP per capita of this group of 49 nations, such as Ukraine, India, and Bangladesh, range from \$1242 to

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<sup>121</sup> For example, a 100% increase in a country's steel production is associated with, on average, a 0.1 and 0.5 percentage point increase in a vote share with China and the U.S., respectively. These results are significant to the 1% level.

\$4095. Among this sub-sample, a 10-percentage point increase in the bilateral debt share of a country is on average associated with a 3.6-percentage point increase in voting alignment with China. Also within this sub-sample, a 1-percentage point increase in the share of a country's military expenditures from China is associated with a 22-percentage point increase in voting alignment. Both results are statistically significant at the 5% level. In total, this group of countries as defined by their GDP per capita, appears to be the most susceptible, on average, to Chinese financial statecraft.

Table 2. Quantile Regression Estimates: Chinese Vote Share by Power Type

VARIABLES	(1)	(2)	(3)
	GDP Capita QREG $\tau=1$	GDP Capita QREG $\tau=2$	GDP Capita QREG $\tau=3$
Bilateral Chinese Trade (ln)	0.00734 (0.00765)	0.00207 (0.00767)	-0.0353 (0.0434)
Bilateral Chinese Debt Share	0.00133 (0.00114)	0.00363** (0.00134)	0.00718** (0.00322)
Bilateral Chinese Mil Share	-0.00257 (0.0398)	0.223** (0.0817)	-0.281*** (0.0314)
Constant	0.678*** (0.183)	0.688*** (0.194)	1.407* (0.758)
Observations	100	81	50
R-squared	0.762	0.896	0.948
Countries	26	24	16
Country FE	YES	YES	YES
Year FE	YES	YES	YES
Controls	YES	YES	YES

Source: Created by author using Michael Bailey, Anton Strezhnev, and Erik Voeten. “Estimating Dynamic State Preferences from United Nations Voting Data,” *Journal of Conflict Resolution* 61, no. 2 (2017): 430-456, <https://doi.org/10.1177/0022002715595700>; Sebastian Horn, Carmen Reinhart, and Christoph Trebesch, “China’s Overseas Lending,” (Working Paper 26050, National Bureau of Economic Research, Cambridge, MA, May 2020), <https://doi.org/10.3386/w26050>; “SIPRI Arms Industry Database,” Stockholm International Peace Research Institute, accessed January 28, 2022, <https://www.sipri.org/databases/armsindustry>; “World Integrated Trade Solution Database,” World Trade Organization, accessed February 27, 2022, <https://wits.worldbank.org/>.

NOTE:

Chinese UNGA voting alignment by GDP capita quantile and power type, 2000-2018

Dependent Variable, Share of Chinese Vote

\*\*\* p<0.01, \*\* p<0.05, \* p<0.1

Robust standard errors reported in parenthesis

Chinese UNGA voting not included in regression outputs

$\tau=1$  first quartile of GDP per capita,  $\tau=2$  second quartile,  $\tau=3$  third quartile

### Distributional Effects of U.S. Voting Proximity

Additional sub-analysis on the U.S. vulnerability in Table 3 presents shows the effect of Chinese instruments on U.S. UNGA voting alignment based on the bilateral

voting distribution. Over the study sample, it appears that countries historically most closely aligned to the U.S. are more likely to change their voting behavior. Among nations in the upper half of voting alignment with the U.S., with average vote share of 0.236 or more, a 10-percentage point increase in the bilateral Chinese debt share of a country is on average associated with a 2-percentage point decrease in U.S. voting alignment. This result is statistically significant at the 10% and 5% level for the third and fourth quartile of U.S. voting alignment, respectively.

Table 3. Quantile Regression Estimates: US Vote Share by Power Type

VARIABLES	(1) OLS U.S. Vote	(2) U.S. Vote QREG $\tau=0.25$	(3) U.S. Vote QREG $\tau=0.5$	(4) U.S. Vote QREG $\tau=0.75$
Bilateral Trade	-0.00141 (0.00209)	-0.00255 (0.00540)	0.00179 (0.00326)	0.000884 (0.00181)
Bilateral Debt Share	-0.00205** (0.000928)	-0.00249 (0.00201)	-0.00220* (0.00121)	-0.00200*** (0.000676)
Bilateral Mil Share	0.0398 (0.0446)	0.111 (0.120)	0.0426 (0.0722)	0.00203 (0.0402)
Constant	0.856*** (0.0419)	0.826*** (0.110)	0.817*** (0.0662)	0.880*** (0.0369)
Observations	264	264	264	264
R-squared	0.022			
Country FE	NO	NO	NO	NO
Year FE	NO	NO	NO	NO

*Source:* Created by author using Michael Bailey, Anton Strezhnev, and Erik Voeten. “Estimating Dynamic State Preferences from United Nations Voting Data,” *Journal of Conflict Resolution* 61, no. 2 (2017): 430-456, <https://doi.org/10.1177/0022002715595700>; Sebastian Horn, Carmen Reinhart, and Christoph Trebesch, “China’s Overseas Lending,” (Working Paper 26050, National Bureau of Economic Research, Cambridge, MA, May 2020), <https://doi.org/10.3386/w26050>; “SIPRI Arms Industry Database,” Stockholm International Peace Research Institute, accessed January 28, 2022, <https://www.sipri.org/databases/armsindustry>; “World Integrated Trade Solution Database,” World Trade Organization, accessed February 27, 2022, <https://wits.worldbank.org/>.

NOTE:

U.S. UNGA voting alignment by quantile and power type, 2000-2017

Dependent Variable, Share of U.S. Vote

\*\*\*  $p < 0.01$ , \*\*  $p < 0.05$ , \*  $p < 0.1$

Robust standard errors reported in parenthesis

U.S. UNGA voting not included in regression outputs

### Findings

This study uncovered two key findings about the nature and effectiveness of modern Chinese economic statecraft. First, an increased use of Chinese financial statecraft, all else equal, is associated with a relatively low increase in the share of

Chinese UNGA voting. These measures are on average most concentrated in relative, not absolute, measures of state debt owed to China as a share of overall state GDP. While coefficient size is low, and therefore potentially of considerable cost to China, these robust findings are of strong practical policy significance. The wide variation in GDP size and debt share throughout the UNGA presents a distribution of relatively easy targets to co-opt voting through increased Chinese debt obligations.

Surprisingly, this study found no comparable trend of Chinese economic influence on U.S. voting alignment across the entire sample. While the exact pathway for relatively low impact of Chinese debt is outside the scope of this research, there are several possibilities based on the conduct of this study. First, the impact of debt could manifest below the state level of analysis, particularly among individual firms. Second, the impact of expanding Chinese debt loads could manifest most acutely above the state level, particularly among supra-national markets and governance bodies. Finally, state-level economic pressure may be an inefficient way to pressure political elites to highly observable and potentially electorally dangerous behavior change, particularly given the relative stickiness of UNGA voting over time.

The second key finding of this study is that the effectiveness of Chinese economic statecraft is highly contextual to the vulnerabilities and resiliencies of the target country. On one hand, this potentially allows China to tailor its basket of financial statecraft tools to maximize their effectiveness. This study found one group of states, based on GDP per capita, that are particularly susceptible to the synergistic effects of common Chinese economic tools. On the other hand, this process allows the U.S. to focus resources to mitigate the impact of Chinese statecraft. This study identified that, all else equal, it is the

relatively long-standing cadre of American partners that are more likely to flip voting proximity from Washington to Beijing. While this study focused primarily on sharp power financial instrument of Chinese bilateral debt stocks, other economic instruments such as bilateral trade and foreign military sales showed similar contextual patterns. Chinese bilateral trade is most impactful on middle- and high-income countries based on the yearly sub-sample, and foreign military sales are most effective among middle-income countries throughout the period of study.

Ultimately, while this study cannot make a direct causal appeal, its nuanced findings do stand in partial rebuke of multiple common narratives of Beijing's economic statecraft, particularly American framing of Debt Trap Diplomacy and Chinese claims to the Community of Common Destiny. As evidenced in trends for relative, not absolute behavior change due to Chinese economic instruments, third party states that make up the battleground in the Sino-American economic competition appear to utilize the same optimization calculus as the respective superpowers themselves. The findings suggest that blanket economic statecraft, based purely on legacy alignment or regions, could be ineffective, inefficient, and potentially counterproductive.

### Summary

Utilizing fixed effects and quantile regression estimation, this study identified the positive but highly contextual impact of Chinese economic statecraft on the international system. It also presented quantitative analysis for determinants of Chinese economic instruments and associated U.S. mitigation strategies. These findings will be the basis for future U.S. policy recommendations in the study's concluding chapter.

## CHAPTER 5

### CONCLUSIONS AND RECOMMENDATIONS

#### Introduction

This study sought to quantitatively assess the effects, determinants, and mitigation measures of Chinese economic statecraft on the U.S. and its partners and allies. It found that Chinese sharp power financial tools drove statistically significant effects on the international system. While the overall effect of Chinese debt stocks are small in magnitude, they are highly responsive to bilateral context. This chapter reviews the study's research implications, and then proceeds to translate identified quantitative trends of the Sino-American economic competition into future policy and study recommendations.

#### Research Implications

This study's core findings bear important implications on American policy. U.S. economic statecraft vis-à-vis China has been criticized as both inconsistent over time and overly homogenous across regions—a particularly insidious combination given the persistent and highly contextual impact of Chinese economic statecraft identified in this study.<sup>122</sup> Armed with additional knowledge of these bilateral economic relationships, the

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<sup>122</sup> Shambaugh's study of the Sino-American competition in Southeast Asia shows the particularly perverse effects of inconsistent and blanket U.S. policy at the regional level. See David Shambaugh, *Where Great Powers Meet: American and China in Southeast Asia* (Oxford: Oxford University Press, 2021); James Steinberg argues this ineffective style of American policy was based on the overarching assumption that a stable and prosperous China most acutely benefited American interests, and as a result prioritized it in subsequent gray zone escalatory events over both direct U.S. and regional partner interests. See Steinberg, "What Went Wrong?," 117-130.

U.S. is better postured to tailor its economic ways and means to regional and county-level dyads, thereby advancing its interest during competition, and if necessary, crisis with China. Subsequent recommendations will identify how ongoing whole-of-government efforts, such as the incipient U.S.-led Build Back Better World (B3W) and Fight Against Corruption may be best implemented to mitigate the effects of Chinese economic statecraft.<sup>123</sup>

Nonetheless, there are important limitations on this study's internal and external validity. While mitigated by this study's estimation techniques, the macroeconomic data utilized from both international institution and academia suffer from missing data which cannot be assumed to occur completely at random.<sup>124</sup> Another complication for internal validity, as explored in chapter four, is that there may be alterative mechanisms by which Chinese debt alters country-level behavior as observed in UN General Assembly voting. There are also qualifications for this study's external validity. On one hand, this study

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<sup>123</sup> Build Back Better World, or B3W, is a U.S.-led effort of the G-7 nations to fund infrastructure needs of low- and middle-income countries. See Gregory Meeks, "The Build Back Better World Partnership Could Finally Break the Belt and Road," *Foreign Policy*, June 28, 2021, <https://foreignpolicy.com/2021/06/28/the-build-back-better-world-partnership-could-finally-break-the-belt-and-road/>; In 2021, the Biden Administration named global corruption as a core United States National Security Interest and directed an interagency review for further direction and action. See U.S. President, "Memorandum on Establishing the Fight Against Corruption as a Core United States National Security Interest," (The White House, Washington, DC, June 3, 2021), <https://www.whitehouse.gov/briefing-room/presidential-actions/2021/06/03/memorandum-on-establishing-the-fight-against-corruption-as-a-core-united-states-national-security-interest/>.

<sup>124</sup> For example, it is possible missing data of direct Chinese debt was purposely misreported based on the interests of Beijing and recipient countries. The methodology of this study utilized fixed effects estimation, a series of control variables, and robust errors to purposely mitigate this risk and yield strong correlational trends.

proposes a novel adaption economic theory and international politics of neo-realism specific to the Sino-American economic competition.<sup>125</sup> On the other hand, this study's econometric modeling is highly specific to this dyadic competition, and if replicated for other bilateral time periods should be adapted accordingly.

### Recommendations

This study finds that counter to modern American foreign policy dogma, the effect of Chinese economic statecraft is highly dependent on the bilateral context, and contingent to the basket of bilateral economic resiliencies and vulnerabilities. Therefore, effective and efficient U.S. policy should vary by country dyad. In general, country and time windows that generally observe low impact from Chinese economic statecraft warrant a punishment or cost imposition strategy. In contrast, high magnitude effects necessitate an economic denial strategy. This study's recommendations are therefore broken into two sub-sections to counter Chinese economic influence: actions to deny and actions to punish.<sup>126</sup>

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<sup>125</sup> For more on the theoretical exploration of economics and international politics in the growth of neo-realism, see Abdalla Elshiekh Sidahmed, "An Economic Model for International Politics: The Question of Applicability of Microeconomic Theory to Kenneth Waltz' Theory of International Politics," (PhD diss., University of Miami, 1993).

<sup>126</sup> This study will largely adapt the definitions of Western deterrence theory, punishment and denial, to the economic instrument. Deterrence by denial holds at risk the catastrophic loss or success of an aggressor's desired objectives while deterrence by punishment raises the costs of an aggressor's actions in hopes of attenuating state behavior. See Michael Mazaar, *Understanding Deterrence* (Santa Monica, CA: RAND Corporation, 2018), 2, <https://doi.org/10.7249/PE295>.

## Components of an American Economic Denial Strategy

Economic denial tactics, such as bilateral sanctions like export and capital controls, seek to prevent Chinese market access required to facilitate economic influence.<sup>127</sup> These tools generate high direct and indirect costs, both to the deterring state and the citizenry of the aggressor state.<sup>128</sup> As a result, such measures should be circumscribed to national security priorities. This study finds that all else equal, when Chinese economic influence does impact U.S. leadership in the UNGA, it is among America's closest partners. These partners and allies, therefore, must be the core focus when the U.S. utilizes economic denial. In order to bolster U.S. attempts at coalition management, this study recommends three sub-components to any American economic denial strategy: interagency prioritization, financial regulatory reform, and partner counter-coercion inducement.

First, any U.S. economic denial strategy will require an improved interagency process to prioritize and assess intended effects. Domestic coordination is necessary to

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<sup>127</sup> For a Cold War-era economic denial considerations, see Louis Walinsky, "Coherent Defense Strategy: The Case for Economic Denial," *Foreign Affairs* 61, no. 2 (Winter 1982/1983), <https://www.foreignaffairs.com/articles/1982-12-01/coherent-defense-strategy-case-economic-denial>.

<sup>128</sup> Direct costs include the economic deadweight loss of transactions that otherwise would have occurred if not for economic coercion measures. For an estimate on the current U.S.-Chinese trade war's impact on the domestic American economy, see Pablo Fajgelbaum and Amit Khandelwal, "The Economic Impact of the US-China Trade War,") Working Paper 29315, National Bureau of Economic Research, Cambridge, MA, December 2021), [https://www.nber.org/system/files/working\\_papers/w29315/w29315.pdf](https://www.nber.org/system/files/working_papers/w29315/w29315.pdf). For more on the indirect costs, such as the unintended consequences of sanctions on target country elites and general population, see Daniel Drezner, "The United States of Sanction: The Use and Abuse of Economic Coercion," *Foreign Affairs* 100, no. 5 (September/October 2021): 142-154.

implement a disciplined differentiation of bilateral economic statecraft based on the contextual impact of Chinese influence. Currently, American economic instruments are dispersed throughout its interagency departments, decentralizing its unified projection and limiting overall unity of effort.<sup>129</sup> Further, unlike other communities in the U.S. government, there is no standing interagency process to publish reoccurring national economic statecraft strategy documents.<sup>130</sup> At a minimum, the U.S. requires a reoccurring National Defense Strategy-style document to guide the application of economic power.<sup>131</sup> That same body should also define and prioritize countering authoritarian influence (CAI) alongside counter financing of terrorism (CFT), as it has since the 9/11 attacks, to properly pivot and assess interagency progress.<sup>132</sup> Finally, this interagency vehicle should also establish screening criteria for the implementation, assessment, and discontinuation of economic denial tactics, especially negative sanctions, to maximize the intended

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<sup>129</sup> U.S. economic statecraft lacks both vertical integration with jurisdiction spread across multiple agencies and absent consistent horizontal integration of purpose on specific geopolitical challenges. See McCormick et al., “Economic Might, National Security and the Future of American Statecraft,” 20-22; For more on the problem of unity of effort within U.S. nonmilitary way of war at large, see Andrew Armstrong, “Challenges to Coordinating the Instruments of National Power,” (Master’s thesis, Johns Hopkins University, 2019), 28.

<sup>130</sup> Drezner, “The United States of Sanctions,” 152.

<sup>131</sup> Ibid.

<sup>132</sup> Josh Rudolph and Thomas Morley, *Covert Foreign Money: Financial Loopholes Exploited By Authoritarians to Fund Political Interference in Democracies* (Washington, DC: Alliance for Securing Democracy, August 2020), 61, <https://securingdemocracy.gmfus.org/covert-foreign-money/>.

coercive effect.<sup>133</sup> Such standardization would serve as an diplomatic and economic signal to private sector firms, domestic American politicians, and potential state aggressors alike of necessary U.S. economic coercion triggers.<sup>134</sup> Improved domestic coordination would also enable the interagency with a disciplined process by which it can differentiate bilateral economic statecraft

A second sub-component of any U.S. economic denial strategy is financial regulatory reform to prevent malign Chinese economic influence within the most vulnerable aspects of American financial markets. Most malign economic influence within the greater global financial system occurs through completely licit channels,

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<sup>133</sup> As an example, in Lin et al.'s study of Chinese gray zone tactics, they assess proper screening criteria for U.S. nonmilitary action would be the extent to which Chinese tactics undermine U.S. policy objectives, the difficulty of U.S. allies and partners to counter Chinese tactics, and how widely Chinese uses the coercive tactic. See Bonny Lin, Cristina Garafola, Bruce McClintock, Jonah Blank, Jeffrey Hornung, Karen Schwindt, Jennifer Moroney, Paul Orner, Dennis Borrman, Sarah Denton, and Jason Chambers, *Competition in the Gray Zone: Countering China's Coercion Against U.S. Allies and Partners in the Indo-Pacific* (Santa Monica CA: RAND Corporation, 2022), 170-175.

<sup>134</sup> This lack of standardization currently clouds U.S. sanction policy and its intended deterrent or compellent effects. Lack of diplomatic clarity generates uncertainty for private firms to enter or return to regions targeted by US economic coercion. For implications on firm level incentives, see Drezner, "The United States of Sanctions," 152-154. For implications on state deterrence, see Edward Fishman, "How to Fix America's Failing Sanctions Policy," *Lawfare* (blog), last modified June 4, 2020, <https://www.lawfareblog.com/how-fix-americas-failing-sanctions-policy#>. For implications of domestic political actor discipline using the example of the U.S. Senate, see Baogang Guo, "Sino-U.S. Decoupling: The Roles of U.S. Congress," *Journal of Chinese Political Science* 2 (August 2021): 543-565, <https://doi.org/10.1007/s11366-021-09752-5>; To see these implications broadly across 20th century application of sanctions, see Gary Hufbauer, Jeffrey Schott, Kimberly Elliot, and Barbara Oegg, *Economic Sanctions Reconsidered*, 3rd ed. (Washington, DC: Peterson Institute for Economics, 2009).

exploiting transparency and accountability loopholes in state and interstate law.<sup>135</sup> As the preeminent global hub for international finance, U.S. financial regulation plays a key role in the vulnerability and resiliency of American partners and allies.<sup>136</sup> The U.S. can take a series of legislative and executive acts to increase the resiliency of its financial system and deny any possible Chinese manipulation. For instance, it can cut legacy U.S. Patriot Act money laundering exceptions for real estate and luxury transport dealers, prioritize implementation of §885 of the 2021 National Defense Authorization Act requiring beneficial ownership reporting for federal acquisition, and pass the ENABLERS Act to bolster transparency requirements to U.S. legal, real estate, and accounting firms.<sup>137</sup> The U.S. should also ban Chinese Variable Interest Entities (VIEs), opaque Chinese investment vehicles designed to allow Chinese firms to circumvent Beijing to access Western capital.<sup>138</sup> VIEs, based on their lack of transparency, induce great financial and security risk to both Western individual and state investors.<sup>139</sup>

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<sup>135</sup> Rudolph and Morley, *Covert Foreign Money*, 10.

<sup>136</sup> Farrell and Newman, “Weaponized Interdependence,” 42-79.

<sup>137</sup> Jodi Vittori, “Biden Must Go Beyond Sanctions to Rid the U.S. Financial System of Dirty Money,” (Carnegie Endowment for International Peace, Washington, DC, March 8, 2022), <https://carnegieendowment.org/2022/03/08/biden-must-go-beyond-sanctions-to-rid-u.s.-financial-system-of-dirty-money-pub-86589>.

<sup>138</sup> Chinese firms circumvent national capital control requirements through offshore companies that gain access to Western credit markets without the required beneficial ownership information. See U.S. Congress, *2021 Report to Congress of the US-China Economic and Security Review Commission*, 117th Cong., 1st sess. (Washington, DC: US Government Printing Office, November 2021), 241-245.

<sup>139</sup> Coppola et al. find that the complicated legal structure of Chinese VIEs significantly degrades the market forces to properly evaluation underlying Chinese assets, resulting in a significant overstatement of Chinese assets within Wester markets in excess

A final sub-component of American economic denial is to establish buffers for partners and allies to withstand Chinese economic influence. Economic inducements, also known as positive sanctions, are powerful, yet often overlooked tools of influence.<sup>140</sup> Many individual actions could build a holistic buffer for American partners and allies from Chinese economic influence. For instance, the U.S. can prioritize and incentivize American investment toward lasting trade, technology, and infrastructure needs of its closest partners, denying access to Chinese firms.<sup>141</sup> It can also support a counter-coercion fund to support like-minded nations hardest hit by explicit and implicit economic pressure from Beijing.<sup>142</sup> In total, these actions strengthen the resiliencies of

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of one trillion USD. See Antonion Coppola, Matteo Maggiori, Brent Neiman, Jesse Schreger, “Redrawing the Map of Global Capital Flows: The Role of Cross-Board Financing and Tax Havens,” *The Quarterly Journal of Economics* 136, no. 3 (August 2021): 1499-1556.

<sup>140</sup> In the historical development of sanctions, positive inducements such as trade, investment, or aid agreements were originally seen the most powerful form of sanction. This has increasingly fallen out of foreign policy lexicon in the post-Cold War era. See Nicholas Mulder, *The Economic Weapon: The Rise of Sanctions as a Tool of Modern War* (New Haven: Yale University Press, 2022), 8-23.

<sup>141</sup> The U.S. has numerous positive economic inducements that can serve as low-cost policy choices, such as bilateral investment treaties or relaxed export licensing, to support critical sectors of partner countries. For nonmilitary trade and investment recommendations, see Matthew Kroenig and Jeffrey Cimmino, “Global Strategy 2021: An Allied Strategy for China,” (Atlantic Council, Washington, DC, 2020), 52, <https://www.atlanticcouncil.org/global-strategy-2021-an-allied-strategy-for-china/>. For military-based trade and investment see Lin et al. findings on future U.S. Security Cooperation. See Lin et al., *Competition in the Gray Zone*, 170-175.

<sup>142</sup> Australia is one nation currently facing extensive direct and indirect Chinese economic pressure. Darren Lim, Zack Cooper, and Ashley Feng, *Trust and Diversity: Geoeconomic Strategy for the Australia-US Alliance* (Sydney, Australia: United States Studies Centre, University of Sydney, September 2021), 21, <https://www.ussc.edu.au/analysis/trust-and-diversify-a-geoeconomic-strategy-for-the-australia-us-alliance>.

the core group of states that underwrite American-led rules-based system, and proactively deny sources of Chinese influence among those most quantitatively susceptible Beijing's interests vis-à-vis the United States.

### Components of an American Economic Punishment Strategy

While this study's findings warrant a small subset of American economic statecraft devoted toward denial, its evidence overwhelmingly supports economic punishment strategy as well. This study found that Chinese influence is most cost effective among low and middle-income nations, particularly of the Global South, but did not generate a parallel erosion of U.S. influence. As a result, this subset of states represent an area of steady cost imposition. These quantitative trends generally reflect Beijing's larger behavioral patterns. In pursuit of its national interests, Beijing appears to willingly trade-off short-run inefficiency for perceived long-run effect.<sup>143</sup> In order to raise the costs of Chinese economic influence within the developing world, this study recommends two sub-components of any American economic punishment strategy: opportunistic competition and attributional suasion.

One necessary component of an American economic punishment strategy is to guide U.S. private industry in competition with China in the developing world. U.S.-led economic alternatives seek to raise the costs of Chinese influence through regional market forces. First, U.S. firms must be able to free-ride off Chinese investments in the developing world, particularly its infrastructure spending, thereby lowering American fixed and variable costs of business operations. This is important in former colonies of

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<sup>143</sup> Economy, *The Third Revolution*, 15, 233.

the Global South, where legacy emphasis on coastal infrastructure creates barriers to market entry for U.S. firms today.<sup>144</sup> This type of visible economic competition provides persistent cultural contact between the United States and the developing world.<sup>145</sup> Also, U.S. firms and institutions must be able to exploit market gaps and credibility of Western technology and finance.<sup>146</sup> The COVID-19 pandemic has placed critical strain on developing world energy access and debt obligations.<sup>147</sup> If U.S.-led firms and institutions cannot provide competitive financing solutions, it risks further displacement by Chinese

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<sup>144</sup> This legacy of colonialism creates large market advantages for physical capital in port areas, such as those in the Chinese BRI. Infrastructure development of post-colonial governments focused almost entirely on maximizing exports in support of European mercantilist models. As a result, many regional markets today are still highly reliant on trade infrastructure centered on rail and road connecting raw materials to deep water ports rather than interstate infrastructure between developing states. For one such study on the path dependencies and associated market barriers from legacy colonial infrastructure, see Remi Jedwab and Alexander Moradi, “Colonial Investments and African Development: Evidence from Ghanaian Railways,” (Center for Economic Policy Research, Washington, DC, June 2021), [https://cepr.org/sites/default/files/meets/789/papers/Jedwab\\_Moradi\\_latest.pdf](https://cepr.org/sites/default/files/meets/789/papers/Jedwab_Moradi_latest.pdf).

<sup>145</sup> Joseph Nye, “Soft Power,” *Foreign Policy* no.80 (Autumn 1990): 153-171.

<sup>146</sup> One example of Western technological advantage in the developing world is through green energy transition, see Ulrich Volz, Shamshad Akhtar, Kevin Gallagher, Stephany Griffith-Jones, and Jorg Haas, *Debt Relief for a Green and Inclusive Recovery: A Proposal* (Boston, MA: Global Development Policy Center, Boston University, November 2020), <https://drgr.org/files/2021/01/DRGR-report.pdf>; For more on how developing world leaders utilize Western finance credibility to bolster their political survival, see Andreas Kern, Bernhard Reinsberg, and Patrick Shea, “IMF Programs, Chinese Lending, and the Political Economy of Leader Survival,” (Working Paper 118, AidData, College of William & Mary, Williamsburg, VA, March 10, 2022), 1-5.

<sup>147</sup> Ying Qian, “Brady Bonds and the Potential for Debt Restructuring in the Post-Pandemic Era,” (Global Development Policy Center, Boston, MA, September 2021), 13-18, [https://www.bu.edu/gdp/files/2021/09/GCI\\_WP\\_018\\_FIN.pdf](https://www.bu.edu/gdp/files/2021/09/GCI_WP_018_FIN.pdf).

equity and currency arrangements.<sup>148</sup> This necessary economic competition will require discipline from the U.S. government. For instance, private firms may require positive inducements such as diplomatic and economic clarity and safeguards for Western firms entry into Chinese-dominated markets.<sup>149</sup> U.S. discipline also entails avoiding costly subsidies and any degradation of financial transparency standards that undercut the very competitiveness of U.S. firms.<sup>150</sup>

Another portion of any economic punishment strategy is to apply suasion against attributable Chinese coercion. Suasion raises Chinese costs by publicly attributing harmful Chinese action, popularly referred to as “naming and shaming.” Attribution is difficult because Chinese economic coercion often manipulates the threshold of

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<sup>148</sup> In particular, Chinese efforts to implement the “Shanghai Model” of sovereign debt restructuring threatens to replace Western “Brady” restructuring plans that have been popular in mitigating debt crisis since the 1990s. The Shanghai Model would effectively generate Brady-like refinancing bonds to mitigate credit risk, but exclusively through Chinese currency and banking systems. See Ying Qian and Yan Wang, “Reflections on Sovereign Debt Restructuring in Low-Income Countries and the ‘Shanghai Model,’” (Global Development Policy Center, Boston, MA, January 30, 2022), <https://www.bu.edu/gdp/2022/01/30/reflections-on-sovereign-debt-restructuring-in-low-income-countries-and-the-shanghai-model/>. This system is growing in favor in light of the stalled G-20 “Common Framework,” an agreement of public-private finance partnership to selectively relieve debt burdens on developing world during the COVID-19 pandemic. See Masood Ahmed and Hannah Brown, “Fix the Common Framework for Debt Before its Too Late,” *Center for Global Development* (blog), January 18, 2022, <https://www.cgdev.org/blog/fix-common-framework-debt-it-too-late>.

<sup>149</sup> Drezner, “The United States of Sanctions,” 152-154.

<sup>150</sup> Scott Morris, “China’s Role in Developing Countries: Resetting US Policy with a ‘3C’s’ Agenda,” (Center for Global Development, Washington, DC, December 2020), 1-7, <https://www.cgdev.org/sites/default/files/chinas-role-in-developing-countries.pdf>.

ambiguous action and response.<sup>151</sup> The U.S. must build an attribution mechanism among like-minded nations facing the shadow of Chinese economic coercion, including leading developing nations such as India, on Chinese economic influence.<sup>152</sup> Next, the U.S. must build procedures to deliver these shared assessments. This entails the careful integration and declassification of various forms of intelligence into actionable products, and then the active cooperation and distribution through various formal and informal channels to target audiences in the developing world.<sup>153</sup> Finally, the U.S. must utilize this informed suasion to adapt its diplomatic narratives with respect to the agency of the third world in its engagement with China. Narratives such as autocracy versus democracy, for instance, tend to alienate other cultures and undercut intended American effects.<sup>154</sup> In

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<sup>151</sup> Kilcullen refers to this style of coercion as part of larger liminal warfare techniques. See David Kilcullen, *The Dragons and the Snakes: How the Rest Learned to Fight the West* (New York: Oxford University Press, 2022), 150-156.

<sup>152</sup> The Group of Seven Nations (G-7), the economic organization of world advanced economies, or the Quadrilateral Security Dialogue (U.S., Australia, India, and Japan) represent possible standing bodies to host an interstate attribution process. For more on interstate attribution, see Lim et al., *Trust and Diversity*, 21-22.

<sup>153</sup> The U.S.-led effort to declassify intelligence to shape the diplomatic environment prior to the 2022 Russian invasion of Ukraine represents one model of information-based moral suasion for gray zone aggression. For more on this conceptual process, see Lindsey Sheppard and Matthew Conklin, “Warning for the Gray Zone: By Other Means Part II, Adapting to Compete in the Gray Zone,” (Center for Strategic and International Studies, Washington, DC, August 13, 2019), <https://www.csis.org/analysis/warning-gray-zone>.

<sup>154</sup> Baogang He, “Biden’s Misguided Framing of US-China Rivalry as Democracy Versus Autocracy,” *East Asia Forum*, December 7, 2021, <https://www.eastasiaforum.org/2021/12/07/bidens-misguided-framing-of-us-china-rivalry-as-democracy-versus-autocracy/>; For more on how cultural misunderstandings attenuate the value of conditionality and suasion on developing nations, see Raymond Fisman and Edward Miguel, *Economic Gangsters: Corruption, Violence, and the Poverty of Nations* (Princeton, NJ: Princeton University Press, 2008), 186-206.

implementing this economic punishment strategy, the U.S. may increase Beijing's anticipated costs relative to its anticipated benefits of any economic coercion, attenuating its behavior as a result.

Together, this bifurcated policy paradigm of selective denial and steady punishment seeks to capitalize on the enduring but highly contextual impact of Chinese economic influence. The U.S. may find comparative advantage in its competition with China in a more effective and efficient application of economic statecraft by reorienting its policy accordingly.

### Future Research

This project primes several areas for future study. For instance, this study's core focus, on the political-economy of sharp power financial instruments, serves as just one component of a larger Chinese center of gravity analysis. Future research may assess other critical requirements of the Chinese economy, such as its SOEs or capital controls. A similar economic center of gravity analysis could assess the impact of US economic tools. For example, there are clear gaps on the outcomes of U.S. foreign military sales over time. Finally, while this study took a state-level approach to assess economic influence, additional study is needed to assess the pathways of financial risk in the global financial system, particularly at the firm, regional, and supranational levels.

### Conclusion

For decades, the United States has disproportionately benefited from an economic system designed to facilitate its economic ends, ways, and means. Cold War historian Hal Brands asserts that America's creation and manipulation of nonmilitary tools and

institutions post-1945, such as Bretton Woods, is “...history’s most successful milieu strategy.”<sup>155</sup> Over this time, America’s global economic hegemony not only resourced its instruments of power, but also established a system that modified the geopolitical environment of any potential adversary, thereby thwarting aggressor goals. However, today’s modern Sino-American competition has upended this advantage. As the U.S. now appears locked into another long struggle of influence, the most important task is to understand. This study’s econometric analysis reveals a highly contextual impact of bilateral Chinese economic influence, and as a result, extends a bifurcated policy prescription of economic denial and punishment. In doing so, the U.S. may find that the best remedy to counter its latest great power rival is to leverage Chinese techniques against it.

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<sup>155</sup> Hal Brands, *The Twilight Struggle: What the Cold War Teaches Us About Great Power Rivalry Today* (New Haven: Yale University Press, 2022), 30-47.

## APPENDIX A

### TABLES

Table 4. Variable Description

Variable	Source	Description	Notes
U.S. Voting Alignment	Bailey et al.	Annual proportion aligned to U.S. UNGA votes	Abstain is half value yay and nay
China Voting Alignment	Bailey et al.	Annual proportion aligned to U.S. UNGA votes	Abstain is half value yay and nay
Chinese Bilateral Trade	WITS	Total bilateral exports from China to recipient country	USD
Chinese Foreign Military Sales	SIPRI	Annual weapons sales from China	USD
Bilateral FMS as Share of Military Expenditures	SIPRI	Annual weapons sales from China / Annual national military expenditures	USD
Chinese Bilateral Debt	Horn et al.	External debt stock owed to China	USD
Chinese Bilateral Debt Share	Horn et al.	External debt stock owed to China/country GDP	USD
GDP per Capita	World Bank	Annual GDP per capita	USD
Regime Similarity	Freedom House	Measure of state democratic practice	Scale 0-10
Military Capability	COW	Composite Index of National Capability	Scale 0-1
Policy Preferences	Bailey et al.	State Ideal Point UNGA estimator lagged one year	
Steel Production	COW	Total Production of Crude Steel	Thousands of tons
Natural Resource Reliance	World Bank	Total resources rents as share of GDP	
Net Energy Consumption	COW	Primary Energy Consumption (Production + Import -Export)	Thousands of coal-tons

*Source:* Created by author using Michael Bailey, Anton Strezhnev, and Erik Voeten. “Estimating Dynamic State Preferences from United Nations Voting Data,” *Journal of Conflict Resolution* 61, no. 2 (2017): 430-456, <https://doi.org/10.1177/0022002715595700>; Sebastian Horn, Carmen Reinhart, and Christoph Trebesch, “China’s Overseas Lending,” (Working Paper 26050. National Bureau of Economic Research, Cambridge, MA, May 2020), <https://doi.org/10.3386/w26050>; “SIPRI Arms Industry Database,” Stockholm International Peace Research Institute, accessed January 28, 2022, <https://www.sipri.org/databases/armsindustry>; “World Integrated Trade Solution Database,” World Trade Organization, accessed February 27, 2022, <https://wits.worldbank.org/>.

Table 5. Summary Statistics

Country Characteristic	Mean	SD	Min	Max	Median	N
UNGA Voting						
Agree U.S. Vote	0.301	0.271	0	1	0.236	3625
Agree Chinese Vote	0.723	0.017	0	1	0.772	3625
Ideal Point	-0.077	0.872	-2.14	2.94	-0.354	3625
Soft Power						
Bilateral Chinese Import (USD, LN)	20.015	2.617	10.294	26.896	20.256	3498
Bilateral Chinese Import Share	0.115	1.749	0.0001	93.458	0.021	3427
Sharp Power						
Chinese Bilateral Debt (USD, LN)	19.416	2.244	1.816	24.344	19.634	1367
Chinese Bilateral Debt Share	3.704	7.899	0	113.021	0.587	1909
Hard Power						
Bilateral Foreign Mil Sales (USD, LN)	16.707	1.589	13.816	20.444	16.732	340
Bilateral Foreign Mili Sales Share	0.054	0.108	0	0.738	0.013	313
Controls						
GDP Per Capita	12730.83	21.385.32	111.927	189170.9	4103.70	3569
Net Energy Consumption (coal-tons)	6665.689	411754.80	0	59000331	7645	3257
Steel Production (thousands of tons)	98121.65	42625.62	0	822698	0	3257
Resource Rent Share of GDP	8.389	12.741	0	86.452	2.31	3347
Freedom House Level of Democracy	6.26	3.11	0	10	0.001	2899
Military Capability	0.005	0.019	0	0.231	7.083	3257

*Source:* Created by author using Michael Bailey, Anton Strezhnev, and Erik Voeten. “Estimating Dynamic State Preferences from United Nations Voting Data,” *Journal of Conflict Resolution* 61, no. 2 (2017): 430-456, <https://doi.org/10.1177/0022002715595700>; Sebastian Horn, Carmen Reinhart, and Christoph Trebesch, “China’s Overseas Lending,” (Working Paper 26050. National Bureau of Economic Research, Cambridge, MA, May 2020), <https://doi.org/10.3386/w26050>; “SIPRI Arms Industry Database,” Stockholm International Peace Research Institute, accessed January 28, 2022, <https://www.sipri.org/databases/armsindustry>; “World Integrated Trade Solution Database,” World Trade Organization, accessed February 27, 2022, <https://wits.worldbank.org/>.

## NOTE:

UN General Assembly members voting and power characteristics, 2000-2018

N countries = 193; N years = 19; N country years = 3625.

All current year U.S. Dollars

Data compiled from various sources, see Table 1 for variable description and sources

Table 6. Bivariate Correlations

	Agree U.S.	Agree China	Bilat Import	Bilat Import Share	Bilateral Debt	Bilat Debt Share	Bilateral Mil Sales	Bilat Mil Sales Share
Agree U.S. Vote	1							
Agree China Vote	-0.323	1						
Bilateral Import	-0.017	0.227	1					
Bilateral Import Share	-0.048	0.244	0.083	1				
Bilateral Debt	-0.203	0.063	0.422	-0.024	1			
Bilateral Debt Share	0.116	0.092	-0.271	0.473	0.440	1		
Bilateral Military Sales	0.033	0.037	0.294	0.076	0.259	-0.151	1	
Bilateral Military Sales Share	0.071	0.021	-0.247	0.315	0.024	0.451	0.222	1

*Source:* Created by author using Michael Bailey, Anton Strezhnev, and Erik Voeten. “Estimating Dynamic State Preferences from United Nations Voting Data,” *Journal of Conflict Resolution* 61, no. 2 (2017): 430-456, <https://doi.org/10.1177/0022002715595700>; Sebastian Horn, Carmen Reinhart, and Christoph Trebesch, “China’s Overseas Lending,” (Working Paper 26050. National Bureau of Economic Research, Cambridge, MA, May 2020), <https://doi.org/10.3386/w26050>; “SIPRI Arms Industry Database,” Stockholm International Peace Research Institute, accessed January 28, 2022, <https://www.sipri.org/databases/armsindustry>; “World Integrated Trade Solution Database,” World Trade Organization, accessed February 27, 2022, <https://wits.worldbank.org/>.

NOTE: UN General Assembly Members voting and power characteristics, 2000-2018

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