

What does the COVID-19 crisis tell us about China?

Understanding the Chinese superpower

The impact on China's small and medium-sized firms

Sarah Kirchberger

[EURICS fellow, spring 2020]

Sarah Kirchberger is the head of Asia-Pacific strategy and security at the *Institute for Security Policy at Kiel University* (ISPK). She was previously an assistant professor of contemporary China studies at Hamburg University and a senior research associate at the Ruhr-University Bochum's Section for International Political Economy of East Asia. Between 2007–2010 she served as a naval analyst with shipbuilder TKMS, Hamburg. She is currently working on China's naval and space development, China's defence economy and China-Russia relations. She is the author of *Assessing China's Naval Power: Technological Innovation, Economic Constraints, and Strategic Implications* (2015).



Kirchberg ©Delany2020

WHAT HAVE WE LEARNED ABOUT CHINA'S SUPERPOWER STATUS?

Long before the spread of the pandemic across the globe began, the emergence of great power rivalry between the USA and China and the prospect of a "Cold War 2.0" had dominated discussions in Western security circles. President Trump's trade war policy and industrial decoupling strategy took a heavy toll on China's national economy, which had begun to register its slowest growth in decades. US sanctions against Chinese tech firms, especially Huawei, had begun to disrupt global supply chains, foreign investment, and trade flows.

In meetings with European and Asia-Pacific counterparts, US officials missed no opportunity to point out to allied nations how trusting Huawei with critical infrastructure development would risk fracturing the alliance. They were also highlighting all the ways in which China's increasingly assertive activity in the South China Sea, the East China Sea and in the vicinity of Taiwan was adding to the risk of confrontation.

Only recently, a war of words over culpability and over China's role in the World Health Organization (WHO) erupted, leading to the drastic step by the US government to freeze its financial contributions to that organization—in the middle of an ongoing pandemic. The backdrop to the health crisis we are experiencing remains the rivalry between China and the United States.

Strengths highlighted by this health crisis

When the outbreak was still confined to Hubei province, some observers expected it to become something of a "Chernobyl moment" for the Chinese Communist Party (CCP)—**a nail in the coffin of an already strained authoritarian government that was struggling to deal with the combined fallout of the trade war, slow economic growth, and rising internal criticism of Xi Jinping's economic strategy.** But as the fight against the epidemic within

.....

The pandemic has created a unique opportunity for China to gather detailed and accurate information on every affected democratic country's political system performance, economic strength, emergency preparedness, and societal resilience.

.....

strengthening its outreach into particular regions (such as Italy), while using every opportunity to shape the narrative and recast China's role from the outbreak epicentre to valuable partner in dire times.

Weaknesses underlined by the outbreak

The initial perception that only China could organize a draconic lockdown quickly dissipated. Many democratic countries adopted various types of lockdown measures of their own consensually and democratically, and even achieved high levels of voluntary compliance among their populaces. Other democratic countries have even been able to contain the outbreak without lockdowns by using more sophisticated tools. In particular, the evidence began to highlight the comparatively much more successful containment strategy employed by Taiwan. Information warfare orchestrated by Chinese internet trolls posing as racist Taiwanese attacking the WHO leadership indicates how serious the threat of the "Taiwan model of containment" is from Beijing's perspective.

Furthermore, the early stage of the health crisis highlighted a key weakness of the Chinese political system: the lack of information freedom. With hindsight it is clear that a decisive factor that enabled the outbreak to get out of control in the first place was the initial suppression of relevant information about the virus by the local authorities, especially regarding its capability for direct human-to-human transmission. Despite credible evidence that local Chinese researchers and doctors knew already in December 2019 what they were dealing with, at a time when Taiwanese researchers had come to the same conclusions, this information was withheld from the WHO and suppressed within China. Whistleblowers were pressured and silenced.

When comparing successful strategies in other Asian countries and Europe (South Korea, Taiwan, Singapore, Japan, Germany, Switzerland, or Norway), accurate and timely

China progressed, some Western observers began to laud the efforts of Chinese authorities to contain the outbreak. Many doubted that a similar level of control would be achievable within a democratic country. As the pandemic expanded outward, China quickly switched gears and began to offer support in terms of medical supplies and expertise to other stricken countries. In doing so, it was

information about cases and infection channels is key for the successful containment of an exponentially spreading pathogen.

In China, between the end of December and mid-February, hundreds of virus-related keywords and messages containing them were banned from WeChat, the country's most widely used instant messaging service (University of Toronto study). Whistleblowers were silenced. Lack of transparency, absence of press freedom and tight information controls in China have proven an unholy combination that enabled the pandemic to spread quickly within Wuhan and from there across the world, when 5 million people were allowed to leave the area before a lockdown was imposed. Within China, numerous critics have come forward despite the personal risk to them. They point out this massive failure and demand information freedom. So far the Chinese authorities' reaction indicates that as before, citizens who criticize the government's response and challenge its narrative will be persecuted and silenced. The posthumous rehabilitation of the tragically deceased whistleblower physician Dr. Li Wenliang is not a valid counterexample: it should be seen as a damage-control measure that came late after Li had already turned into a martyr figure in the eyes of many Chinese.

Had China's government employed its pervasive surveillance capabilities in time for containing the initial outbreak, and had China succeeded, this might have created an opportunity for China to tout the merits of its governance model to other nations more convincingly. **But as it stands, China's government not only opted to focus on information control, but also began an information warfare campaign towards the outside world for deflecting blame and shaping the narrative. Nonetheless, blunders defined the early Chinese government response to the outbreak, at a time when it mattered the most. It is hard to see how these primary choices made by the CCP leadership could make China's surveillance state approach seem attractive as a model.** The Asian democracies have overall fared far better, and so have some countries in Europe such as Germany that early on opted for maximum testing, screening, contact tracing, and transparency.

What opportunities does the pandemic create?

Once spread across the globe, **the pandemic turned into a real-time stress test for every affected country, in particular in terms of state preparedness and capacity.** This has created a unique opportunity for China to gather detailed and accurate information on every affected democratic country's political system performance, economic strength, emergency preparedness, and societal resilience. This type of insight is in itself extremely valuable to strategists within the security, diplomacy, and economic spheres alike. The knowledge thus gained can be exploited in various means, for economic gain, for devising political and diplomatic strategies, for strategic investments in industries under

duress, and also for military purposes. Precisely for this reason, on their part authoritarian countries such as Russia, China, or North Korea do not release a comparable amount of data into the public sphere. Though, they still benefit from the data coming out of other countries. Therefore, the pandemic has created an asymmetrical opportunity to analyse democratic and authoritarian systems under stress.

It also has military security implications. **Many countries' military readiness levels will be affected by the pandemic for some time to come, likely until a vaccine becomes finally available.** Outbreaks among the crews of warships have impacted on the readiness of strategic weapon systems in several nations already, including the US (with at least two aircraft carriers in the Pacific contending with outbreaks on board); France (whose only carrier had to abort its mission because of an outbreak) and Russia.

China's recent claim that there have been zero infections among the People's Liberation Army (PLA) is hardly credible. Wuhan is the site of numerous military installations and many PLA medics have been deployed to help fight the outbreak... The military readiness of authoritarian countries including China and North Korea (another country that claims to have no infected soldiers) can be expected to be likewise affected, even if data on that remains classified.

China has also used the distraction of the international community, which is preoccupied with the pandemic, to step up threatening military moves against Taiwan in the form of fighter jet patrols and naval exercises. It also sank a Vietnamese fishing vessel near the Paracel Islands in the South China Sea. Either these moves are directed inward and intended to signal strength at a time of domestic crisis in China, or the intention is to use an opportunity to enlarge China's scope of action, e.g., against Taiwan. In any case the US has taken care to signal its concerns and warned against such a course of action.

The pandemic has also created an opportunity for China to exercise pressure on international organizations, especially the WHO. During the early phase of the pandemic, this seemed to pay off. The WHO resisted calls to label the outbreak a "pandemic" for surprisingly long and criticized countries that early decided upon travel restrictions against China, even though such restrictions later had to be adopted on an almost universal scale. Much more worrisome, WHO functionaries fully complied with Chinese demands to ignore information provided by Taiwan (which had warned the WHO already in December of human-to-human transmission) and not to endorse Taiwan's successful measures of containment.

Threats spotlighted by the pandemic

Early Chinese government attempts to suppress information on the outbreak of a new coronavirus indicate that **the epidemic was foremost seen as a localized threat to CCP**

rule. This analysis was done despite the previous experience with the SARS outbreak. China had unique abilities to monitor its population that are not available in democratic countries and also had the capacity to impose a strict lockdown, but these tools were not used in time to contain the outbreak within Wuhan.

Rather, the administration opted for a delayed response, allowing millions of people to leave Wuhan, while enforcing strict control over the information sphere. **This choice illustrates the priorities of the leadership: fighting the epidemic came second, controlling the narrative was paramount.** This strategy did not even succeed fully within China, certainly not in Wuhan where angry residents have voiced hitherto unknown levels of criticism and protest.

After the pandemic spread to other countries, China's leaders not only jumped at the opportunity to deflect blame, some officials even resorted to spreading conspiracy theories that the virus might have been planted in China by the US military. At the same time, the party-controlled media began pointing to the supposed "superiority" of the Chinese containment measures compared to the delayed, and in some cases less than successful, responses in other countries (most of all heavily stricken Italy, Spain, and France). This narrative was not generally well received in Western countries, and has led to a backlash.

What does all this tell us about China as a superpower?

At the Munich Security Conference last February, when quizzed by the host what China on its part could do to improve its increasingly strained relationship with the USA, Foreign Minister Wang Yi retorted that "All these accusations against China are lies, not based on facts. But if we replace the subject of the lie from China to America, maybe those lies become facts." Before this health crisis, Chinese officials had done little to alleviate the sense of a deepening rift between China and the US. In that respect, State-led obfuscation of the outbreak and attempts to shift the blame for it to the US seem to mark a continuity.

Such an attitude signals to Europeans that sitting on the fence between China and the US in all the various issues under contention may not remain a feasible strategy much longer. **While the coronavirus outbreak might not tell us much about China's prospects of becoming a superpower in the future, it does apprise us a lot about the nature and priorities of the PRC's political system. It also starkly highlights the dangers that ensue when the entire world depends on state-controlled information flows and supplies of critical goods and equipment from China.**

To go further

Read **Sarah Kirchberger's** article in French and English and turn to additional references on **eurics.eu**

Xiaobo Zhang

[EURICS Fellow, spring 2020]

COVID-19'S IMPACT ON CHINA'S SMALL AND MEDIUM-SIZED FIRMS

Business activity in the world's second-largest economy grounded to a halt for about two months because of COVID-19. China's GDP declined by 6.8% in the first quarter of 2020 compared to the first three months of 2019. It is the first time the country reports a contraction in its economy since it began publishing quarterly results in 1992. China's small and medium enterprises (SMEs), which generate 90% of employment, constitute 80% of exports, and account for 70% of GDP, have been hit particularly hard.

To gauge the impact of COVID-19 on SMEs, in early February 2020, the Enterprise Survey for Innovation and Entrepreneurship in China (ESIEC) team, led by Peking University, did a follow-up survey of 2,349 previously sampled SMEs in seven provinces, which are largely representative at the provincial level and the major industrial level for China as a whole. The survey asked about the resumption of production, as well the different challenges enterprises face.

How long can the firms' current cash flow sustain the firms' survival?

Fourteen percent of surveyed firms would be unable to last beyond a month on a cash flow basis, and 50% would close down after three months. At the end of March 2020, after two months of lockdowns, quarantine rules and travel restrictions, life was slowly returning to normal in China. Activity is gradually resuming, but throughout the country, barriers to business

operations remain numerous: labour shortages, supply chain challenges (e.g., parts manufactured in provinces where factories are still closed), declining consumer demand, and cancellation of orders from international buyers, etc. SMEs are struggling to survive.

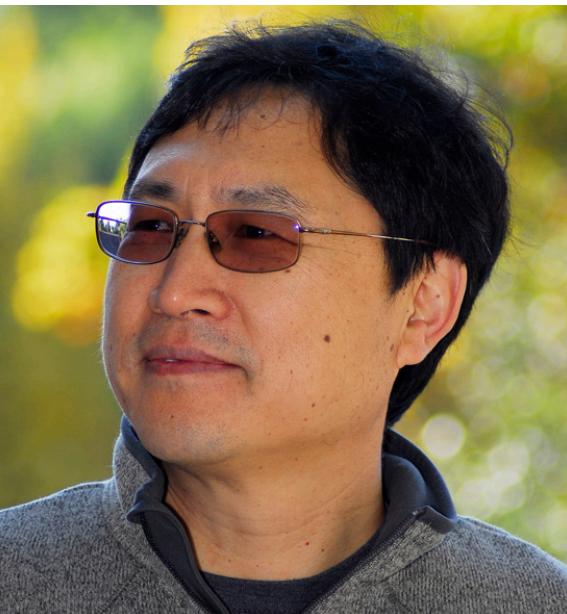
Xiaobo Zhang is a distinguished chair professor of economics at the *National School of Development*, Peking University in China, and Senior research fellow of IFPRI (Washington DC). Chief Editor of *China Economic Review*, he received the prestigious Sun Yefang Prize for Economics Research in China and Zhang Peigang Award in the field of development economics. He has rich field experience in developing countries (China, Bangladesh, Egypt, Ethiopia, India, and Myanmar). He is the principal investigator (PI) of Enterprise Survey for Entrepreneurship and Innovation in China (ESEIC).

Even in provinces such as Gansu, where the impact of the epidemic was relatively limited, by mid-February the work resumption rate stood at only 16%. In order to control the spread of the disease, many Chinese villages were locked down, thus increasing tremendously the logistical cost for businesses in remote areas. In February, a beekeeper in Sichuan province committed suicide after his bees starved to death as local travel restrictions had made it impossible to buy food for the colony or relocate it to an area where they could feed naturally.

A large heterogeneity of impact across sectors

Export firms suffered more than others. They rely only on a few suppliers, so they faced a higher risk of supply disruption: if a supplier failed to deliver the order on time, it would be hard for the firm to find a replacement in short time. Furthermore, export SME's tend to employ more migrant workers from other provinces than other sectors. They suffer from a lack of workers: the restrictions of mobility imposed after the outbreak of coronavirus prevented many migrant workers from returning to their previous jobs in other provinces.

Due to the strike of pandemics, businesses in Europe and the US have cancelled orders from China, sending another round of shockwave to Chinese exporters. China's exports have dropped by 17.4% this year. Export firms in China have been struggling for survival. Not surprisingly, they held more pessimistic views on business prospects than non-exporters. The slowdown in Chinese exports has huge implications on the stability of the global supply chain. For example, the disruption of production in some automobile parts in Hubei forced Hyundai and Kia to shut down a few assembly lines in South Korea. What about the tertiary sector? The resumption of production in the consumer and business service sectors was lower than in the industrial sector.



Consumers are afraid of eating out, watching movies in cinemas, and sending children to participate in extracurricular activities. Most business travel was cancelled, and trade fairs have been postponed. Given the lingering fears of consumers and companies, it will take a longer time for the service sector to recover than the manufacturing sector.

In 2003, at the time of the SARS epidemic, the services sector's share of total GDP was about 42%, which is 10 percentage points lower than today. The loss in Chinese GDP caused by SARS was estimated to be between one and two percentage points. The impact of COVID-19 on the Chinese economy is therefore expected to be larger than that of SARS, not only because of the duration and magnitude of the crisis, but also because of the increased weight of the service sector in the economy.

What's happening now that coronavirus is largely under control?

Overall, our survey shows that COVID-19 has landed a heavy blow on Chinese SMEs, with huge differential effects across sectors and regions. Now that coronavirus is largely under control in China, resuming production has become high on the policy agenda.

However, in order to zealously pursue for zero case of COVID-19, some regions have imposed extremely stringent regulations for firms to resume production. For example, in one region, if a firm wants to restart its business, it has to fill in 15 forms, two letters of commitment, plan for the resumption of production, plan for canteen health safety, and plan for workers' dormitory safety. The cumbersome regulations prevent firms from restarting their operations.

There are also some good experiences. Zhejiang Province has implemented a unique health QR code system. The green code allows someone to move freely, the yellow code

requires a seven-day self-quarantine, the red code requires a 14-day self-quarantine. The yellow and red codes can be turned green after the quarantine time. Each citizen must monitor and record their temperature and update their profile daily. With this system, a healthy worker with a "green code" can travel and work in the province, a key factor in the recovery of SMEs. Recently a few more provinces have adopted the same model. They recognize this health certification among each other.

Although at the national level the situation is improving, in response to the spread of COVID-19, many countries have adopted a lockdown policy, putting production activities to a halt. China is facing a decline in external demand and disruptions of global supply chain on domestic productions. Although COVID-19 is temporally under control in China, SMEs still face headwinds.

It should be noted that China now accounts for 17 percent of the world economy, compared with 4.3 percent during the SARS outbreak in 2003. China drives 30 percent of the world's GDP growth and is a trade partner to more than 100 countries.

Given COVID-19 has now spread to many other countries, the findings on its impact on SMEs in China may be relevant elsewhere, when a similar type of lockdown strategy is adopted. Given the larger share of the service sector in total GDP in developed countries, negative impacts are likely to be more pronounced there. In developing countries, the disruptions in logistics may hit the key agricultural sector, such as livestock farms, particularly hard.

To go further

Read **Xiaobo Zhang's** article in French and English and turn to additional references on eurics.eu

EURICS is an institute working to strengthen the European research and analysis capacities on China. It works to enhance cooperation at the core of a network of European research centers and think-tanks with focusing on Chinese studies, and to help forge a common European understanding of China.

Inspired by the model of the Institutes for Advanced Study in Human and Social Sciences, EURICS hosts high-level scholars for a period ranging from three to ten months. EURICS supports a multidisciplinary research approach, aiming to seize both mechanisms and motivations of the evolution that marked not only the traditional Chinese culture in its diversity, but also the political, economic and societal transformations that shaped China's long history.

Moreover, EURICS encourages collaborative research and analysis on current dynamics such as environmental transition, population ageing, urbanisation, migrations, social inequalities, learning society, cultural change, economic transformations, as well as on China's international and regional role.

EURICS is an independent institute with an institutional, scientific and financial independence that guarantees the autonomy of its research, analysis and debate. Opinions expressed by the authors do not necessarily reflect those of the institute.

EURICS.
欧洲中国研究院 European
Institute
for Chinese
Studies

Head of editorial:
Alain Peyraube
Olivier Bouin
Aurélien Louchart

www.eurics.eu
@EURICS1