

China Politics Weekly

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Dear friends and colleagues,

This week's newsletter below. Old issues are always available at www.chinapoliticsweekly.com. Sign up or unsubscribe by sending an email to info@chinapoliticsweekly.com. Comments and feedback always welcome.

I'll be traveling for the next five weeks, so the newsletter is likely to be abbreviated during that time. If any of you are in New York or DC (or Charlotte, NC?) and would like to meet up, drop me a line.

It's not an easy time to be a Chinese leader. The economy is looking increasingly shaky, tensions in the South and East China Seas are increasing and domestic terrorism is ever more frequent. It's also the 25th anniversary of Tian'anmen Square on Wednesday. How China responds to these challenges in the coming weeks and months should give us a much clearer picture of the Xi-Li administration's approach and capabilities.

Trouble at home (with homes)

The government seems increasingly nervous about an economic slowdown. The financial system looks unsteady with property prices falling and NPLs on the rise. Xi Jinping is trying to manage expectations with talk of a "new normal" that accepts lower growth. Meanwhile the State Council is trying to cushion the blow with its "mini-stimulus" measures, the latest of which was a reserve ratio requirement cut for smaller banks announced on Thursday. This came a day after the [MOF encouraged governments to speed up spending on approved projects](#). The PBOC- which has been injecting liquidity for months- also seems to be preparing for the worst as it [considers direct buying of bonds](#).

It's difficult to find somebody who has positive things to say about the economy; my own recent conversations with economists and businessmen have been overwhelmingly negative.

And yet, there is one reason for optimism: top leaders have so far shown no sign of backtracking on the reform process. Xi's speech at the Politburo study session last week reaffirmed the Party's view that the market should now play the "decisive" role in resource allocation, a positive sign that market-oriented reforms will continue to be pushed from the top. And the "mini-stimulus" measures have all been purposefully contained to avoid the widespread expansion of credit and consequent malinvestment that characterized the 2008-2009 stimulus.

Instead of pushing up investment, Li made clear on Thursday that the government's focus is on creating a more transparent market economy. He deplored the current state of hidden fees that increase uncertainty in the marketplace and [called on ministries and local governments to publish a "fee catalogue"](#) that would make clear

the costs of doing business for firms. The premier also called out local officials who have failed to implement the new administration's directives.

One's views about China's prospects often come down to a judgment on the ability of the Party to correctly assess and respond to challenges. There is a correction coming in China; it will be painful in the short term, but is necessary for sustainable long-term growth. For now, we should be encouraged that the government seems willing to accept slower growth, and still seems committed to the reform path.

Trouble on the high seas

More worrisome than China's economic troubles are the rising tensions in the East and South China Seas. A Vietnamese fishing boat was sunk last week, and further clashes between Chinese and Vietnamese boats were reported on Sunday. China's aggressive behavior has stirred nationalist sentiments across the region, and is increasing the chance of conflict with neighboring countries, particularly Vietnam and Japan.

The United States has not helped the situation with its foreign policy in the region. A visit to the region last month by US President Barack Obama was supposed to reassure allies that the US is committed to its Asian "pivot", but the lasting impression from the trip was one of a disengaged president unwilling to truly commit to the region. The impression was reinforced days later when the Chinese set up an oil rig in disputed waters, apparently without consequence.

US Defense Secretary Chuck Hagel tried to rectify the situation in his speech at the Shangri-La Dialogue in Singapore on Saturday. He called China's actions destabilizing and tried to send a clear message that the US would not accept further Chinese aggression in the region. However, Hagel's message was undercut by Obama's foreign policy address at West Point a few days prior. Obama's speech focused on the damaging consequences of sending US forces into battle and reinforced the impression that the President has no appetite for foreign wars, signalling that things that would have to be very serious before the US put troops on the ground (or sea).

The next US president, be it Hillary Clinton or a Republican challenger, is almost certain to take a tougher stance in the region. The Chinese know this. The worry thus becomes that China attempts to establish facts on the ground in what it perceives as a two-year window to act without threat of a robust American response. This is dangerous, and increases the chance of war. Geopolitical risk is now the greatest risk affecting businesses in the region.

Trouble out west

The second Central Work Conference on Xinjiang was held last week. The main topic of discussion was how to promote stability and eliminate domestic terrorism.

There are no easy answers. Ultimately, the government probably needs to drop the current Soviet-inspired system that classifies all citizens by ethnicity and subjects different groups to different rules regarding family planning, education and employment. Such a system has reinforced, and in some times created, divisions between ethnic groups. It often serves to keep minorities separated from mainstream Han society, while also engendering resentment among the Han.

But in the near term, the government is probably best served by continuing a policy of positive discrimination that tries to ensure that minorities share in the benefits of economic development. In my own travels in Xinjiang, the biggest complaint among Uighurs has been that the Han keep them from participating in the development that is happening all around them.

Xi and others vowed to increase employment and living standards for Uighurs. At the same time, there is concurrent movement towards a more assimilationist approach. These are steps in the right direction, but they may very well be counteracted by an increased security crackdown and [show trials like the one last week](#). These tend to underline the “us versus them” mentality that’s at the heart of recent violence.

The government is walking a difficult line. It must not look weak or unresponsive in the wake of the violence, while also working to ease ethnic tensions. Let’s hope they get the balance right.

PBSC Week in Review

Xi Jinping	June 3	Xi addressed the International Conference on Engineering Science and Technology.
	May 31	Xi exchanged congratulatory messages with Malaysian Supreme Head of State Abdul Halim Mu’adzam Shah on 40 years of diplomatic relations.
	May 30	Xi met with Prime Minister of Malaysia Najib Razak. <i>Celebrating 40 years of diplomatic relations. Malaysia holds ASEAN chairmanship in 2015. China wants good relations so that it continue to keep ASEAN from formulating coordinated response to South China Sea disputes.</i>
		Xi visited a primary school to commemorate International Children’s Day. <i>“All sectors of society should work together to nurture the seeds of socialist values in their heart so that the values can take root and germinate,” said Xi.</i>
	May 29	Xi attended the Central Work Conference on Xinjiang.
	May 28	Xi attended the Central Work Conference on Xinjiang.
	May 27	Xi attended the 2014 Conference on Transitioning Military Personnel into Civilian Life.
Li Keqiang	June 3	Li held talks with Kuwaiti Prime Minister Sheikh Jaber Al-Mubarak Al-Hamad Al-Sabah. <i>10 MOUs signed.</i>
	May 31	Li attended a ceremony with Malaysian Prime Minister Najib Razak celebrating 40 years of bilateral relations.
	May 30	Li chaired an executive meeting of the State Council. Li visited the Bayi Children’s Hospital to commemorate International Children’s Day.

	May 29	Li spoke with Prime Minister of India Narendra Modi by telephone. <i>Li was the first foreign leader to call up Modi after he was sworn in. Chinese Foreign minister Wang Yi is going to Delhi on June 8, and could become the first foreign minister to visit India after the new government took over. Modi, as chief minister of Gujarat, had visited China in November 2011, much before the West started engaging with him. Modi and Li spoke for about 25 minutes.</i>
		Li held talks with Malaysian Prime Minister Najib Razak. <i>The two sides pledged to achieve a targeted trade volume of USD 160 billion in 2017, up from about USD 100 billion presently. Malaysia will take over chairmanship of ASEAN in 2015</i>
		Attended the Central Work Conference on Xinjiang.
	May 28	Attended the Central Work Conference on Xinjiang.
	May 27	Li met with Solvita Aboltina, Speaker of the Latvian Parliament.
		Li attended the 2014 Conference on Transitioning Military Personnel into Civilian Life.
		Li attended the Annual Meeting of the Global Research Council.
Zhang Dejiang	May 30	Zhang met with Malaysian Prime Minister Najib Razak.
	May 29	Attended the Central Work Conference on Xinjiang.
	May 28	Attended the Central Work Conference on Xinjiang.
	May 27	Zhang met with Solvita Aboltina, Speaker of the Latvian Parliament.
Yu Zhengsheng	May 29	Attended the Central Work Conference on Xinjiang.
	May 28	Attended the Central Work Conference on Xinjiang.
	May 27	Yu chaired a CPPCC symposium focused on reducing excess productive capacity.
		Yu met with Lucas Chomera, the first deputy chairperson of the Mozambican parliament.
Liu Yunshan	May 30	Liu attended a meeting for central level departments on the Mass Line Education Campaign.
	May 29	Attended the Central Work Conference on Xinjiang.
	May 28	Attended the Central Work Conference on Xinjiang.

May 27 **Liu attended the 2014 Conference on Transitioning Military Personnel into Civilian Life.**

**Wang
Qishan**

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Zhang Gaoli

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May 28 **Attended the Central Work Conference on Xinjiang.**

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