

Statement before the  
Congressional-Executive Commission on China

“How China Uses Economic Coercion to Silence  
Critics and Achieve its Political Aims Globally”

A Testimony by:

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December 7, 2021

Chairman Merkley, Chairman McGovern, and distinguished Members of the Commission, thank you for holding this important hearing and asking me to participate.

Economic coercion – defined here as a threatened or actual imposition of economic costs by a state on a target with the objective of extracting a policy concession – is an increasingly prominent instrument of Chinese foreign policy. A vast array of economic coercion measures combined with a set of positive inducements comprise China’s economic statecraft toolkit. As the world’s top trading nation, the second largest market, and one of the largest providers of development finance, Beijing has the potential to wield significant influence by using these sticks and carrots. Although China’s employment of economic coercion has had only limited success in changing the behavior of targets, it has been more successful in deterring countries and companies from undertaking actions harmful to Chinese interests. In addition, PRC positive economic inducements have unquestionably persuaded some states and firms to refrain from criticizing PRC policies, although this impact is more difficult to measure.

Unlike traditional economic sanctions, Beijing’s economic coercion usually relies on informal measures that provide plausible deniability and enable China to ratchet pressure up or down as needed. Whereas there are many instances of Chinese officials and state media threatening to take punitive economic actions against countries and foreign firms, there are very few cases where the Chinese government has publicly acknowledged implementing coercive acts. For example, after Australia called for an independent investigation into the origins of the coronavirus, China’s ambassador to Australia, Chen Jingye warned that ordinary Chinese would say “Why should we drink Australian wine? Eat Australian beef?” Beijing subsequently cited violations of phytosanitary requirements as the reason for holding up imports of Australian beef, timber, and lobster. China also falsely alleged that Australia was dumping barley and wine and subsidizing the producers of those products. After months of vague import restrictions on Australian coal, the Chinese government formalized the ban by granting approval to Chinese power companies to source coal from a list of countries that did not include Australia.

The PRC has employed coercive economic measures in support of its foreign policy objectives since at least 2010 when it used coercion on two occasions: 1) halting rare earth exports to Japan to compel Tokyo to release the captain of a Chinese fishing trawler who was detained after colliding with a Japanese patrol boat operating near the disputed Senkaku/Diaoyu islands; and 2) restricting salmon imports from Norway after the Norwegian Nobel Peace Prize Committee granted the annual award to Chinese dissident Liu Xiaobo. Since then, the PRC has used economic coercion against over a dozen countries. In virtually every case, the targets have been companies and industries in democratic states. The Chinese apparently believe that by pressuring influential business constituencies in democracies they can change the policies of targeted governments.

Beijing often uses other non-economic coercive tactics in combination with economic coercion. Downgrading bilateral relations, cancellations of high-level dialogues, or preventing foreign officials from meeting with their Chinese counterparts are commonly used alongside economic coercion tactics. Arbitrary indictments, detainments, and harsh sentences for imprisoned foreign nationals have been used by the PRC to exert pressure on foreign governments. In its attempt to compel Ottawa to release Huawei's CFO Meng Wangzhou, Beijing's illegally detained Canadian citizens Michael Kovrig and Michael Spavor as well as restricted imports of Canadian commodities such as canola seeds, oil and meal. Swedish citizen Gui Minhai was sentenced to 10 years in prison in 2020 on charges of illegally providing intelligence to foreigners. Gui was awarded the annual Tucholsky Prize for writers and publicists living under threat or in exile by Swedish PEN, an NGO committed to defend freedom of expression. China's ambassador to Sweden publicly announced that his country planned to impose restrictions on economic ties and trade with Sweden and deny visas to reports from Sweden who criticize China.

Below are four categories of PRC coercive economic diplomacy:

### **Trade Restrictions**

The majority of cases have included the imposition of export and import restrictions. Beijing has employed many tactics, including tariff increases, targeted customs inspections, license denials, informal embargoes, and selective use of international regulations. In one of the most recent cases, Beijing ended all trade with Lithuania by delisting it as a country of origin, which meant that imported goods from that country cannot clear customs. The measures were taken to punish Vilnius for permitting Taiwan to establish a representative office with the name "Taiwanese Representative Office." China has only taken measures to restrict imports of products for which it doesn't have an easily available substitute. It did not target imports of iron ore from Australia, for example, because China sources 60% of its iron ore from Australia and has no reliable alternative suppliers.

### **Tourism Curbs**

With a large number of outbound tourists and considerable control over their movements, Beijing has frequently restricted tourist flows to other countries. The Philippines was one of the first targets of a freeze on Chinese tourist visits in 2012 after a Philippines warship attempted to arrest Chinese fishermen who were fishing in the lagoon at Scarborough Shoal, which is disputed between the PRC and the Philippines. Protests against China in Manila provided a pretext for the state-owned China Travel Service to suspend indefinitely all tours to the Philippines due to "strong anti-China sentiment" that could pose a risk to the safety of PRC citizens.

### **Actions Against Foreign Companies and Industries**

A high degree of centralized government control enables the PRC to take punitive measures against companies and industries that are associated with a country that China

is seeking to punish. When South Korea deployed the Terminal High Altitude Area Defense (THAAD) anti-missile system in 2017, Beijing rejected certification of Korean batteries for hybrid-electric vehicles, which prevented any vehicle equipped with cells made by LG Chem and Samsung SDI from being sold in China.

In some instances, the PRC uses economic coercion to target companies to change specific practices that the Chinese Communist Party deems objectionable which are not connected to government policy. In early 2018, the PRC threatened to take action against Western airlines and companies that listed Taiwan as a “country” on their websites. The following year, China canceled digital streaming of Houston Rockets games after the NBA team’s General Manager Daryl Morey posted a tweet supporting Hong Kong protesters. Rather than risk being shut out of the Chinese market, the NBA and other entities that have faced censorship from China have issued public apologies and many companies have complied with Chinese demands.

Just last month, Taiwanese company Far Eastern Group and its subsidiaries were fined US\$13.89 million for alleged breaches involving environmental, land use, fire safety, tax issues and other regulations at factories in five Chinese provinces. Beijing openly accused the company of supporting Taiwanese independence by providing large political donations to candidates from Taiwan’s ruling party, the Democratic Progressive Party. China has long required Taiwanese businesses seeking to invest in China to support the “One China” policy, but it has rarely enforced this policy. Seeking to prevent further punitive actions from being taken against his company, Far Eastern Group Chairman Douglas Tong Hsu published an article stating that he has always opposed Taiwan independence and supported the “one-China principle.”

### **Popular Boycotts**

The PRC uses state and social media to encourage its citizens to launch nationalistic boycotts against companies and industries from a target state. The South Korean conglomerate Lotte Group, which provided the land in Seoul for the THAAD deployment, was targeted with massive protests that eventually forced it to shut down its 112 stores in China. In 2012, Chinese authorities fueled anti-Japanese protests after Tokyo’s prefectural governor Shintaro Ishihara announced his decision to let the municipality purchase three of the disputed Senkaku/Diaoyu Islands from their private owner.

In some cases, popular boycotts by the Chinese people and companies may occur without Chinese government urging or direction, as PRC officials claim. However, it is undeniable that the government has employed a range of levers to both promote and tamp down popular boycotts during foreign policy disputes. The fact that Chinese officials threatened to instigate consumer boycotts of some Australian products in retaliation for Canberra’s offending policies indicates that Beijing views popular boycotts as a useful coercive economic tool.

Although this hearing is focused primarily on economic coercion, it is important to note the negative impact of China's positive economic inducements as well. In addition to creating debt crises, corruption, environmental damage, and other negative consequences, China's financing to developing countries under the Belt and Road Initiative has stifled global criticism of Chinese violations of human rights. Many recipients of China's BRI funding have openly supported Beijing's position that its actions against Uighurs and other minorities in Xinjiang are necessary to counter terrorism and extremism. During the 47<sup>th</sup> session of the United Nations Human Rights Council earlier this year, more than 90 countries, including several with majority Muslim populations, expressed their support for China's stance and 65 of them opposed interference in China's handling of the situations in Xinjiang and Tibet. Although it is difficult to prove, it is likely that many of the states that sided with China did so because they want to continue to receive Chinese loans and investment, and fear that refusal to support Beijing would put those benefits at risk.

When has the PRC's economic coercion been successful and why? Studies show that the level of economic pain that initiating countries can inflict on targets rarely, by itself, determines whether coercion is effective. In the cases in which China has employed economic coercion, the failure to compel many of the targeted foreign governments to alter their policies is due in part to the fact that Chinese application of economic pressure has generally been aimed at a small number of companies or industries in each target country and therefore the impact on China's total trade with that country has been relatively limited. In most cases, the economic hardship has been short lived because companies have discovered ways to circumvent PRC restrictions or found new markets for their goods. For example, Canada's exports to China fell by \$3.5 billion in 2019, but that loss only constituted a small fraction of Canada's \$447 billion in exports that year. Of the almost one dozen Australian products targeted by Chinese coercion, all are being shipped elsewhere, except for a small percentage of high-end Australian wine.

The PRC's move to halt all trade with Lithuania will not have a major negative effect on the Lithuanian economy because only 1% of its exports go to China. However, if Beijing were to take similar actions to block all imports from a state that has a greater trade dependency on China, the impact could far more damaging. Since the PRC's decision to delist Lithuania as a country of origin is in clear violation of WTO rules, it is possible that this action may strengthen the willingness of democracies to unite to push back against Chinese economic coercion.

In the cases that PRC pressure has successfully led to policy changes in the target state, political factors have played a bigger role than the effectiveness of economic coercion. Norway's exports to China declined as much as \$1.3 billion between 2011 and 2013, but by 2014 its exports had rebounded to normal levels. The Norwegian government remained subject to significant restrictions on political interactions with Beijing, however. After seven years, Oslo agreed to make political concessions to China to restore the bilateral relationship to normal. In 2017, Norway signed a new political agreement

with Beijing in which it said that Norway “fully respects China’s sovereignty and territorial integrity, attaches high importance to China’s core interests and major concerns, will not support actions that undermine them, and will do its best to avoid any future damage to the bilateral relations.”

Mongolia conceded to Chinese demands more quickly than Norway. The PRC implemented measures to hamper trade with Mongolia after Ulaanbaatar hosted the Dalai Lama, Tibetan’s spiritual leader, for a visit. The Mongolian government subsequently publicly stated that “Tibet is an inseparable part of China and the Tibet issue is China’s internal affair.” It agreed to never host the Dalai Lama again. Both political and economic factors likely played a role in Ulaanbaatar’s decision. Mongolia was desperate for Chinese investment in mining and infrastructure and Beijing had canceled talks to discuss a potential loan. The country’s geographical proximity to China also requires preserving some modicum of friendliness and stability in relations with its much larger neighbor.

In Japan’s case, although China was not successful in blocking rare exports to Japan, Tokyo capitulated and released the Chinese captain of the fishing vessel. Japan’s decision was likely based on political considerations, and perhaps concerns that Beijing could take more harmful measures, such as acting against Japanese investment in China.

In the majority of instances in which Beijing has used economic coercion against states, it has failed to change the policies of its targets. In some cases, China’s trade weaponization has backfired. In the wake of being subjected to Chinese pressure, some countries have taken steps to reduce their dependence on China and create more resiliency in their supply chains. Although China won a short-term victory against Japan in 2010, Tokyo subsequently slashed its vulnerability to China: over 90% of Japan’s rare earths were imported from China in 2010, it cut that reliance to 58% within a decade.

Moreover, Beijing’s coercion has caused many countries to rethink their economic relationships with China and encourage their companies to diversify. In some cases, China’s use of coercive tools has inadvertently caused the formation of nascent anti-China coalitions. The pursuit of trade restrictions against Australian industries was probably a factor in Canberra’s reassessment of its security environment that led to its decision to sign the trilateral AUKUS pact with the United States and Australia.

China’s economic coercion has likely been more successful in deterring some countries from taking actions that could damage Chinese interests than in compelling policy reversals. In fact, the intended target of Chinese actions often may not be the offending country; instead, China often coerces one to deter another – “killing the chicken to scare the monkey.”

## **Recommendations**

Despite its limited success and occasional blowbacks, Beijing continues to view economic coercion as a valuable tool in its economic statecraft toolkit. This is likely because it judges that the cost to China is negligible. Recent developments such as the

AUKUS deal and the pending EU anti-economic coercion tool suggest that countries are willing to band together to impose greater costs on China. The United States should consider undertaking unilateral steps as well as work with like-minded partners to counter and deter potential Chinese economic coercion, and to prepare measures to limit potential damage to companies and industries.

*To Do List:*

- *Diversify trade relationships:* The United States should identify sectors which are overly dependent on the Chinese market and therefore vulnerable to coercive trade practices. National and local governments should actively promote trade diversification.
- *Assist companies and industries to identify and respond to trade coercion:* The United States should help potential targets of economic coercion to develop tools to identify cases of trade coercion and respond quickly. Trade associations and other stakeholders should be encouraged to work closely with U.S. government agencies. Mechanisms should be created for sharing information and best practices.
- *Prepare to assist targets of coercion:* Encourage companies to have a plan in place to respond to potential Chinese coercion. They should be encouraged to report all instances of coercion to appropriate U.S. government entities. The U.S. government should become actively involved in coercion cases in various ways, ranging from diplomatic condemnations of China's actions to providing compensatory support for targeted industries and workers. Congress should explore how to appropriate funds for a vehicle to compensate companies affected by Chinese coercion. The provision of assistance to targets of coercion will likely reduce incentives to comply with Chinese demands.
- *Encourage private sector trade associations to develop a voluntary code of conduct regarding China.* Such a code would include commitments by U.S. companies to refrain from self-censorship and other activities in China that are contrary to U.S. values and interests. The U.S. should consider developing incentives that could be provided to companies that sign on to the code of conduct.
- *Create a voluntary counter-coercion coalition of like-minded countries willing to push back against economic coercion:* When instances of economic coercion take place, coalition members can decide whether and how to respond. Through collective action, the coalition would seek to compel China to stop its economic coercion campaign and to desist from taking future coercive measures in the future. Collective steps could include: 1) issuing a joint declaratory statement condemning Chinese behavior and other coordinated diplomatic actions; 2) encouraging targeted countries to pursue WTO dispute settlement cases against instances of economic coercion where WTO remedies are possible, with other

coalition members then signing on to those cases as third parties; 3) explore ways of taking retaliatory trade, investment or other policy measures against China that are consistent with WTO rules; and 3) create a counter-coercion reserve fund to compensate companies for economic losses. The fund should be capitalized by coalition members and private sector firms who might be targeted by coercion and receive compensatory support. Even a small amount of compensation would send a signal of political support to the targets of coercion, and more broadly to allies, partners, and the private sector.

- *Work with allies and partners to reform the WTO so that member states are protected from economic predation.* Realistically, this cannot be achieved quickly, but it is in the interests of democracies to strengthen the WTO so it can effectively penalize bad behavior when it occurs and arbitrate disputes objectively.



# PRC Trade Coercion

<u>Country</u>	<u>Year</u>	<u>Precipitating Action</u>	<u>Punishment</u>
Norway	2010	Liu Xiaobo granted Nobel Peace Prize	Curtail salmon imports; freeze FTA talks
Japan	2010	Chinese fishing captain arrested	Block rare earth exports
Philippines	2012	Confrontation at Scarborough Shoal	Block tropical fruit imports/cut tourists
Mongolia	2016	Dalai Lama visit	Impose fees on commodity imports
South Korea	2016	THAAD deployment	Boycott South Korean products
Taiwan	2016*	Refusal to endorse "one China"	Restrict tourists, boycott fruit
Australia	2017*	Campaign against interference/5G policy/ call for investigation into origins of Covid19	Limits on coal, wine, barley copper, sugar, timber, and lobster imports
Canada	2018	Arrest of Huawei CFO Meng Wanzhou	Ban some Canadian agricultural goods
New Zealand	2019	Huawei blocked from 5G rollout	China-NZ year of tourism postponed
Sweden	2019	Culture Minister gives rights prize to Gui Minhai	Trade/business delegations canceled
Czech Republic	2019	Prague signs sister city deal with Taipei	Shanghai cuts ties, ends official contacts
United Kingdom	2020	UK support for Hong Kong protesters	Suspend Shanghai-London stock connect
Sweden	2021*	Ban on Huawei in 5G telecom market	Reduced Ericsson's share in tender
Lithuania	2021*	Taipei opens "Taiwan" office in Vilnius	Suspend rail freight, stopped trade

\*ongoing      ■ successful      ■ partly successful (This list is selective; there are additional cases not included )