DIGITAL-ONLY COMMENTARY

Warning

There Are Two Other Chinese Epidemics—Finance and Technology

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While the world remains transfixed and in a state of ongoing coronavirus response, it is easy to overlook China's drive to open its markets to global finance further as it produces more of the commonly used information communication technologies (ICT). The dynamic change and growing convergence in both sectors not only transform the digital landscape but also threaten economic stability and political freedom inside and outside of China. Over the past few decades, the synthesis and profusion of financial algorithms and electronic communications, lightning-fast data streams, abundance of cheap surveillance capabilities, and increased access to emerging technologies have propelled opportunities to enhance society, generate prosperity, and offer new digital goods and services. Indeed, China pioneers many of the technologies and techniques available for the digital marketplace, from electronic payment via Alipay to communications infrastructure with Huawei servers.[1]

More importantly, there are signs of systemic weakness and rising risk to the global community as China expands its market share and competes globally in both sectors. There is the specter of an immediate pandemic in global finance and an emergent pandemic in ICTs. These pandemics may even coincide. However, both directly point back to China, as did the coronavirus pandemic. The symptoms of these two diseases are not overtly apparent. Based on reporting from Chinese sources, China appears to be at best "healthy" and at worst "asymptomatic."

Conversely, an objective diagnosis reveals that the prognosis may be dire. As experience with COVID-19 highlights, it is critically important to rapidly identify a pathogen and then correctly prescribe treatment. Quarantine or other preventive measures may be necessary. If not, these contagions could spread rapidly from an epidemic level to a pandemic level across the globe.[2]

Yet, the global community cannot socially distance itself from China's growing influence across international finance or the proliferation of a Chinese-backed digital environment. Moreover, there are no vaccinations available to inoculate from either. Luckily, antibodies are coming together in the form of pushback on multiple fronts. However, it may not be enough.

How Are Global Finance and ICTs Like the Coronavirus?

COVID-19 laid bare many assumptions and vulnerabilities for the United States and the global community. The world feels smaller now, watching the virus's rapid transmission, witnessing the spread of medical information (and disinformation), and delivering lifesaving supplies from abroad. Almost a year into the global pandemic, disease-related fatalities continue to climb past 1.6 million, and affected economies expend trillions of dollars in stimulus.[3] Critical questions remain unanswered. How secure or vulnerable are the supply chains from disruption and manipulations? Should ICTs that share personal information, like virus-tracking apps, be mandated during a public health crisis? How should governments invest resources in a crisis to improve outcomes? What is the role of global organizations to address common problems? Can governments adequately sustain the appropriate level of fiscal stimulus response?

As the global community and Americans sort through the answers to these and other questions as they combat the virus, it is critical to take a pause and recognize two other looming threats. Both are spreading, relatively undetected, out of China. And their transmission rates are enhanced because they are digitally interwoven. China is using foreign capital to continue an artificial, debt-fueled supply-side economic growth model, while government-linked Chinese firms are exporting vulnerable hardware and software with the expertise to leverage them to control and oppress populations. For example, it is possible to purchase Renminbi or trade shares of Sinopec, while on a Chinese-produced smart device with little effort. At every point along the way, the user's most personal and intimate information can be tracked by a digital "eye." A digital chain now exists that links a user and their data directly to China from anywhere in the world. With 4 billion people online, increased Internet access equates to an increased risk of exposure.[4] This level of financial and digital interconnectedness was unheard of until recently. Still, the revelation becomes more unsettling against the myriad of warning signs and indicators emanating from China in both finance and ICTs.

China's Financial Epidemic

China rapidly became a focal point for investment as finance was globalized over the past few decades.[5] As China absorbed capital, Beijing pursued economic policies that synergized and mimicked the strength of capitalism and the free market–based economy in tandem with preserving the Chinese Communist Party's (CCP) authoritarian governance structure. Often, this synergy is referred to as authoritarian capitalism or statist capitalism.[6] Regardless of nomenclature, China's economy is heavily influenced by and subservient to the desires of Chinese leadership, which ultimately rests with the CCP. The recent and prominently publicized dispute between the party and billionaire Jack Ma over his highly anticipated Ant Financial initial public offering (IPO) illustrates this point all too well.[7] After evoking the ire of key officials, Ma delisted and withdrew the IPO. The action scuttled a valuation in the tens of billions of dollars and rattled international investors. Another billionaire, Ren Zhiqiang, who criticized General Party Secretary Xi Jinping's handling of the COVID-19 pandemic, faces an 18-year prison term.[8] These are two of many concerning incidents in China's business community. However, there was a string of other unsettling financial trends detected in China before the COVID-19 pandemic.

China's domestic economy now exhibits a litany of symptoms associated with severe financial infection. First, China had accumulated over 40 trillion USD in debt—nearly 15 percent of the global total—by late 2019.[9] Second, China's debt as a percent of gross domestic product ballooned to a record 327 percent, whereas the United States is around one-third of that.[10] Third, bankruptcies tripled in the past few years leading into 2019.[11] To compensate, China adopted significant portions of the United States' bankruptcy laws and stood-up more than 90 bankruptcy courts, because no comprehensive bankruptcy system existed in China. Fourth, China's growth rate slowed to a 30-year low in 2019 and was projected to slow even more into 2020 before the pandemic.[12] Fifth, China now has the world's largest property asset bubble, valued at nearly 52 trillion USD, mainly in real estate.[13] Sixth, China publicly maintains financial solvency despite two significant and historic hits to its currency reserves. In 2008, China dipped into its coffers and spent 586 billion USD on domestic projects to stave off economic decline.[14] In 2015, China dipped into those reserves a second time to inject up to 1 trillion USD to buoy its crashing stock market.[15] China took these hits before the COVID-19 pandemic wreaked havoc on its economy and bottom line. Surprisingly, Chinese financial reserves appear to be unaffected by these incidents. Chinese bank officials claim their foreign currency reserves have hovered around 3.1 trillion USD, leaving many economists perplexed.[16] Regardless, it is unclear how much is left in the currency reserves for future exigencies. Finally, there is a spate of high-level defaults among Chinese state-owned enterprises that is spooking investors.[17] However, looking beyond China's borders, another debt contagion flares too.

China's global financial portfolio is chronically infirm. Hundreds of billions of dollars in loans linked to its ambitious Belt and Road Initiative (BRI) show signs of distress.[18] One BRI project, the 4.5 billion USD Djibouti-Ethiopian Railway, is a case in point. The Chinese export and credit insurance company Sinosure lost close to 1 billion USD on this railway, which continues to operate at a loss.[19]

Examples like the railway continue to pile up elsewhere. Some states beholden to China have avoided default by restructuring their debts or conceding to land or commodities swaps, raising concerns of more "debt-trap diplomacy."[20] For others, like Zambia, the financial crunch was unavoidable. Zambia captured headlines when it defaulted because it pitted Chinese creditors against Eurobond holders and others seeking recoupment.[21] Zambia is just the latest to fall, like a row of dominoes, with others behind it. Venezuela, which holds billions in Chinese debt, defaulted earlier this year.[22]

Separately, Chinese companies listed on overseas exchanges, like the Nasdaq, have come under increased scrutiny. When it was disclosed that Luckin Coffee reported 300 million USD in fraudulent sales, the Nasdaq subsequently delisted the company.[23] Under the recently passed Holding Foreign Companies Accountable Act, US officials now will require Chinese companies listed on American stock exchanges to use American auditors instead of Chinese auditors.[24] Finally, the pandemic has accelerated trends from increasing online commerce to experimentation with drone delivery and supercharging income inequality.[25] Dubious investments were already showing signs of fracturing before the coronavirus. They will be no different, even in China.

Consequently, the accumulation of these various, adverse transactions leaves a Chinese financial ledger less than desired. Unfortunately, the financial community seems to have misdiagnosed the fact that China is bust. China may indeed be insolvent, but it is too global to fail. An economic collapse in China will be worse than the American financial meltdown in September 2008 or the Chinese stock market crash in 2015. This is because Chinese-driven consumption and production are so widespread and adequate financial resources are not available for a larger, more systemic bailout this time around. Additionally, many nations are spread thin financially by their response to COVID-19.

In China, economic remedies ran lower than anticipated earlier this year, as its economy shrank significantly for the first time since the Mao Zedong era.[26] Equally, the United States' already tapped a 2.2 trillion USD stimulus package in the spring.[27] The US deficit has breached 3.1 trillion USD for the year, and future stimulus packages remain uncertain.[28] The bottom line is that there is little financial medicine left to dispense. As a result, America's national security establishment should take heed. The US defense budget, which remains at historically high levels, likely will be reduced after 2021.[29] China, on the other hand, probably will press ahead with its newly stated goals for military modernization by 2027 with few, if any, resourcing trade-offs or concessions.[30]

Beijing more than likely recognizes the precarious financial state China is in. It is even likely that China knew this for some time. That would explain various patterns in Chinese financial behavior that seek to capture as much capital and foreign currencies as possible without losing control of any. It would justify the People's Bank of China's obfuscation of official state financial reporting and opaque financial system.[31] And it would rationalize currency manipulation.[32] China's roll-out of the Digital Yuan *e*-currency, which enhances centralized control over currency, lends itself to this pattern.[33] Draft laws that raise the Chinese retirement age, shaving trillions of dollars in benefits, suggest another option that Chinese policy makers are pursuing to shore up finances.[34] Additionally, Beijing accelerated the opening of major portions of China's financial markets to foreign investment for the first time, while severely restricting the ability of investors to exit those markets with their currencies.[35] At the same time, China strictly controls the flight of foreign currencies out of China through the heavy hand of the State Administration for Financial Exchange.[36] These patterns reveal severe weakness. Even though the globe seems to have missed the diagnosis in finance, there is still time to diagnose the one in ICTs.

An ICT Epidemic

China delivers much of the global marketplaces' content, devices, cables or conduits, financing, programmers, hardware, software, and protocols. Furthermore, China backs this up in conjunction with state-based initiatives such as Made in China 2025 and the Digital Silk Road as part of the broader BRI.[37] In Africa alone, Huawei provided 70 percent of the 4G networks.[38] Yet, Huawei has come under criticism for assisting Uganda's president to spy on political opponents.[39] Meanwhile, the Shenzhen-based Transsion's TECHNO phone remains the top-selling phone on the continent. However, Chinese smart devices can curate a user's content.[40]

As more ICTs are digitally interconnected, China stands to enhance monitoring and surveillance not just in China, but elsewhere. This becomes more pronounced as there may be 25.1 billion connected devices.[41] They include DaHua-produced surveillance cameras found in Xinjiang detention centers or a neighbor's home surveillance system.[42] These devices also include DJI Drones that surveil quarantine breakers in Beijing or that are flown by your local drone enthusiast[43] and commercially available facial recognition technologies that come prepackaged in Smart City/Safe City applications for cities like Kuala Lumpur, Malaysia.[44] These are sensors sold at scale.

China has been working on a comprehensive Internet security and surveillance program for domestic use for some time.[45] China's global drive in ICTs further enables this development. That is why the revelations of the broad collection and aggregation of millions of peoples' personal data, like the Shenzhen Database, should be no surprise.[46] Simply put, if any of Edward Snowden's revelations regarding the clandestine surveillance system called PRISM are to be believed, then basically China is creating and packaging its version of PRISM for sale into the stream of global commerce.[47] The Senate Foreign Relations Committee found that technologies such as these enable China to "establish, expand, internationalize, and institutionalize a model for digital governance," enhancing Beijing's influence over participating regimes and their citizens across the digital domain, especially by leveraging ICTs.[48]

Moreover, China's conduct reveals that it has few qualms about harnessing any or all these technologies and techniques to advance its interests. In fact, China's technologically enforced authoritarianism has been coined "digital dictatorship," "digital authoritarianism," or the "new panopticon."[49] The panopticon is particularly disturbing. It harkens back to a prison model championed by the English philosopher Jeremy Bentham in 1795 that was revived in the twentieth century by French intellectual Michel Foucault to describe a government's extension of social control over its citizens.[50] Today, it is possible to replicate and export the digital dragnet in Xinjiang to the farthest corners of the world. While not as pressing and immediate as the financial epidemic, the ICT epidemic represents a steady dosage of digital control along with a gradual deterioration in personal privacy.

Will These Epidemics Reach Pandemic Level?

China did not pioneer the free market, nor did it create the Internet. Still, Beijing has learned to leverage global finance and ICTs for China's interests. By opening its financial markets, pulling in global capital, and building out the digital information environment worldwide, China is exporting an excessive level of risk to the world. The overriding concern is that there is no holistic appreciation of the unintended consequences and the impact from the spread of these capabilities and capacities by China abroad. China has spawned an immediate and dangerous financial contagion that risks the health of the global economy. Simultaneously, Beijing promotes a digital control chain that not only links participating governments with their citizens and one another but also binds their data to China.

The global community and the US national security establishment need to recognize these epidemics for what they are. However, the diseases must be accurately diagnosed first. That way, it will be possible to anticipate and plan accordingly. There are signs of antibodies in the form of pushback from the United States and others in critical areas, like delisting Luckin or contesting Huawei's encroachment on 5G; yet, more is required.[51]

It remains to be seen how China will react to these two contagions. There are viable solutions to forestall or mitigate these epidemics, but the time for the

United States and others to act is closing. Perhaps the best treatment is openness and transparency. Beijing could come clean regarding China's finances or disclose more clearly how it processes the information harvested by its ICT infrastructure. However, this would be anathema to China's leadership. Ostensibly, it may be too late for them to change course. Looking back to the initial COVID-19 outbreak in China, openness and transparency were crucial to identifying the virus and alerting the global health community. Unfortunately, by the time China did so, COVID-19 had already exploded to a pandemic level. American and global officials may avoid infection this time, but proper diagnosis is required immediately. ✪

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Notes

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