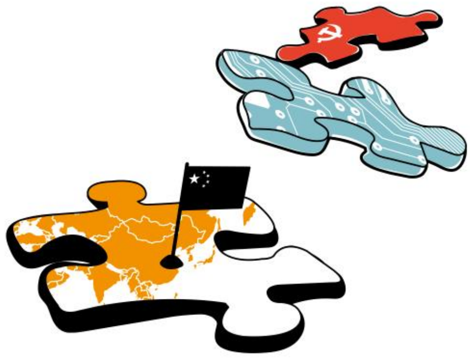
DECEMBER 7, 2023

MERICS China Essentials



CONTENTS

MERICS Mercator Institute for China Studies

TOP STORY

China's climate strategy: Deferring leadership to others

120 countries this week vowed to triple global renewable energy capacity by 2030. The headline-grabbing pledges at the UN Climate Change Conference "COP28" helped China distract from its continued refusal to commit to a deadline for ending coal power or to do more to help poorer countries to finance the huge costs of the green transition. The slew of renewables undertakings in Dubai came only two weeks after China and the USA lent a months-long international process final momentum with a similar bilateral pledge – neither commitment bound governments to phasing out coal by a certain date.

Chinese Vice-Premier Ding Xuexiang used a speech at COP28 to call on "all nations" to "increase the proportion of renewable energy" – and on "developed countries" to make more effort to help developing nations master the challenges posed by climate change. According to the 1992 UN Framework Convention on Climate Change, today's global superpower belongs to a group of "vulnerable countries" that deserve "investment, insurance and technology transfer" for green transition. If China remains content to go on using this definition, its image as climate-action laggard seems unlikely to change.

Despite being the biggest current and third-biggest cumulative emitter of greenhouse gases, China had in the run-up to COP28 again opposed deadlines for coal power. Weeks before a meeting with his US counterpart John Kerry, climate envoy Xie Zhenhua said a complete phase-out of coal or other fossil fuels remained "unrealistic". They then agreed a deal that privileged the eventual crowding out of fossil fuels over fixed phase-outs – useful for China and its coal-power construction plans. As parts of the region that is the second-highest cumulative emitter, most EU states plan to phase out coal by 2030. The USA, the biggest cumulative emitter, has pledged to do the same – as yet without a date.

MERICS analysis: "China wants to dilute 'grey' with green energy in the hope of crowding out fossil fuels at some conveniently undefined point," said **Nis Grünberg**, MERICS Lead Analyst. "This stability-oriented approach appeals to Beijing as an alternative to the swift-but-costly fossil-fuel phase-out the planet needs – but it will fail to limit global warming to 1.5 degrees above pre-industrial levels. If Beijing wants to speak for vulnerable developing economies, it needs to act more quickly on fossil fuels."

Media coverage and sources:

- Carbon Brief: The Carbon Brief Profile: China
- China Dialogue: COP28 Preview: China in the world's spotlight
- Xinhua: China's role highlighted at COP28 in global climate action

METRIX

2

For more than two years, a group of hackers with links to China went undetected as it ferreted around the IT-network of NXP, a Dutch semiconductor manufacturer. Chimera, as it was dubbed by cybersecurity firm CyCraft, regularly accessed the company's system and encrypted small loads of chip-design data to transfer home. Dutch newspaper NRC said NXP only became aware of its problem after hearing of a hack elsewhere –and the company was not worried about the theft as its chip designs were too complex to reproduce. Chimera has in the past targeted other microchip makers in other parts of the world. (Source: Ars Technica)

TOPICS

US concern over China tech transfer endangers business ties in the UAE

The facts: Amid national security concerns and increased China tech competition with China, US intelligence officials have flagged a tie-up between US company OpenAI, inventor of ChatGPT, and the United Arab Emirates tech group G42, which has connections to many Chinese companies. The collaboration will integrate advanced AI capabilities into G42's many domains. Washington is worried that this will be a back door for China to access American cutting-edge AI technology. In October, Washington expanded its semiconductor export controls to countries including the UAE, to prevent such diversion to China. G42, with interests from healthcare to finance to energy, is controlled by UAE national security advisor Sheikh Tahnoon bin Zayed.

What to watch: The Biden administration has reportedly pressured Sheikh Tahnoon to cut Chinese ties. The UAE and G42 have cultivated deep collaborations with major companies from both the US and China – G42 has partnerships with both Microsoft and Huawei. Such relationships are facing greater scrutiny amid US concerns over technology transfer to China, as more and more companies are being forced to take sides in the current geopolitical environment.

MERICS analysis: "Washington's alarm over G42 is part competition with China for regional influence in the Middle East, part protecting access to cutting-edge AI software," says **Wendy Chang**, Analyst at MERICS. "In making everyone choose sides, the room for international businesses or research institutions to collaborate with both the US and China is shrinking further. Scrutiny over this collaboration is an extension of US efforts to keep China behind in the development of cutting-edge AI. But restricting large AI models is much harder than just putting export controls on advanced semiconductors, as much of AI software is open source. Given the highly sensitive nature of this collaboration, we can expect the US to try and find a way to stop it."

More on the topic:

- AI entanglements: Balancing risks and rewards of European-Chinese collaboration, MERICS Report by **Rebecca Arcesati, Kai von Carnap, Wendy Chang** and **Antonia Hmaidi**

Media coverage and sources:

- The New York Times: Warnings emerge over Emirati A.I. firm G42's ties to China
- Fortune: AI chip export controls on China underfunded: Raimondo
- Protocol: Commerce Department export controls on chips EDA software

Chinese ship damaging European pipeline raises question of state involvement

The facts: Finland has accused a Chinese container ship of deliberately damaging the Baltic connector gas pipeline linking Estonia, Finland and Sweden at the beginning of October. "Everything indicates it was intentional", Minister of European Affairs Anders Adlercreutz told the news-website Politico. The vessel Newnew Polar Bear, associated with a new and apparently little-known Chinese shipping company, is said to have severed the gas pipeline and nearby cables while dragging – and then losing – its six-ton anchor on the Baltic Sea floor. The Chinese Ministry of Foreign Affairs said any damage was accidental, noting that the vessel had navigated properly in adverse sea conditions. It also said it would co-operate with a Finnish investigation into the incident.

What to watch: Despite China denying that the Baltic connector was deliberately sabotaged, the incident echoes the damage done in 2022 to the infamous North Stream pipeline. There are concerns about China's possible use of grey zone tactics – aggressive acts below the level of war, often by seeming non-state actors – to signal its continuing support for Russia. China is said to have used such practices to assert its territorial claims in the South China Sea – often in the form of "accidents" by apparently commercial actors. Despite declaring itself neutral in the Russia-Ukraine war, Beijing has since early 2022 intensified its links to Moscow, buying Russian oil and gas, and selling it a broad range of civilian industrial equipment that has directly and indirectly helped Russia's military campaign.

MERICS analysis: "A Chinese vessel damaging a foreign pipeline appears to be the first event of its kind. Authorities may never prove whether this was an accident involving a commercial vessel or state-sponsored sabotage," said MERICS Analyst **Claus Soong**. "China's geopolitical interest in the Baltic Sea is still developing, but the incident signals its presence there, whether by accident or design."

Media coverage and sources:

- Yle, Finnish Broadcasting Company: Niinistö: China plans to cooperate in gas pipeline investigation
- Politico: 'Everything indicates' Chinese ship damaged Baltic pipeline on purpose, Finland says

- Guancha (CN): 芬兰总统称希望得到中方协助，调查天然气管道受损事故 (The Finnish President hopes to receive assistance from the Chinese side in investigating the incident of damage to the natural gas pipeline)

Evergrande reprieve foreshadows how China may handle property sector crisis

The facts: On December 4, China's massively overleveraged property developer, Evergrande, was given an unexpected reprieve in a Hong Kong court to delay liquidation proceedings until late January 2024. The deal is seen as a way to give Evergrande additional time to organize a restructuring strategy and convince its creditors there is a path forward other than unstructured liquidation of the company. The company, China's largest and most indebted property developer, defaulted on payments in late 2021 and has been subjected to extensive pressure in China and overseas.

What to watch: Evergrande is the most high-profile example of current dysfunctions in China's debt-ridden property sector. How Beijing handles its unravelling will be indicative of how the government responds to the sector more generally. As such, Beijing is trying to straddle a line between an economic or financial crisis on one side and the dangers of moral hazard from a bailout on the other. Beijing has spent the last several years softly bailing out Evergrande by having state-owned enterprises and state-run banks buy the company's assets or take over its ongoing projects to inject the company with liquidity and reduce its more toxic lines of business. At the same time, to mitigate moral hazard risks, regulatory crackdowns and party-initiated corruption campaigns have aimed to punish the company and its leaders.

MERICS analysis: "In effect, Beijing is slow-walking the likely eventual collapse of Evergrande in a way that gives officials time to spread contagion risks across a wider range of firms while still maintaining discipline in the broader deleveraging campaign," says MERICS Lead Analyst **Jacob Gunter**. "However, Beijing can't replicate this model too many times with all of China's worst-behaving property developers – at least not without undercutting the vitality of other economic actors in the name of risk mitigation."

Media coverage and sources:

- Reuters: Evergrande liquidation hearing pushed to Jan, focus on new debt revamp plan
- Caixin: Evergrande liquidation hearing postponed in surprise to lenders
- WSJ: China Evergrande says chairman Hui Ka Yan is suspected of crimes

MERICS CHINA DIGEST

Moody's cuts China credit outlook to negative as economy slows (Guardian)

Rating agency downgraded its outlook for Chinese sovereign bonds from stable to negative on Tuesday. It says Beijing may need to bail out local governments amid the ongoing crisis in the property sector. (23/12/05)

Italy tells China it is leaving Belt and Road Initiative (Reuters)

Italy was the first and so far only major Western nation to join the trade and investment program. Prime Minister Giorgia Meloni stated that she wanted to withdraw from the deal when she took office in 2022. (23/12/07)

China lifts trade barriers it imposed on Lithuania (Taipei Times)

Lithuania became embroiled in a dispute with China in 2021 after allowing Taiwan to set up a "Taiwan" representative office – the first under this name in Europe. China took economic measures, which Lithuania labeled as "economic coercion" and challenged before the WTO. (23/11/30)

Study: "Substantial volume" of clothing tied to Uyghur forced labour entering EU (The Guardian)

Dozens of well-known brands have been identified as being at high risk of sourcing materials, particularly cotton and PVC, made by Uyghurs compelled to participate in state-imposed labor transfer programs, according to a report from Uyghur Rights Monitor, Sheffield Hallam University and the Uyghur Centre for Democracy and Human Rights. (23/12/06)

EDITORIAL TEAM

MANAGING EDITOR

Claudia Wessling
Director Communications
and Publications, MERICS

EDITORS

Ellen Thalman
Freelance editor

Gerrit Wiesmann
Freelance editor

Linda Heyer
Project Manager, MERICS

Hannah Seidl
Communications Manager, MERICS

GRAPHICS

Alexandra Hinrichs
Graphic Designer, MERICS

PUBLISHER

MERICS | Mercator Institute for China Studies
Klosterstraße 64
10179 Berlin
Tel.: +49 30 3440 999 0
Mail: info@merics.de
www.merics.org