COUNCIL on FOREIGN RELATIONS

June 13, 2024

Hearing on "China's Stockpiling and Mobilization Measures for Competition and Conflict"

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Before the

U.S.-China Economic and Security Review Commission
2nd Session, 118th Congress

Hearing co-chairs Commissioner Cliff Sims and Commissioner Carte Goodwin, commission members, and staff, thank you for the opportunity to speak with you today. I commend the commission for calling a hearing on this critical subject. My testimony today will focus on China's attempts to develop an antidote to the West's weaponization of the existing U.S.-led international trade and financial system against China.

The escalation of U.S.-China trade tension since 2018 and G7's sanctions against Russian entities and individuals since 2022, notably the freezing of Russian foreign exchange reserves, have prompted China's policymaking community to strategize immunizing the Chinese economy against Western sanctions and strengthen China's financial security. Despite Western pressure and sanctions against Russia, China continues trading with Russia. During Russian President Putin's visit to Beijing in April 2024, Chinese President Xi Jinping and President Putin strengthened their solidarity.

While criticizing Western sanctions against Russia as having no legal basis, Beijing has been pragmatically evaluating the danger of China's reliance on Western countries for strategic industrial inputs and technology. Unabated U.S.-China geopolitical tensions and Western governments' industrial policies to incentivize firms to reduce supply chain dependence on China have diminished trade between China and the West and fueled concerns among Chinese policymakers and academics about further intended decoupling. The Chinese government has accelerated its development of an anti-sanction policy framework and an alternative global system to prevent China from falling victim to Western sanctions like Russia did.

China's economic growth slowdown and domestic economic wounds will not stop the Communist Party of China and the Chinese government from fortifying defense against potential Western financial sanctions. Such determination is driven by two primary factors: first, the perception of U.S. containment necessitates China's self-sufficiency and strengthened defense against forced decoupling; second, Chinese President Xi prioritizes enhancing China's financial security as integral to national security and aspires to build up China's financial prowess.

I. China's Perceived Necessity to Sanction-Proof the Chinese Economy

In the eyes of Chinese leaders and policymakers, the punitive economic retaliation against Russia by the United States and its allies reveals that global supply chains and the U.S.-led global financial system can be weaponized against China in extreme geopolitical scenarios. However, the economic war against Russia to punish President Putin's invasion of Ukraine is not the only factor that raises Chinese policymakers' concerns about the potential threat of trade and financial weaponization against China. Shortly after President Biden took office, Chinese observers already concluded that the Biden administration's China policy would feature containment, creating demand for China's pursuit of economic and technological self-sufficiency.

One year into the Biden administration – that was before the West's collective sanctions to punish President Putin's war against Ukraine – Chinese academics and state media perceived U.S. policy towards China as containment. For example, in June 2021, Zhang Monan, a chief researcher at China Center for International Economic Exchanges, a public policy think tank operating under the National Development and Reform Commission, observed that "Biden's China containment policy will go further than Trump."[1] In August, the Bureau of Development and Planning of China Academy of Sciences wrote, "The focus of the U.S. Innovation and Competition Act of 2021 is to contain and compete with China in science and technology, centered on digital technologies such as semiconductors and 5G."[2] Also in August, Xinhua, China's leading state media, quoting Chinese academics, described the trips to Southeast Asia by senior officials in the Biden administration, such as Secretary of Defense Austin and Vice President Kamala Harris, as "the United States seeking to woo Southeast Asia to contain China"[3] with quotes from Chinese academics. In January 2022, the Chongyang Institute for Financial Studies at Renmin University published an article arguing that containing China has become a "new normal" in U.S. policymaking calculations.[4]

In this context, Chinese policymakers have become convinced that the United States is determined to implement a full-fledged strategy of containment against China before the West's punitive sanctions against Russian individuals and entities following President Putin's war against Ukraine. Naturally, Chinese officials, academics, and media rhetoric increasingly talk of self-reliance and are preparing for a forced decoupling from the United States. Fang

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[1] "Zhang Monan: Biden's China Containment Policy Will go Further Than Trump's" (张茉楠：拜登的遏华政策将比特朗普走得更远), fisnet.com, June 30, 2021, http://comment.cfisnet.com/2021/0630/1323271.html.

[2] "Science & Technology Policy & Consulting: The American Innovation and Competitiveness Act of 2021 Targets Technology Competition with China," Bureau of Development and Planning of China Academy of Sciences, August 5, 2021, http://www.casisd.cn/zkcg/ydkb/kjzcyzxkb/2021/zczxkb_202108/202110/P020211009319571471401.pdf.

[3] "The U.S.'s Attempt to win Over Southeast Asia to Contain China is Unlikely to Succeed" (美国拉拢东南亚 遏华图谋难得逞), *Xinhuanet*, August 21, 2021, http://www.xinhuanet.com/world/2021-08/21/c_1127783060.htm.

[4] "Cai Tongjuan: The New Normal of U.S. Containment of China Has Emerged. How Should China Respond?" *Chongyang Institute for Financial Studies, Renmin University*, January 25, 2022, http://rdcy.ruc.edu.cn/zw/zl/0254c474c1d8424c98ec5fa2465c00bd.htm.

Xinghai, a vice chairman of the China Securities Regulatory Commission, proposed accelerating the yuan's internationalization to prepare for the risk of forced financial decoupling.[5] Even the more moderate voices have acknowledged the profound changes in U.S.-China relations behind the "decoupling theory" and called for China to "prepare for the worst but strive for the best."[6] Under the leadership of President Xi, the Communist Party of China made "independence and self-reliance" a centerpiece in the landmark Historic Resolution enacted in 2021.[7] On February 25, 2022, one day after President Putin's invasion of Ukraine, the *People's Daily* published an editorial that wrote, "Independence and self-reliance ensure that the cause of the Party and the people will continue to move from victory to victory."[8]

Beijing views the Biden administration's regional arrangements in the Indo-Pacific region as destabilizing and undermining China's interests. For Beijing, the Indo-Pacific Economic Framework for Prosperity is the economic mirror of the Quadrilateral Security Dialogue and AUKUS, two U.S.-led security pacts that Beijing regards as anti-China coalitions. In May 2022, as President Biden embarked on his first trip to Asia since taking office to visit Korea and Japan, Xinhua characterized U.S. policies towards the Indo-Pacific region as "exhibiting new features of an integrated China containment policy across multiple dimensions" (美遏华战略呈现多领域一体布局的新特征).[9] In June, the Ministry of Foreign Affairs characterized America's China policy as an attempt at "comprehensive containment and suppression of China" in a statement entitled "Fallacies and Truth in America's Perception of China" (美国对华认知中的谬误和事实真相).[10]

Beijing also views America's industrial policies, such as the CHIPS Act and the Inflation Reduction Act, and U.S. trade and investment restrictions from export controls to inbound and outbound investment screenings as tools of economic and technological containment against China. *Global Times* criticized U.S. chip export restrictions as aiming to "suppress and contain the rise of Chinese technology to preserve U.S. hegemony" and quoted expert opinions saying "domestic production in related industries has already become an industry consensus in China."[11] Researchers at the Bank of China Research Institute and China Institutes of Contemporary International Relations commented that America's "yard and fence harm global supply chains" and that "U.S. industrial policies have China as the primary target of containment and suppression."[12] With the ongoing hot war in Europe and a cold war in economic and technology competition, a Shanghai-based academic argued that "the peace dividend is over"—hence, "it is time that China prepare for a full decoupling."[13]

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[5] "Fang Xinghai: China Must be Prepared for the Risk of Being Cut Off From the U.S. Dollar Payment System" (方星海：中国必须为被切断美元支付体系的风险做好准备), *The Chinese American Professors and Professionals Network,* July 2, 2020, http://scholarsupdate.hi2net.com/news.asp?NewsID=27803.

[6] "Observations and Reflections on the Current Sino-U.S. 'Decoupling Theory'" (对当前中美"脱钩论"的观察与思考), *People's Forum Academic Frontiers,* May 29 2020, http://www.rmlt.com.cn/2020/0529/581929.shtml.

[7] "Full Text: Resolution of the CPC Central Committee on the Major Achievements and Historical Experience of the Party Over the Past Century," *The State Council of the People's Republic of China,* Updated November 16, 2021, https://english.www.gov.cn/policies/latestreleases/202111/16/content_WS6193a935c6d0df57f98e50b0.html.

[8] "Adhere to Independence and Self-Reliance to Open up the Road Ahead (Special Topic for Deep Reflection)" (坚持独立自主开拓前进道路（专题深思）), *People's Daily Online,* February 25, 2022, http://hb.people.com.cn/n2/2022/0225/c194063-35148981.html.

[9] "The United States' Containment of China Has a New Feature of a Multi-Field Integrated Layout" (美国遏华呈多领域一体布局新特征), *Xinhuanet,* May 20, 2022, http://www.xinhuanet.com/world/2022-05/20/c_1211649146.htm.

[10] "The Fallacies and Truths in the U.S.'s Perception of China" (美国对华认知中的谬误和事实真相), *Ministry of Foreign Affairs News,* June 19, 2022, https://www.mfa.gov.cn/wjbxw_new/202206/t20220619_10706065.shtml.

[11] "Tearing Off the Mask of Free Competition and Curbing China's Technological Development, how Many 'Devils' are Hidden in the U.S. 'Chips Act'?" (撕下自由竞争面具，遏制中国技术发展，美"芯片法案"藏着多少"魔鬼"？), *Global Times,* August 15, 2022, https://world.huanqiu.com/article/49FvK8I1mg9.

[12] "American-Style 'Guardrails'" Harm to the Global Industrial Chain" (美式"护栏"：全球产业链之害), *China Trade Remedies Information, Ministry of Commerce People's Republic of China,* September 28, 2022, https://cacs.mofcom.gov.cn/article/flfwpt/jyjdy/cgal/202209/174513.html.

[13] "'The Peace Dividend Has Ended, and it is Time for China to Prepare for a Comprehensive Decoupling': Thoughts of a Shanghai Professor" ("和平红利已终结, 中国到了不得不准备全面脱钩的时候": 一位上海教授的思考), *NetEase,* June 2, 2022, https://www.163.com/dy/article/H8T28O5Q052100BV.html.

Chinese scholars and policymakers are ideologically prepared for a forced decoupling from the West despite knowing that decoupling undermines China's interests. They have debated the necessity of reforming the dollar-based global financial system and diversifying away from dollar assets overseas. The Chinese government has taken concrete steps to develop the renminbi's pricing power in major global commodities. The People's Bank of China and its affiliates have been working on developing an alternative financial system with the digital renminbi at the center. China's legislatures have designed an anti-sanctions regulatory framework to deter and penalize cooperation with foreign sanctions against Chinese entities and individuals. Besides these defensive measures, the Chinese state has also identified offensive retaliatory measures by weaponizing China's critical position in global supply chains.

II. Chinese President Xi Jinping's Emphasis on Financial Security and Financial Power

Since President Xi Jinping came to power in 2013, he has repeatedly emphasized worst-case scenario thinking to "prevent macro-risks that may delay or interrupt the process of the great rejuvenation of the Chinese nation."[14] From Xi's vantage point, China's state-owned financial institutions and enterprises must inoculate themselves in advance against more disastrous international sanctions that might be levied against them in the event of a military conflict with the West over Taiwan. That concern has only grown more urgent after China witnessed the collective sanctions imposed by the West on Russian entities and individuals to punish President Vladimir Putin for his war against Ukraine.

Financial security is a core aspect of President Xi's "Comprehensive National Security." When addressing a Politburo study group in April 2017, Xi Jinping, as the General Secretary of the Party, emphasized that "financial security is an important part of national security. Protecting financial security is strategic and fundamental to China's overall economic and social development."[15] However, it is important to note that President Xi did not invent financial security as national security. In fact, financial security has become an indispensable part of China's national security discourse since the 1997 Asian financial crisis. Addressing the National Finance Work Conference in November 1997, President Jiang Zemin stressed that "ensuring financial security, efficiency, and stability is a basic prerequisite for the sustained rapid development of the national economy."[16] Jiang warned, "If the financial system is unstable, it would inevitably affect economic and social stability." Jiang's speech reflected the normative impact of the Asian financial crisis on the conceptualization of national security, financial governance, and financial risk management among the third generation of the Communist Party of China's (CPC) leadership. Awakened by the severity of the crisis, CPC leaders realized for the first time that national security could not be narrowly defined only by military competencies and defense capabilities but must also include financial security.

Under President Xi's leadership, defending China's financial security means not only managing market risks but also geopolitical risks. Developing alternative systems to hedge sanction risk and reduce China's strategic vulnerabilities due to its dependence on the U.S. dollar in international trade and investment has become a priority of the CPC. At the October 2023 Central Finance Work Conference, Xi reiterated that "preventing and managing risk is a perpetual theme of financial work" and elaborated on the geopolitical challenges to China's financial security.[17] He observed that "a small number of countries treat finance as tools for geopolitical games. They repeatedly played with currency hegemony and frequently wielded the big stick of financial sanctions. … All these have presented new challenges to

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[14] "General Secretary Xi Jinping on Bottom-Line Thinking" (习近平总书记论底线思维), *China Communist Party News Network,* August 22, 2023, http://theory.people.com.cn/n1/2023/0822/c40531-40061461.html.
[15] "Financial Security is an Important Part of National Security" (金融安全是国家安全的重要组成部分), *China Communist Party News Network,* April 28, 2017, http://theory.people.com.cn/n1/2017/0428/c40531-29244246.html.
[16] "Jiang Zemin: Deepen Financial Reform and Guard Against Financial Risks" (江泽民：深化金融改革，防范金融风险), *Selected Works of Jiang Zemin Volume 2 (江泽民文选第二卷),* November 19, 1997, http://www.reformdata.org/1997/1119/5723.shtml.
[17] "The Ministry of State Security Issued a Statement: Be a Firm Guardian of Financial Security" (国安部公号发文：做金融安全的坚定守护者), *Caixin,* November 3, 2023, https://china.caixin.com/2023-11-03/102124204.html.

maintaining financial security under the new situation."

President Xi's recent speech suggests that he views improving the renminbi's international status as an indispensable component of strengthening China's financial security. In January 2024, President Xi urged leading cadres at provincial and ministerial levels to strengthen China's financial power and listed "powerful currency" as the top priority among several core financial factors.[18] He called on Chinese officials to promote China-governed financial infrastructures that are safe and efficient to improve China's financial autonomy.

III. China's Strategies to Reduce its Strategic Vulnerability to the Dollar Hegemony

In response to Chinese policymakers' anxieties over the country's financial security, China in recent years has accelerated its development of an alternative global financial system independent of the dollar to fortify its economy against potential sanctions. The Chinese government has pursued three primary strategies to push for reforming the existing U.S.-led system while developing an alternative. One strategy has been to support and expand regional and multilateral currency and financial cooperation through various non-Western partnerships. The second strategy has been to increase the broader use of the renminbi in international trade and investment while promoting renminbi-based international financial infrastructure. The third strategy is to improve the renminbi's role in global commodities pricing, especially in the context of the clean energy transition.

1. Promote Regional and Multilateral Currency and Financial Cooperation

The 1997 Asian financial crisis drove demand for a regional currency arrangement to address short-term liquidity difficulty for regional members and reduce reliance on the International Monetary Fund (IMF). Japanese finance authorities proposed establishing an Asian Monetary Fund (AMF) but failed due to the U.S. government's opposition. In May 2000, ASEAN+3 (China, Japan, and South Korea) managed to launch the Chiang Mai Initiative (CMI), the first regional currency swap arrangement, as an incremental step and laid the foundation for continued regional currency cooperation.[19] The CMI is composed of the ASEAN Swap Arrangement among ASEAN countries and a network of bilateral swap arrangements among ASEAN+3 countries.

A decade later, in May 2008 amid the 2007-2008 global financial crisis, ASEAN+3 (China, Japan, and South Korea) finance ministers agreed to establish a regional foreign exchange reserves pool with a minimum amount of $80 billion,[20] which later increased to $120 billion[21] with China and Japan each contributing $38.4 billion (each 32%) and South Korea $19.2 billion (16%).[22] In December 2009, an Asian regional foreign exchange reserves pool was launched, a step closer to an AMF. In March 2010, ASEAN+3 finance ministers and central bank governors meeting clarified that countries could implement local currencies – U.S. dollar swaps in the $120 billion collective regional foreign exchange reserves pool. In May 2012, the size of the regional foreign exchange reserves pool increased to $240 billion.

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[18] Xi Jinping Delivered an Important Speech at the Opening Ceremony of the Seminar for Provincial and Ministerial-Level Leading Cadres on Promoting High-Quality Financial Development" (习近平在省部级主要领导干部推动金融高质量发展专题研讨班开班式上发表重要讲话), *The State Council of the People's Republic of China,* January 16, 2024, https://www.gov.cn/yaowen/liebiao/202401/content_6926302.htm.
[19] Chalongphob Sussangkarn, "The Chiang Mai Initiative Multilateralization: Origin, Development and Outlook" (ADBI Working Paper 230, Tokyo: Asian Development Bank Institute, July 2010), https://www.adb.org/sites/default/files/publication/156085/adbi-wp230.pdf.
[20] "China, Japan, South Korea and ASEAN Jointly Pledge US$80 Billion to Combat Financial Risks" (中日韩和东盟 800 亿美元共御金融风险), *Sina News,* May 6, 2008, https://news.sina.com.cn/o/2008-05-06/074813836007s.shtml.
[21] "The ASEAN+China, Japan and South Korea (10+3) Special Finance Ministers' Meeting was Held in Thailand on the 22nd" (东盟+中日韩(10+3)特别财长会议 22 日在泰国举行), *The Central People's Government of the Republic of China,* February 24, 2009, https://www.gov.cn/gzdt/2009-02/24/content_1241525.htm.
[22] "The Forty-Second Annual Meeting of the Board of Governors of the Asian Development Bank: Summary of Proceedings," Document No. BG42-1, *Asian Development Bank,* May 2009, https://www.adb.org/sites/default/files/institutional-document/771541/annual-meeting-2009-proceedings.pdf.

In dealing with the economic shocks of the COVID-19 pandemic, at the G20 meeting in February 2022, PBoC Governor Yi Gang said that China would work with Asian countries to promote the use of local currencies in trade and investment to strengthen regional financial security and resilience against external shocks.[23] In June, the PBOC and the Bank for International Settlement launched an RMB Regional Liquidity Arrangement,[24] with the participation of Bank Indonesia, the Central Bank of Malaysia, the Hong Kong Monetary Authority, the Monetary Authority of Singapore, and the Central Bank of Chile. This arrangement has since become an additional liquidity support for participating central banks in times of market volatility.

The Chinese government has actively cooperated with non-Western multilateral partnerships, such as the Shanghai Cooperation Organization (SCO)[25] and BRICS,[26] to develop a non-dollar-based financial system and promote the use of local currencies in trade and investment. Following the West's punitive sanctions against Russian entities and individuals to punish Putin's war against Ukraine, the Chinese government has sought to capitalize on concerns among members of the Global South over the West's sanctions, especially the freezing of Russian reserves. An important agenda behind China's support of the expansion of non-Western regional and multilateral partnerships, such as the SCO and BRICS, has been to accelerate the expansion of a non-dollar-based system. For example, at the September 2022 SCO Summit, Chinese President Xi Jinping proposed[27] to expand the shares of local currency settlements to promote regional integration, strengthen the development of local-currency cross-border payment and settlement systems, and promote the establishment of an SCO development bank. SCO members agreed on a "roadmap" to expand trade in local currencies.[28] Iran – whose regime has been coping with severe Western sanctions and firmly in favor of de-dollarization– has joined the SCO as its ninth full member. Iranian President Ebrahim Raisi made it clear that Tehran sees SCO membership as a way to help thwart American unilateralism and bypass sanctions.[29]

China's expressed interest in using the SCO framework to promote the use of local currency for bilateral trade and settlement already emerged before the launch of the Belt and Road Initiative in 2013. Following the 2007-2008 global financial crisis, promoting the use of local currencies in bilateral trade has become an important issue in China's partnership with SCO members, which has received support from SCO members. For example, at the 2012 SCO Business Forum, Vice Premier Wang Qishan stressed that SCO members should promote using local currencies in trade settlement, advance bilateral currency swaps, strengthen regional financial cooperation, and develop new financing models.[30]

2. Promote the cross-border use of renminbi and renminbi-based financial infrastructure

Besides collaborating with regional and multilateral groups to pursue the development of a non-dollar-based system,

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[23] "China to Work With Asian Nations to Grow Use of Local Currencies in Trade," *Reuters,* February 15, 2022, https://www.reuters.com/world/china/china-work-with-asian-peers-boost-use-local-currencies-trade-2022-02-16/.
[24] "BIS Announces Renminbi Liquidity Arrangement," *Bank for International Settlements,* June 25, 2022, https://www.bis.org/press/p220625.htm.
[25] Zongyuan Zoe Liu, "China Is Quietly Trying to Dethrone the Dollar," *Foreign Policy,* September 21, 2022, https://foreignpolicy.com/2022/09/21/china-yuan-us-dollar-sco-currency/.
[26] Zongyuan Zoe Liu and Mihaela Papa, *Can BRICS De-dollarize the Global Financial System?* (Cambridge University Press, February 2022), https://www.cambridge.org/core/elements/can-brics-dedollarize-the-global-financial-system/0AEF98D2F232072409E9556620AE09B0.
[27] "Xi Jinping's Speech at the 22nd Meeting of the Council of Heads of State of the Shanghai Cooperation Organization" (习近平在上海合作组织成员国元首理事会第二十二次会议上的讲话（全文)), *Xinhua News Agency,* September 16, 2022, https://www.gov.cn/xinwen/2022-09/16/content_5710294.htm.
[28] "China-Led SCO Bloc Agrees to Expand Trade in National Currencies," *Reuters,* September 16, 2022, https://www.reuters.com/markets/commodities/china-led-sco-bloc-agrees-expand-trade-national-currencies-2022-09-16/.
[29] "Iran Can Thwart U.S. Sanctions Via Shanghai Organization," *Iran International,* September 16, 2022, https://www.iranintl.com/en/202209162127.
[30] "Wang Qishan Attended the Opening Ceremony of the Shanghai Cooperation Organization Business Forum and Delivered a Speech" (王岐山出席上海合作组织工商论坛开幕式并致辞), *The Central People's Government of the People's Republic of China,* June 6, 2012, https://www.gov.cn/ldhd/2012-06/06/content_2154772.htm.

the Chinese government also attempted to improve the cross-border use of renminbi since the 2007-2008 global financial crisis. In July 2009, Chinese financial regulators and central government agencies promulgated "Administrative Rules on Pilot Program of Renminbi Settlement of Cross-border Trade Transactions," allowing qualified Chinese enterprises designated by the state to settle cross-border trade in renminbi.[31] The Rules marked China officially taking the first step to promote greater international use of the renminbi, with the goal of ultimately establishing the Chinese currency as an international reserve currency alongside the U.S. dollar and the euro.

The Chinese government has put resources into developing renminbi-based financial infrastructure to facilitate the cross-border use of the renminbi. Launched in 2015, CIPS has become a proprietary financial infrastructure that could allow sanctioned entities to plumb into global markets, although dodging sanctions was not the original motivation for its introduction. Initially developed as a critical piece of financial infrastructure to promote yuan internationalization,[32] the Shanghai-based CIPS is increasingly seen as China's alternative to SWIFT[33] even before Russian banks were recently kicked off SWIFT. CIPS allows global banks to clear cross-border renminbi transactions onshore instead of through offshore renminbi clearing banks, providing a one-stop alternative to the combination of the SWIFT messaging system and the New York-based Clearing House Interbank Payments System. However, CIPS is not a complete departure from SWIFT and still uses SWIFT's standards to connect with the global system. It has adopted the ISO 2022 international payments messaging standard in order to make it interoperable with other payment systems as well as with correspondent banks around the world.[34] The adoption of the existing cross-border messaging standards serves China's interest in making CIPS a critical piece of financial infrastructure to promote the international use of the renminbi. According to the CIPS website, CIPS currently has 139 direct participants, 100 of which are in Asia, 23 in Europe, 6 in Africa, 5 in Oceania, 3 in North America, and 2 in South America.[35] In 2023, CIPS's annual business volume reached RMB123 trillion.[36] By January 2024, CIPS's average daily transaction volume reached RMB666.8 billion ($93.6 billion). [37]

The Chinese state has accelerated the development of alternative financial infrastructure as a hedging strategy due to mounting concerns over being isolated from the U.S.-led global financial system as tensions between the United States and China have escalated since 2018. The PBoC has cooperated with SWIFT to get localized services, which in theory could mitigate the impact of sanctions. In August 2019, SWIFT set up a wholly foreign-owned unit in Beijing that uses renminbi for its services and products in China and provides the Chinese financial community with localized and customized services.[38] In January 2021, the PBoC and SWIFT launched a €10 million ($12 million) joint venture named Finance Gateway Information Services (FGIS),[39] shortly after the United States, the European Union, U.K., and Canada sanctioned several Chinese officials for human rights abuses against the Uyghurs. FGIS will build a local network for financial messaging services and establish a localized data warehouse to store, monitor, and analyze cross-border payment messaging information.[40] Notably, the CIPS and Digital Currency Research Institute are FGIS

[31] "The People's Bank of China, the Ministry of Finance, the State Administration of Taxation, the China Banking Regulatory Commission Announcement [2009] No. 10" (中国人民银行 财政部 商务部 海关总署国家税务总局 中国银行业监督管理委员会公告〔2009〕第 10 号), *The Central People's Government of the People's Republic of China,* July 2, 2009, https://www.gov.cn/zwgk/2009-07/02/content_1355475.htm.
[32] "Report on the Internationalization of the RMB (2015)" (人民币国际化报告 (2015 年)), *People's Bank of China,* June 2015, http://www.pbc.gov.cn/eportal/fileDir/image_public/UserFiles/goutongjiaoliu/upload/File/人民币国际化报告（2015 年）.pdf.
[33] "China's Fledgling Cross-Border Payments System Grows Its Reach," *Bloomberg,* September 22, 2021, https://www.bloomberg.com/news/articles/2021-09-22/china-s-fledgling-cross-border-payments-system-grows-its-reach?embedded-checkout=true.
[34] "CIPS Accelerates the Internationalization of the RMB," *Swift,* October 28, 2016, https://www.swift.com/news-events/news/cips-accelerates-internationalisation-rmb.
[35] "CIPS Global Services," *CIPS,* 2024, https://www.cips.com.cn/.
[36] "Cross-Border Interbank Payment System," *CIPS,* 2024, https://www.cips.com.cn/en/index/index.html.
[37] Ibid.
[38] "SWIFT Opens Wholly Owned Subsidiary in China," *China Daily,* August 9, 2019, https://www.chinadaily.com.cn/a/201908/09/WS5d4d268da310cf3e35564de4.html.
[39] "PBoC JV with Swift May Signal Bid to Boost Digital Yuan's Reach," *Asia Financial,* February 10, 2021, https://www.asiafinancial.com/pboc-jv-with-swift-may-signal-bid-to-boost-digital-yuans-reach.
[40] "PBoC, SWIFT to Establish Cross-Border Payment Stability," *Regulation Asia,* March 25, 2021, https://www.regulationasia.com/pboc-swift-to-establish-cross-border-payment-stability/.

shareholders. Their presence suggests that FGIS is empowered to promote the use of digital yuan in cross-border transactions. Once materialized, this could be another damage control mechanism if major Chinese banks were de-SWIFTed.

It is currently unclear whether a localized messaging network combined with a localized data warehouse would be sufficient to achieve netting settlement services for cross-border payments and thereby help China circumvent U.S. sanctions. However, the participating Chinese shareholders can reveal the technical potential of this joint venture. Apart from SWIFT's €5.5 million investment for a 55% stake, the joint venture's primary Chinese shareholder is China National Clearing Center, which invested €3.4 million euros for a 34% stake. Other Chinese shareholders include CIPS (Cross-border Interbank Payment System), DCRI (Digital Currency Research Institute), and PCAC (Payment & Clearing Association of China, an industry self-regulatory agency under the PBoC).[41] The participation of CIPS and DCRI accentuates the potential of the joint venture to promote a renminbi-based financial system and boost the cross-border use of the digital renminbi.

In January 2023, the Ministry of Commerce and the PBoC jointly issued a policy notice to encourage Chinese firms engaging in international trade and investment to use renminbi in their cross-border settlement and investment.[42] The policy notice also encouraged Chinese banks to extend overseas renminbi loans. Over thirty countries have started to use the renminbi for cross-border trade and settlement.[43] Major Chinese oil suppliers, such as Russia, Angola, Venezuela, Iran, and Nigeria, now accept renminbi in their oil trade with China.

3. Improve the renminbi's commodities pricing power.

Although China has laid down the renminbi-based financial infrastructure for the international use of the renminbi and has achieved settling commodities trade using the renminbi with over thirty countries,[44] the renminbi's commodities pricing power remains limited. The major commodity pricing centers are in New York, Chicago, and London, with the U.S. dollar dominating about 90 percent of the pricing of major commodities in global markets.[45] Chinese policymakers have publicly expressed their concerns about the renminbi's limited pricing power over commodities.[46]

Chinese policymakers are right to consider improving renminbi's pricing power in global commodities markets as an essential component to boost China's financial power. China is the world's largest consumer of fossil fuels[47] and dominates the supply chains of several highly sought-after critical minerals deemed critical for the clean energy transition, such as cobalt and rare earth minerals, which cannot be easily substituted by other materials using existing technology in the clean energy transition. Making the renminbi the pricing currency of major commodities powering the global economy is a crucial step to constructing a renminbi-based global commodities trading system, which could

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[41] "PBoC JV with Swift may signal bid to boost digital yuan's reach," *Asia Financial*, February 10, 2021, https://www.asiafinancial.com/pboc-jv-with-swift-may-signal-bid-to-boost-digital-yuans-reach.
[42] "The Ministry of Commerce and the People's Bank of China Jointly Issued the, 'Notice on Further Supporting Foreign Trade Enterprises to Expand the Cross-Border Use of RMB and Promote Trade and Investment Facilitation" (商务部 中国人民银行联合印发《关于进一步支持外经贸企业扩大人民币跨境使用 促进贸易投资便利化的通知》),*Macroprudential Policy Bureau of the People's Bank of China,* January 11, 2023, http://www.pbc.gov.cn/huobizhengceersi/214481/214511/3406535/4763611/index.html.
[43] "Major Good News! More Than 30 Countries Have Started Using RMB for Settlement. Do You Know Which Countries They Are?" (**关注 |** 重大利好！30 多国**启用**"人民币"结算，你知道都是哪些国家吗？), *InvestGo.cn,* March 31, 2023, https://www.investgo.cn/article/yw/zctz/202303/662141.html.
[44] Ibid.
[45] "The Evolution of Global Commodity Pricing Mechanism and China's Countermeasures" (全球大宗商品定价机制演进 及中国对策), *Bank of China,* July 16, 2021, https://pic.bankofchina.com/bocappd/rareport/202107/P020210716602228280859.pdf.
[46] Xingqiang Liu, "Why Don't We Havve Global Commodity Pricing Power?" (为什么我们没有全球商品定价权?), *China Economic Weekly,* no. 50 (2010), http://paper.people.com.cn/zgjjzk/html/2010-12/27/content_710445.htm?div=-1.
[47] David Stanway, "China Climate Envoy Says Phasing Out Fossil Fuels 'Unrealistic'," *Reuters,* September 22, 2023, http://paper.people.com.cn/zgjjzk/html/2010-12/27/content_710445.htm?div=-1.

reduce China's economic and geopolitical vulnerabilities in the global resources trade, elevate China's influence in the global financial system, and strengthen China's financial security. In this context, improving the role of the renminbi in global commodities pricing is not just a critical step towards renminbi internationalization but also an essential condition to reduce China's strategic vulnerabilities.

In this context, China has developed several commodities trading platforms, such as the renminbi-denominated futures market and commodity exchanges. For example, China launched renminbi-denominated oil futures in 2018[48] and copper futures in 2020[49] on the Shanghai International Energy Exchange. It also launched the Ganzhou Rare Metal Exchange in 2019,[50] where China's renminbi currency is used to quote prices for spot trading of tungsten, rare earth products,[51] and critical minerals (like cobalt) that are essential to the clean energy transition. The Shanghai crude oil futures market has already risen to the third-biggest oil futures market by trading volume,[52] behind West Texas Intermediate and Brent, but it is surpassing comparable offerings traded in Singapore and Dubai by a significant margin.

The commodities trading platforms and financial instruments provide marketplaces for the emergence of a renminbi-based commodities trading and settlement system. When addressing the China-Gulf Cooperation Council (GCC) Summit in December 2022, Chinese President Xi Jinping emphasized that China and members of the GCC should deepen cooperation in using the renminbi in oil and natural gas trading and settlement through the Shanghai Petroleum and Natural Gas Exchange (SHPGX).[53] The recent expansion of BRICS supported by China, especially the inclusion of commodities majors such as UAE and Iran, opens up new avenues for members to pursue the use of local currency in commodities pricing and trading. This expansion allows China opportunities to boost the renminbi's commodities pricing power and erode the U.S. dollar's dominance in global commodities markets.

Since Xi's speech, Chinese national oil and gas companies have accelerated initiatives to use the renminbi, instead of the U.S. dollar, in their international fossil fuels transactions through SHPGX. In March 2023, China National Offshore Oil Corporation — known as CNOOC, China's largest offshore oil and gas field operator — used the renminbi to complete the transaction of importing 65,000 metric tons of liquefied natural gas (LNG) from TotalEnergies SE, a French multinational oil and gas company, through SHPGX.[54] The LNG was produced in the United Arab Emirates, a member of the GCC, carried by a Liberian-flagged LNG tanker Mraweh,[55] and finished unloading in May[56] at the CNOOC Guangdong Dapeng LNG receiving station. This transaction was the world's first cross-border LNG trade settled using the renminbi. Since then, CNOOC has executed more renminbi-settled transactions using the renminbi through SHPGX.[57] In October, PetroChina, the largest oil and gas producer and distributor in China, settled a purchase of one million barrels of crude oil using the digital renminbi through SHPGX,

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[48] "China Launches Crude Oil Futures Trading," *XinhuaNet,* March 26, 2018, http://www.xinhuanet.com/english/2018-03/26/c_137065815.htm.
[49] Tom Daly, Mai Nguyen, and Emily Chow, "China's New Copper Futures Add Another Card to Global Yuan Deck," *Reuters,* November 17, 2020, https://www.reuters.com/article/china-derivatives-copper/rpt-chinas-new-copper-futures-add-another-card-to-global-yuan-deck-idUKL1N2I30GE/.
[50] "China's First Rare Earth Exchange Opens in Ganzhou" (全国首家稀交所在赣州开业), *XinhuaNet,* January 2, 2020, http://m.xinhuanet.com/jx/2020-01/02/c_1125413757.htm.
[51] "Ganzhou Rare Metal Exchange," *gzrme.com,* 2024, https://www.gzrme.com/#/ResourceDocuments.
[52] "2023 RMB Internationalization Report," *People's Bank of China,* http://www.pbc.gov.cn/en/3688241/3688636/3828468/4756463/5163932/2023120819545781941.pdf.
[53] "Xi Jinping's Keynote Speech at the China-Gulf Cooperation Council Summit" (习近平在中国—海湾阿拉伯国家合作委员会峰会上的主旨讲话), *The State Council of the People's Republic of China,* December 10, 2022, https://www.gov.cn/xinwen/2022-12/10/content_5731130.htm.
[54] "China's First Cross-Border LNG Shipment, Settled in Yuan, Completes Offloading," *Global Times,* May 16, 2023, https://www.globaltimes.cn/page/202305/1290796.shtml.
[55] "Mraweh," *Marine Traffic,* accessed May 2024, https://www.marinetraffic.com/en/ais/details/ships/shipid:752790/mmsi:636010457/imo:9074638/vessel:MRAWEH.
[56] Zheng Xin, "China's First Yuan-Settled LNG Trade Unloaded From UAE," *China Daily,* updated May 16, 2023, https://www.chinadaily.com.cn/a/202305/16/WS646369f3a310b6054fad34c2.html.
[57] "Chinese Major CNOOC and French Energy Company Engie Settle LNG Trade in Yuan on Shanghai Exchange," *LNG Journal,* October 18, 2023, https://lngjournal.com/index.php/latest-news-mainmenu-47/item/109586-chinese-major-cnooc-and-french-energy-company-and-utility-engie-settle-lng-trade-in-yuan-on-shanghai-exchange.

marking the first cross-border oil transaction using the country's central bank's digital currency.[58]

In the near-to medium-term, China could capitalize on the current energy transition to cultivate a "gas-yuan," emulating the petrodollar. Just as oil-producing countries depend on dollar revenues that aren't freely spendable elsewhere, gas-producing ones such as Russia and Iran could be dependent on the renminbi. In China's "World Energy Development Report (2017)," Chinese scholars proposed the concept of gas-yuan. Given the fragmented nature of global natural gas markets and China's leverage as a leading buyer, the emergence of the gas-yuan is not a pipe dream. Russia, Iran, and China collectively produce more natural gas than the United States[59] and they all have non-dollar financial infrastructure in place. China has become the world's largest LNG importer.[60] Iran, which shares the world's biggest gas field with Qatar, is reviving its previously sanction-stalled LNG export plan[61] as the E.U. attempts to cut its dependence on Russian gas as a punishment for President Putin's invasion of Ukraine. Although China has not provided material support to Russia or bluntly helped Russia dodge Western sanctions, China's natural gas imports from Russia more than doubled in 2022 from 2021.[62] The collective revisionist geoeconomic power of China, Russia, and Iran arguably is much stronger than that of the OPEC. Higher global demand for natural gas as a transition fuel towards Net Zero and the decoupling of gas prices from oil prices also provide a benign macro condition for the emergence of a gas-yuan.

In the medium-to-long run, China could also leverage its dominance in critical mineral supply chains and its partnership with mineral-rich countries as the global economy transitions from hydrocarbon-dependent to mineral-dependent. SCO members include major hydrocarbon and minerals exporters in Central Asia like Kazakhstan and Uzbekistan, Russia and its newest member, Iran.[63] SCO also includes major commodities importers like China and India. Two of the world's five largest lithium producers —China and Brazil — are members of BRICS. Iran, a member of both SCO and BRICS, announced last February the discovery of its first lithium deposits,[64] estimated to be the world's second-largest after Chile.[65] Iran already possesses[66] the world's largest proven[67] zinc reserves that are extractable using existing technology, the fifty-largest copper deposits,[68] the 10th-largest uranium reserves, and the 10th-largest iron ore reserves.[69] The Iranian regime has been coping with severe Western sanctions for decades and is firmly in favor of de-dollarization.

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[58] Shi Jing, "Crude Oil Deal in e-CNY Marks Breakthrough," *China Daily,* October 21, 2023, https://global.chinadaily.com.cn/a/202310/21/WS65330f53a31090682a5e9ddb.html.
[59] "Natural Gas Production," *World Energy & Climate Statistics—Yearbook 2023,* 2023, https://yearbook.enerdata.net/natural-gas/world-natural-gas-production-statistics.html.
[60] Keefe Borden, "China Becomes World's Largest LNG Importer," *Compressor Tech²,* December 20, 2021, https://www.compressortech2.com/news/china-becomes-world-s-largest-lng-importer/8017084.article.
[61] Patrick Sykes, "Iran Revives LNG Export Plan as World Scrambles for Natural Gas," *Bloomberg,* March 15, 2022, https://www.bloomberg.com/news/articles/2022-03-15/iran-revives-lng-export-plan-as-world-scrambles-for-natural-gas?embedded-checkout=true.
[62] "China's Gas Imports From Russia Double in 2022 Amid Ukraine Crisis," *Kyodo News,* January 20, 2023, https://english.kyodonews.net/news/2023/01/7c9c6997d76f-chinas-gas-imports-from-russia-double-in-2022-amid-ukraine-crisis.html.
[63] Sudhi Ranjan Sen, "Iran Joins SCO, the China-Founded Regional Security Grouping," *Bloomberg,* July 4, 2023, https://www.bloomberg.com/news/articles/2023-07-04/iran-joins-sco-the-china-founded-regional-security-grouping?sref=51J26SiN&embedded-checkout=true.
[64] Kit Million Ross, "Iran Claims to Have Discovered 8.5 Million-Ton Lithium Deposit," *Mining Technology,* March 7, 2023, https://www.mining-technology.com/news/iran-discovers-major-lithium-deposit/.
[65] "These Countries Are Driving Lithium Production," *McKinsey & Company,* May 25, 2022, https://www.mckinsey.com/featured-insights/sustainable-inclusive-growth/chart-of-the-day/these-countries-are-driving-lithium-production.
[66] "Iran's Mineral Output: 258m Tons in 10 Months," *Financial Tribune,* February 5, 2017, https://financialtribune.com/articles/economy-business-and-markets/58965/iran-s-mineral-output-258m-tons-in-10-months#:~:text=According%20to%20the%20United%20States,7%25%20of%20global%20mineral%20reserves.
[67] "Proven and Probable Reserves," *Cameco,* last updated December 31, 2023, https://www.cameco.com/invest/overview/reserves-resources/proven-probable#:~:text=About%20mineral%20reserves&text=proven%20reserves%3A%20the%20economically%20mineable,a%20high%20degree%20of%20confidence.
[68] "China-U.S. Futures: Pathways to Peaceful Coexistence" (panel discussion moderated by Ker Gibbs), *International House at UC Berkeley,* accessed May 2024, https://ihouse.berkeley.edu/china-us-futures-pathways-peaceful-coexistence.
[69] "2015 Minerals Yearbook: Iran [Advance Release]," *U.S. Geological Survey,* September 2018, https://d9-wret.s3.us-west-2.amazonaws.com/assets/palladium/production/mineral-pubs/country/2015/myb3-2015-ir.pdf.

As a non-Western group of countries, SCO potentially represents a potent coalition of exporters and importers of commodities centered around using the renminbi to finance the entire commodities lifecycle from production to trade to consumption. Similarly, the expansion of BRICS to oil-rich nations bolsters the group's collective economic power and influence on the clean energy transition despite introducing greater internal complexity among its members, such as regional rivalries in the Middle East, China's rivalry with India as well as rising populism and its subsequent political unpredictability in Latin America. SCO and BRICS now share overlapping members with similar incentives for using local currencies in international trade settlement and investment. This configuration facilitates formal and informal policy efforts to implement incremental de-dollarization initiatives in energy and commodities markets, with the potential to scale up, making the two major non-Western groups attractive platforms for China to create an alternative financial system as the world moves beyond hydrocarbon.

IV. China's Anti-Sanctions Regulatory Framework

Besides developing a renminbi-based financial system to reduce its vulnerabilities to Western financial sanctions, the Chinese government has also developed anti-foreign sanctions regulatory framework to provide domestic legal basis to weaponize access to Chinese market. From Norwegian salmon, Philippine bananas, to Australian lamb, the Chinese government has often resorted to importing restrictions to punish foreign governments for their violation of what China deems as its core national interests. Escalating tensions with the United States since 2018 have led China to establish domestic legal foundations to restrict market access should foreign entities choose to comply with foreign sanctions and hurt China's interests. In October 2018, China enacted its International Criminal Judicial Assistance Law (ICJAL) as a blocking statute to prohibit entities located in China from unilaterally cooperating with foreign civil and criminal investigations without the consent of the Chinese government.[70] Specifically, Article 4 of the ICJAL states that "the international criminal judicial assistance shall not damage the sovereignty, security and social public interests of the People's Republic of China, and shall not violate the basic principles of the laws of the People's Republic of China." This provides a broad spectrum of legal basis for Chinese entities not complying with foreign investigations.

The Chinese government further weaponized access to the Chinese market by establishing the Provisions of the Unreliable Entity List, or UEL Provisions, an export controls framework issued by the Ministry of Commerce of China (MOFCOM) on September 19, 2020.[71] MOFCOM published the UEL Provisions the next day after the U.S. Department of Commerce implemented an Executive Order to restrict the use of WeChat and TikTok, two Chinese-owned apps, in the United States. MOFCOM first announced the establishment of such an entity list on May 31, 2019, ten days following the U.S. Department of Commerce added Huawei to its entity list. The timing of these events suggests that China's entity list is designed in response to foreign actions.

In January 2021, MOFCOM issued another sanction blocking statute, Rules on Counteracting Unjustified Extra-Territorial Application of Foreign Legislation and Other Measures, or the Extra-territorial Rules, as a countermeasure to the U.S. long-arm jurisdictions.[72] The Rules empower aggrieved parties to report damages to MOFCOM and sue for compensation in Chinese courts. The Rules also grant Chinese authorities certain powers to block the extraterritorial application of foreign laws if deemed as unjustifiably prohibiting or restricting Chinese individuals or entities from engaging in "normal economic, trade, and related activities" with foreign entities, especially secondary

[70] "International Criminal Judicial Assistance Law of the People's Republic of China" (中华人民共和国国际刑事司法协助法), *The National People's Congress of the People's Republic of China,* October 26, 2018, http://www.npc.gov.cn/zgrdw/npc/xinwen/2018-10/26/content_2064576.htm.

[71] "Ministry of Commerce Order No. 4 of 2020 on the Unreliable Entity List" (商务部令 2020 年第 4 号 不可靠实体清单规定), *Ministry of Commerce of the People's Republic of China,* September 19, 2020, http://www.mofcom.gov.cn/article/b/fwzl/202009/20200903002593.shtml.

[72] "MOFCOM Order No. 1 of 2021 on Rules on Counteracting Unjustified Extra-Territorial Application of Foreign Legislation and Other Measures," *Ministry of Commerce of the People's Republic of China,* January 9, 2021, http://english.mofcom.gov.cn/article/policyrelease/announcement/202101/20210103029708.shtml.

sanctions and export controls. According to the Rules, the Working Mechanism, which is comprised of MOFCOM, the National Development and Reform Commission, and other relevant Chinese authorities, is in charge of determining whether the extraterritorial application of a reported foreign law or measure is unjustified.

Within five months of the issuance of the Rules, the Standing Committee of the National People's Congress enacted China's Anti-Foreign Sanctions Law.[73] This Law leans heavily towards countermeasures rather than blocking, as evidenced by the fact that eleven out of the twelve articles in the Law are dedicated to specifying the content, standard, and legal responsibilities of countermeasures. The Law introduces a new sanctions list known as the Countermeasure List. The Ministry of Foreign Affairs and other relevant ministries have the discretion to identify foreign entities to put on this list. This legislation came in response to the United States, E.U., and U.K. sanctioning more Chinese individuals and entities over concerns of human rights violations in Xinjian or ties to China's military and surveillance activities.

Altogether, China's anti-sanctions regulatory framework is designed to deter and penalize cooperation with foreign actions perceived to be detrimental to Chinese business and national interests. As the enforcement of these statutes continues to flesh out, the Chinese state can force foreign companies to choose either the Chinese market or Western markets.

V. China's Retaliatory Capacity Through Export Controls and Controls of Overseas Ports

Strengthening the international role of the renminbi, developing an alternative financial system, and building an anti-sanctions regulatory framework are defensive in nature. If China were forced to decouple from the dollar-based global system, such defensive measures could provide some relief for China but cannot fully immunize China from collective Western sanctions. However, in the worst-case scenario of a financial war, Beijing would not confine itself to financial defense. It would likely retaliate against Western sanctions with offensive measures. Beijing could respond with two detrimental retaliatory measures: China could impose export controls on some controlled items, including but not limited to rare earth minerals; it could also deny foreign access to critical infrastructure, especially ports, around the world controlled by China.

In October 2020, China promulgated its Export Control Law.[74] The ECL is the first Chinese law that establishes a comprehensive and integrated export control regulatory regime to protect China's national security and interests. It has a provision on "reciprocal measures," which states that China may take reciprocal measures against any country or region whose abuse of export control measures endangers China's national security and interests as assessed by Chinese government agencies. In December 2021, the State Council published a white paper on China's Export Control that states the government strives to build an export control system commensurate with China's international status and in line with the state's national security and interests.[75] The ECL and the follow-up white paper suggest that Chinese policymakers have formed a more mature view of how to strategically leverage China's critical status in global supply chains to protect China's national interests and retaliate against foreign restraints when necessary.

China's export control framework may give the Chinese government a new opening to restrict rare earth exports under a national security exception to WTO rules against restraints on free trade. Deng Xiaoping said in 1992 that

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[73] "Anti-Foreign Sanctions Law of the People's Republic of China" (中华人民共和国反外国制裁法),*The National People's Congress of the People's Republic of China,* June 10, 2021, http://www.npc.gov.cn/npc/c2/c30834/202106/t20210610_311892.html.
[74] "The Export Control Law Passed the Third Review and Will be Implemented on December 1 This Year" (出口管制法三审通过 今年 12 月 1 日起施行), *The National People's Congress of the People's Republic of China,* October 17, 2020, http://www.npc.gov.cn/npc/c2/c30834/202010/t20201017_308292.html.
[75] "China's Export Controls" (中国的出口管制), *Information Office of the State Council of the People's Republic of China,* December 29, 2021, https://www.gov.cn/zhengce/2021-12/29/content_5665104.htm.

"the Middle East has oil; China has rare earths." China produces 60 percent of all rare earth elements used as components in high-tech devices and controls about 80 percent of the global supply. China has also maintained a near-monopoly over the complex refining process, controlling about four-fifths of global rare earth refining capacity. Beginning in 2007, China has set rare earths production limits, export quotas, and cut down the number of export enterprises to meet diverse policy objectives ranging from reducing pollution and increasing fiscal revenue to the development of processing sectors. Beijing believed these restrictions were justified under the WTO's General Agreement on Tariffs and Trade Article XX on General Exceptions for the conservation of exhaustible natural resources and the protection of human health. However, the WTO ruled in July 2011 that China violated international trade rules by restricting the exportation of raw materials, refuting Beijing's claim that these restrictions were based on environmental grounds. China rejected the WTO ruling, arguing that it was unfair and subjective, exposing the insufficient representation of developing countries in the WTO and its inability to understand developing nations' problems. The ECL could provide a legal foundation to empower the Chinese government to ban exports of rare earths and refining technology to countries or corporations it views as a threat to China's national security.
If isolated from the US-led global financial system, China could possibly retaliate by restricting exports of rare earths that are crucial for the manufacture of high-tech consumer electronics and sophisticated American weaponries, including F-35 fighter jets, to the United States and U.S. allies. China supplied 80 percent of U.S. rare earth imports between 2014 and 2017.[76] Beijing reportedly has been exploring such an option in 2019, following deteriorating Sino-US relations and an emerging technology war between the two countries. Imposing export control over certain rare earths has been a frequently used tool in China's economic statecraft repository. The reported threat of retaliation against the United States mirrors China's ban of rare earths exports to Japan in 2010 following the detention of a Chinese fishing boat capital who rammed Japanese patrol boats in disputed waters near the Senkaku/Diaoyu Island.

Besides its dominance over rare earths, China's critical position in global supply chains also rests on its emergence as a leading commercial maritime power. Domestically, China has more shipping ports than any other country in the world. Globally, China invested in 101 port projects by 2019, including 37 in Asia, 33 in Africa, 11 in Europe, 9 in South America, 6 in North America, and 5 in Oceania.[77] Three Chinese port operators, COSCO Shipping Ports, China Merchants Port Holdings, and Qingdao Port International Development, had already held stakes in 16 European ports as of 2018.[78] Chinese port operators controlled 10 percent of European shipping throughput in 2021.[79] COSCO, a leading ports operator in the world that carries one-tenth of global seaborne trade with its one-eighteenth of the entirety of global shipping capacity, has stakes in some of the world's largest ports, including a 67 percent stake in the Piraeus Port Authority. It owns 100 percent of Peiraeus Terminal, 85.5 percent of Zeebrugge Terminal, 51 percent of Valencia Terminal, and minority shares in several other European ports. To date, central-government-owned port operators, such as COSCO Shipping Port and CMPort, and central-government-owned constructors and builders, such as China Communications Construction Group and its subsidiaries, remain the primary participants in overseas port projects investment and construction, sometimes with financial participation from Chinese sovereign funds such as China Investment Corporation and policy banks such as Export-Import Bank of China and China Development Bank.

Besides investing in commercial ports, China has also pursued a strategic strongpoint approach to developing dual-use port facilities, which has been a cause for concern in the West. Chinese naval deployments have followed Chinese

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76 "China's Rare Earth Supplies Could Be Vital Bargaining Chip in U.S. Trade War," *Reuters,* May 30, 2019, https://www.reuters.com/article/idUSKCN1SS2WL/#:~:text=China%20hosts%20most%20of%20the,the%20U.S.%20Geological%20Survey%20showed.
77 Zongyuan Zoe Liu, "Tracking China's Control of Overseas Ports," *Council on Foreign Relations,* November 6, 2023, https://www.cfr.org/tracker/china-overseas-ports?utm_source=tw&utm_medium=social_owned.
78 Joanna Kakissis, "Chinese Firms Now Hold Stakes in Over a Dozen European Ports," *National Public Radio,* October 9, 2018, https://www.npr.org/2018/10/09/642587456/chinese-firms-now-hold-stakes-in-over-a-dozen-european-ports.
79 Jacob Mardell, "COSCO Takes Stake in Hamburg Port Terminal," *MERICS,* September 30, 2021, https://merics.org/en/tracker/cosco-takes-stake-hamburg-port-terminal.

investments in the ports of Djibouti, Sri Lanka, and Pakistan. While there is no public record of China's plan to turn European ports into Beijing's military bases, a Chinese navy fleet's visit to Greece's Piraeus port in 2017 did raise the eyebrows of some European policymakers. Chinese port acquisitions grant the Chinese government greater control over global shipping and commercial flows, which may pose risks to the ability of foreign governments to secure supply chains.

VI. Assess China's Existing Ability to Defend Against Financial Sanctions and Issues for Congress to Consider

Despite China's intention to hedge against sanction risk, plenty of evidence suggests that China does not have the capability to fully neutralize Western sanctions. The renminbi is far from being a global currency, let alone posing a credible threat to the dollar's hegemonic power. China's proprietary financial infrastructure has limited international coverage compared with SWIFT. Additionally, China's CIPS still relies on interoperability and integration with SWIFT if it wants broader participation of leading global financial institutions. China's anti-sanctions regulatory regime could force Western companies to choose either China or the West. However, it lacks concrete enforcement mechanisms. Finally, the PLA does not have combat experience commensurate with China's prominent commercial maritime power.

While China has been attempting to mobilize a de-dollarization coalition to defend against the dollar-based system weaponized against China through non-Western partnerships such as SCO and BRICS, such a coalition at present remains a vision and cannot provide China with substantive material support to mitigate Western financial sanctions, especially secondary sanctions. The reason is that commodity-exporting countries from which China imports resources to fuel its economy depend on the dollar-based system to price and trade their commodity exports. Their banks remain reliant on the SWIFT-CHIPS system for international payment settlements. However, the basic infrastructure for mitigating sanctions has come into existence. If China could expand the renminbi-based financial infrastructure to cover its major trading partners and convince them to use the renminbi for cross-border settlements, its ability to shelter the Chinese economy from Western financial sanctions would be much higher.

Chinese policymakers have witnessed that Europe's dependence on Russian energy has not prevented the European Union from sanctioning Russia for Putin's invasion of Ukraine. Therefore, from Beijing's vantage point, the West's dependence on China may not stop the United States and its allies from slapping stringent sanctions on the Communist Party of China and Chinese entities in reaction to dramatic events, such as a militarized conflict over Taiwan or in the South China Sea. Beijing views that the risk of Western sanctions against China may increase if the West reduces its economic dependence on China.

Members of the U.S. Congress need to consider that if China and the West were to engage in economic warfare within the next decade, the cost to the entire global markets would be enormous. The United States would not be exempted from the losses. According to a U.S. Chamber of Commerce-Rhodium Group report, if half of the U.S. investment in China were abandoned, it would cost American companies $25 billion annually in lost profits, on top of a $500 billion hit to the U.S. gross domestic product.[80]

Members of the U.S. Congress also need to consider that supply chain diversification cannot be achieved overnight, and hastened policies to bring manufacturing back to America cannot achieve its desired goals but raise inflationary pressure at home while increasing protectionist concerns among U.S. allies and partners. It takes time and effort for people to move houses; supply chain diversification is much more complicated than moving houses. If the United States and China were pulled into a financial war before Western companies could be sufficiently independent of

[80] Daniel H. Rosen and Lauren Gloudeman, "Understanding U.S.-China Decoupling: Macro Trends and Industry Impacts," *Rhodium Group,* February 17, 2021, https://rhg.com/research/us-china-decoupling/.

Chinese suppliers and markets, the costs to U.S. companies and American consumers would be enormous, disrupt American people's ordinary lives, and end globalization. While it is hard to determine whose loss would be greater, a forced decoupling of China from the existing global system would put a definitive end to globalization.

I encourage the U.S.-China Commission and members of the U.S. Congress to consider the following policy recommendations aiming at strengthening U.S. financial leadership and keeping China embedded in the U.S.-led system so that the U.S. government can maintain the credibility of its financial deterrence in the long term.

First, Congress should develop mechanisms to offset the potential negative impact of the Rebuilding Economic Prosperity and Opportunity for Ukrainians Act (REPO Act), passed by Congress and signed into law by President Biden, on the role of the U.S. dollar. The REPO Act specified conditions in which the President may confiscate Russian official assets subject to the jurisdiction of the United States to provide aid for Ukraine. While seizing Russian assets for Ukraine aid may be seen as an optimal solution given the current geopolitical circumstances, the cost of unilateral or coordinated confiscation of Russian official assets by the U.S. government with its allies to support Ukraine is likely to lead to diminished trust in the U.S. dollar-based system as well as decreased U.S. leverage over foreign rivals in the long run. To mitigate the negative consequences, Congress should consider legislative measures to strengthen the use of the U.S. dollar in international trade and investment. To this end, Congress can consider empowering the U.S. International Development Finance Cooperation (DFC) in its ability to work with a broader range of partners and countries rather than limiting it to a restricted set of low- and lower-middle-income countries. By expanding the countries and regions where DFC can work, the United States can offer a credible alternative to China's state-led development finance that aims to advance a renminbi-based financial system.

Second, while currently there is no evidence to suggest that China can credibly augment the rudimentary renminbi-based financial infrastructure to be a full-fledged alternative to the dollar-based system, China and its partners that are concerned about Western sanctions will continue deepening their de-dollarization cooperation via new technological means and platforms, such as block-chain based central bank digital currencies. Additionally, the availability of digital assets such as cryptocurrencies and their exchangeability with other assets offer new mechanisms to bypass financial sanctions. Congress should consider legislation to enhance scrutiny of crypto asset transactions, especially stablecoins, to prevent them from being used by foreign entities and individuals to circumvent sanctions. The Financial Innovation and Technology for the 21st Century Act passed by the U.S. House of Representatives made good progress in establishing regulatory oversight of the digital asset markets in the United States.[81] However, as it stands now, the regulation does not include clear rules on monitoring and restricting the illegal use of digital assets and cryptocurrencies for sanction evasion. Updating U.S. law to combat the illicit use of digital assets is critical for U.S. national security and for maintaining the credibility of U.S. government financial statecraft in the long term.

Third, Congress needs to consider strengthening U.S. critical minerals supply chain security and resilience to support the continued U.S. leadership in a decarbonized global economic system. China currently dominates the refining and processing of key mineral resources critical for the clean energy transition. China has in the past weaponized its dominant position in rare earths minerals and rare earth processing technology to retaliate against territorial disputes and export controls, which makes U.S. dependence on China for mineral resources a national security concern. The United States depends on China for over half of its supply of 25 mineral commodities,[82] making the U.S. economy and industries vulnerable to supply disruptions stemming from China, especially in times of geopolitical tension. As the global economy continues to move beyond hydrocarbon, China's dominance in critical minerals supply chains combined with the Chinese government's attempts to increase the renminbi's pricing power in mineral resources markets could dilute the dollar's centrality in a decarbonized global economy. So far, the United States has taken

[81] "H.R.4763 - 118th Congress (2023-2024): Financial Innovation and Technology for the 21st Century Act," Congress.gov, May 22, 2024, https://www.congress.gov/bill/118th-congress/house-bill/4763.
[82] Zongyuan Zoe Liu, "Critical Minerals and the New Cold War," *The Diplomat,* October 1, 2023, https://thediplomat.com/2023/09/critical-minerals-and-the-new-cold-war/.

substantive measures to secure critical mineral supply chains by forging minilateral partnerships in the Indo-Pacific region through the Quadrilateral Security Dialogue, commonly known as the Quad, comprising the United States, Australia, India, and Japan. The Indo-Pacific Economic Framework for Prosperity, as outlined by the White House,[83] also put on its agenda the assurance of critical minerals access as a means to counter China's dominance. In addition, the Biden administration has launched a broader multilateral Minerals Security Partnership (MSP) with critical partners to "friend-shore" critical mineral supply chains. These initiatives are necessary but insufficient to boost domestic supply and secure diversified access to overseas supply in a timely manner. Congress needs to consider streamlining the permitting and licensing process and setting timelines to ensure the timely development of critical mineral projects at home. Congress also needs to consider expanding funding for research and development on alternatives and mineral resource recycling technologies.

Last, Congress may wish to consider China-related legislative measures across the whole spectrum of geoeconomic competition with China to allow fair competition, avoid costly conflict, and prevent unintended escalation. A motivating factor for China to develop an alternative system to hedge against Western sanctions originates from Chinese leaders' perceived insecurity and vulnerability in the U.S.-led global system. It is in the interest of U.S. national security and the American people that Congress takes punitive measures against the Chinese government's unfair practices. However, an overreliance on "sticks" to punish China without offering any "carrots" to incentivize China to behave as a responsible stakeholder in the U.S.-led global system would likely only encourage China to pursue an alternative international trade and finance system further. Congress may wish to supplement its existing laws on China with issue-specific legislative measures that encourage U.S.-China cooperation in areas that do not pose national security risks to the United States while also creating jobs and bringing tangible socioeconomic benefits to communities across the United States. Three areas worth Congress's consideration include environment and climate change cooperation, food security cooperation, and disaster relief cooperation. Neither the United States nor China can effectively deal with the worldwide challenges of climate change, food security, and disaster relief. The U.S. government cannot stop the Chinese government from developing an alternative trade and financial system to defend against Western sanction risk. The U.S. government also cannot make macroeconomic policy decisions for China. However, the U.S. government and members of Congress can take measures to encourage China to stay embedded in the U.S.-led global financial system rather than incentivizing China and its partners to divert trade settlements and financial flows outside of the dollar-based system.

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[83] "Statement on Indo-Pacific Economic Framework for Prosperity," *The White House,* May 23, 2022, https://www.whitehouse.gov/briefing-room/statements-releases/2022/05/23/statement-on-indo-pacific-economic-framework-for-prosperity/.