



SHAKY CHINA

Five scenarios for Xi Jinping's third term

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Five scenarios for Xi Jinping's third term

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Executive Summary

In March 2023, Xi Jinping sealed a third term in power heading both the Chinese Communist Party (CCP) and the Chinese state. **In “Xi III”, China is entering a phase of increasing uncertainty.** Three trends that shaped China in Xi’s first and second term will remain particularly relevant: slower growth, external pressure and increased centralization of power. Whatever path China takes will have serious implications for its own people and the rest of the world.

This study lays out **five scenarios for China’s path over the coming years in order to help formulate strategic responses.** They were developed at Mercator Institute for China Studies (MERICS) with methodological guidance from the Fraunhofer Institute for Systems and Innovation Research (ISI) and draw on 15 political, social, economic and technological factors.

The **baseline scenario is a “Shaky China”, an unstable ‘status quo’ scenario**, in which China’s economy, politics and engagement with the world follow the trends seen at the outset of Xi’s third term in office. Significant changes in some of the underlying factors could create pathways to cross over into one of four more extreme scenarios:

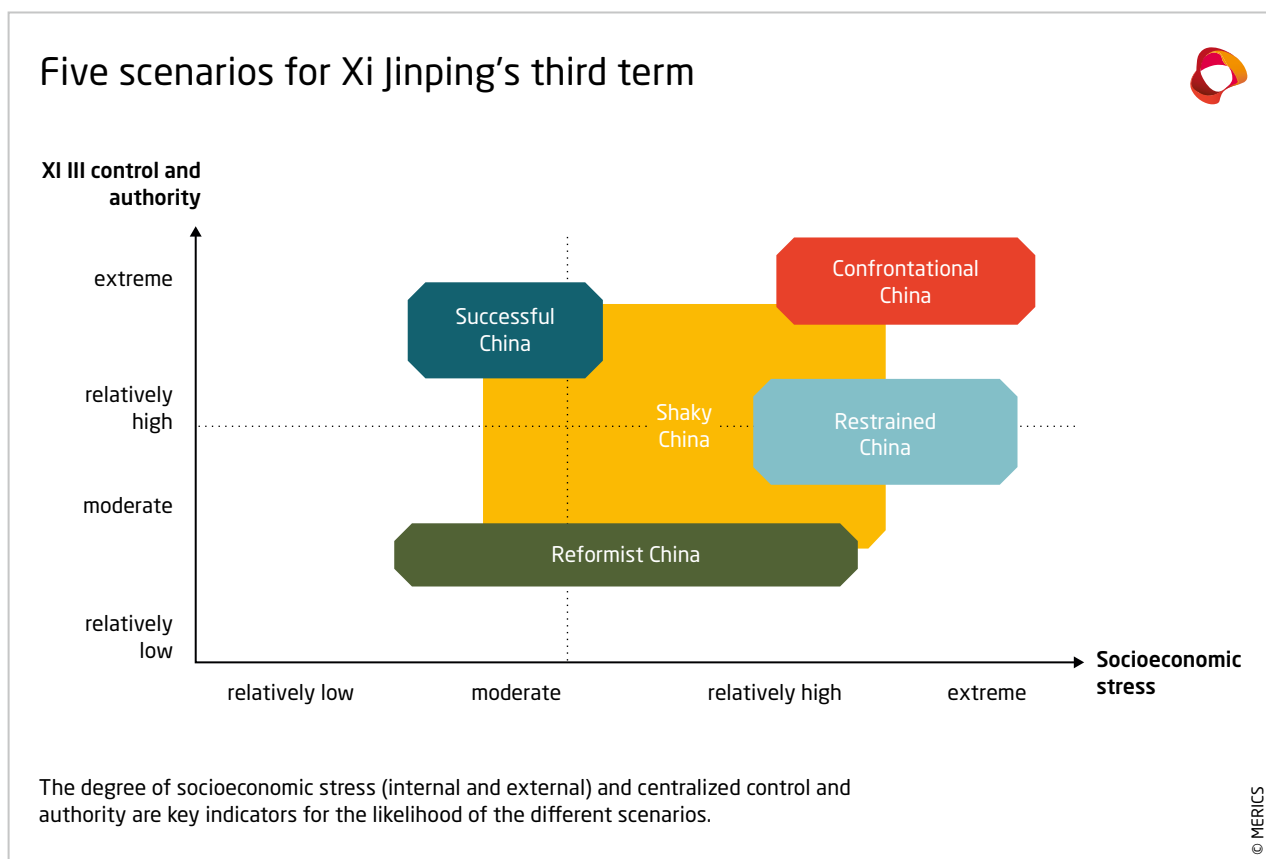
- **Confrontational China:** In this scenario, tensions over Taiwan escalate to a point where the grey-zone conflict is heightened enough to make open military conflict feel increasingly likely. This generates extreme bifurcation and significant de-coupling between China and the West.
- **Successful China:** In this scenario, China is perceived to achieve key goals in Xi’s agenda: all-encompassing party-state control, a shift to sustainable green growth, technological independence and global influence rivalling the US. Preconditions for this scenario would be a significant crisis of the West, tangible Chinese success stories and a successful power play with the Global South.
- **Restrained China:** In this scenario, China’s internal weaknesses, plus coalition-building by the United States and likeminded countries, hamper Beijing’s efforts to diversify the economy, maintain growth, achieve technological independence, build external coalitions or pursue an effective global power play.
- **Reformist China:** In this scenario, China’s internal crises result in a political course correction. The confrontation between China and the West is reduced amid expectations of a return to “reform and opening up”, if under new circumstances.

All scenarios are possible, but this does not mean that a scenario will be realized in full. Trajectories and perceptions of them matter. **The degree of socioeconomic stress (internal and external) and centralized control and authority are key indicators of the likelihood of different scenarios.** The baseline scenario “Shaky China” covers the broadest range of different levels of stress and centralization. Should socioeconomic stress rise even further, both a “Confrontational China” or a “Restrained China” become more likely. A “Successful China” becomes more realistic if the CCP were perceived to be extremely successful at mitigating socioeconomic stress. A “Reformist China” would imply significant decentralization of power and currently seems almost impossible.

European policy makers and private businesses alike need to understand the realities of a more “Shaky China” and the possibility of a shift into more extreme scenarios. The risk exposure of individual actors and opportunities associated with different scenarios vary greatly. Whatever their situation, three steps are needed:

- **Analyzing opportunities and risks:** In Europe, policy makers and private businesses need to find a new balance between China-related risks and opportunities. This study provides a broad overview from the perspective of European policy makers and corporates.
- **Planning preparation and mitigation measures:** Policy makers and private enterprises need a full-fledged portfolio of mitigation measures. In the EU, these are currently being discussed and developed around the concept of “de-risking”. To build robust strategies, actors need to consider various pathways rather than preparing for a single scenario.
- **Tracking triggers:** Decision makers need to closely monitor China’s development, in particular by tracking the potential triggers that could bring a change in China’s trajectory. This study offers an overview of triggers that could turn out to be significant and deserve the attention of decision makers.

Exhibit 1



Shaky China

Five scenarios for Xi Jinping's third term

In March 2023, Xi Jinping sealed a third term in power heading both the Chinese Communist Party (CCP) and the Chinese state. His victory overturned more than 30 years of collective leadership and was enabled by constitutional amendments. Xi's ambitious political agenda and handpicked leadership team will shape China's path at a decisive juncture; the next five years could emerge as a tipping point in China's rise or its stagnation. To manage this phase, Xi has established a system of party-state steering that restores centralized power and control and is continuing to centralize political and economic life still further. Tight control is Xi's preferred way to grapple with China's unprecedented socio-economic challenges. It is far from clear if this path will be successful, but if it is Xi may well seek to extend his third five-year term into a fourth one.

The one forecast that can be made with confidence is that in "Xi III", China is entering a phase of increasing uncertainty. It is one of the few matters on China's leadership and mainstream foreign China analysts agree. Whatever path China takes will have serious implications for its own people and the rest of the world.

This study lays out five scenarios for China's path over the next five years in order to help formulate strategic responses. As with all scenario exercises, these are not predictions of the future. They are a framework for mapping and tracking key dynamics that will shape China's trajectory and a tool for policy makers and businesses to stress test strategies and action plans against different pathways.

THREE TRENDS SHAPING CHINA'S NEXT FIVE YEARS: SLOWER GROWTH, EXTERNAL PRESSURE AND INCREASED CENTRALIZATION OF POWER.

No one doubts that Xi has fundamentally changed China in his first ten years in power, regardless of how they view him. Xi has already put in motion dynamics that will continue to deliver significant change in the years ahead. China is already very different from when Xi took over in 2012/2013. In the immediate post-Mao era, the CCP established a peaceful transition of power based on two-term limits and age limits. Under this system, power passed from Deng Xiaoping to Jiang Zemin to Hu Jintao to Xi. He broke with party tradition when he clinched a third term as the party's General Secretary at the 20th Party Congress in October 2022, though the move was universally expected as Xi signaled his intentions in 2018 by abolishing the two-term limit for the party post of PRC Chairman - a title usually held by the state president. In 2022, Xi installed a new leadership team of (overwhelmingly male) cadres of proven personal loyalty and effectiveness at implementing his political agenda. The annual meeting of China's largely ceremonial parliament in March 2023 approved Xi's third term as president, clearing the way for his ambitious "New Era" agenda. As the "New Era" includes a fundamental reorganization of government institutions to further tighten the party's control over all state organs, it is likely that China's governance will look very different by the 21st Party congress in 2027.

Three trends that shaped China in Xi's first and second term (Xi I and Xi II) will also be particularly relevant for China's development in Xi III: Slower growth, external pressure and increased centralization of power.

Slower growth

China's economic growth, the engine of its tremendous progress since the 1980s, is facing a long-expected slowdown as the easy gains of catch-up development fade. Growth from infrastructure construction and low-tech exports has run its course. But China has not yet made the shift to a more sustainable growth path built on better paid jobs, increased technological capabilities and less environmental damage. The challenges of this economic transition were anticipated long before Xi came to power. During his first term (Xi I), the effects became fully visible, but were relatively well controlled, as growth rates descended from the double-digit-era of the early 2000s to around 6 percent annually. In Xi's second term (Xi II), growth volatility started to pose serious tests for stability. Although triggered by the Covid-19 crisis, they stemmed from many underlying factors – low productivity and high dependence on exports or government investment. In Xi's third term, China's socioeconomic challenges will carry the risk of significant crises, even by the party's own assessments, which cite negative demographic trends, financial stress and external pressure.

External pressure

The changing international environment is the second main trend seriously impacting China's trajectory, in particular the rivalry between China and the United States. In 2013, Xi inherited a Sino-US relationship that, though stressed and competitive, was fairly stable. Relations deteriorated during Xi's first term and longstanding conflicts moved to the forefront, beginning with tensions over US president Barack Obama's "pivot to Asia" and the on-and-off volatile hostility during President Donald Trump's tenure. Under the Biden presidency, the relationship has moved towards the more systemic competition and sustained confrontation. As Xi's third term gets underway, both the United States and China are locking in their security, economic and technology policies with the determination to prevail in a long, fierce rivalry to be the world's leading power.

The combination of slowing growth and a shifting, more volatile international environment is producing considerable socioeconomic stress.

Centralization of power

Xi has centralized power in a way not seen since – and in some ways exceeding – the era of Mao Zedong. The party frames its push towards centralization and control as a necessary and effective policy response to rising socioeconomic challenges. Strengthening the CCP with himself at the core, has also been a priority of Xi's and one that he has fulfilled successfully. In effect, he put in place a system in which he wields so much authority that even China's policy mistakes during the Covid 19 crisis were no serious challenge to his position, despite sparking rare public demonstrations of anger.

Although Xi and the CCP leadership have achieved their top priorities, even they concede that China has moved from a stressed, but rather stable country to one that is more unstable and less predictable in the ten years since 2013. The fact that "stability and control" are now key concepts of Xi's agenda underscores what shaky ground the system is standing on. In an unstable environment, pathways can easily lead into other, more extreme scenarios.

FIVE SCENARIOS FOR A SHAKY CHINA

Whether this less stable and less predictable China becomes the “new normal”, or whether China experiences more radical shifts, will depend on developments in different arenas. This study therefore draws on 15 factors which are key for China’s future path. These include

Political and social factors

- China-US relations
- China’s role in blocs and coalitions
- China’s hard power projection
- China's political system
- China's stability and social policy
- Cross-strait relations
- Energy system and supply
- Food and water systems and supply

Economic and technological factors

- China’s economic governance model
- China’s domestic economic sustainability
- China in the global economy
- China’s macro growth path
- China’s technological independence
- China's innovation capacity
- China as a digital actor

For each factor, sub-scenarios were developed and tested for mutual influence and consistency (see methodology chapter). Since many factors influence one another, major developments in some areas could generate changes in other dimensions and potentially shift China’s trajectory into a totally different scenario.

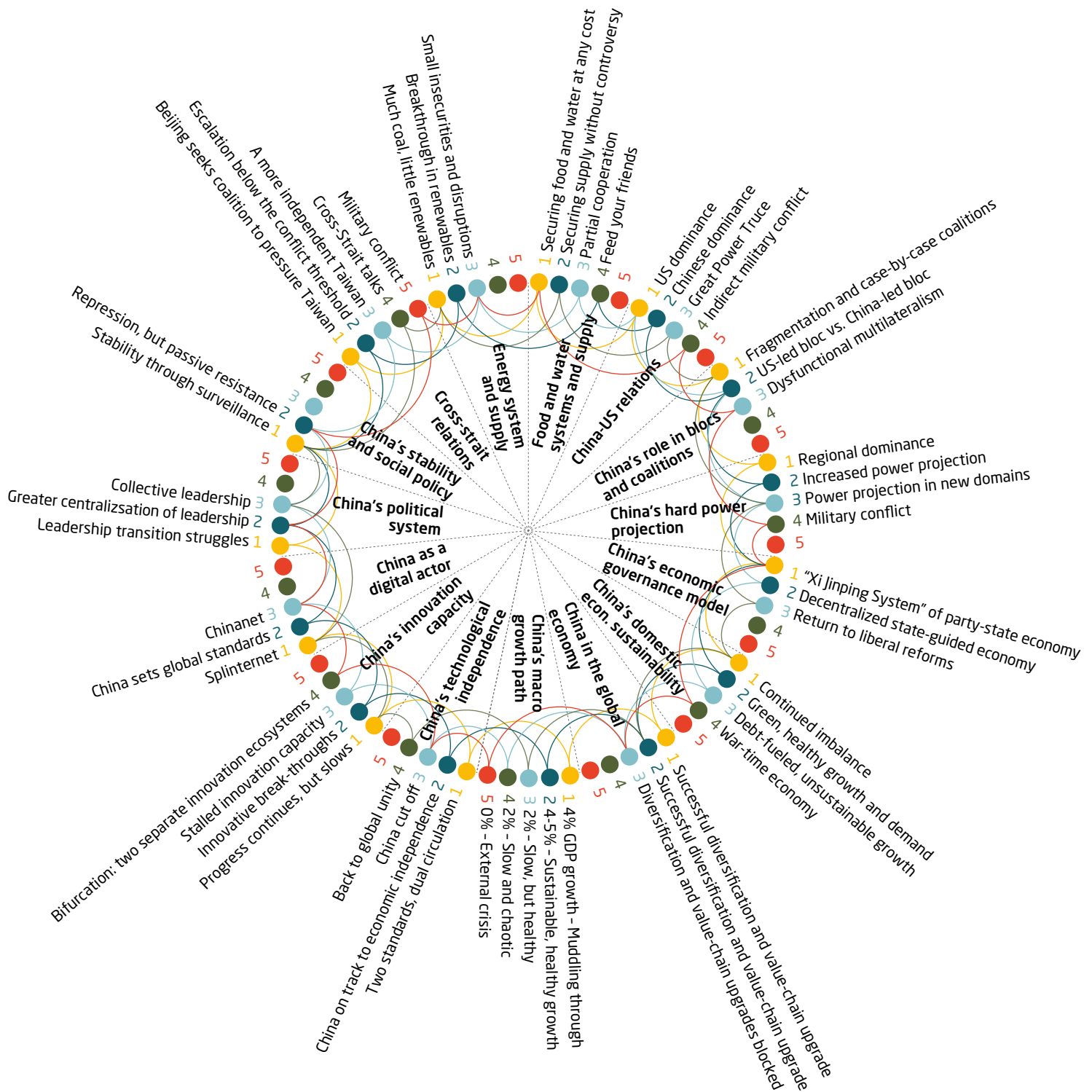
Looking at potential developments within the different factors has led us to formulate five distinct scenarios.

Exhibit 2

Scenario overview

The scenarios draw on 15 factors. For each factor, 2-5 sub-scenarios were developed.

■ Shaky China ■ Successful China ■ Restrained China ■ Reformist China ■ Confrontational China

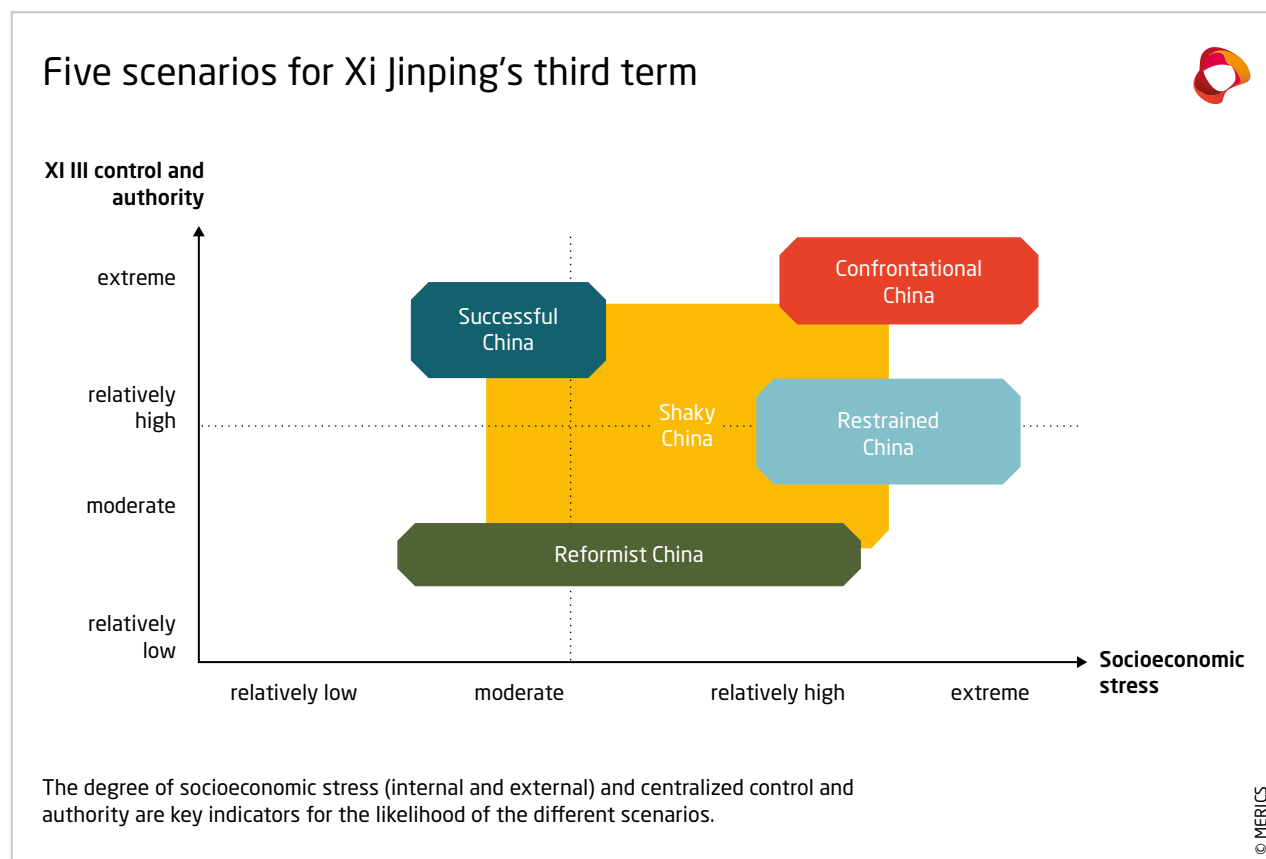


The baseline scenario is a **“Shaky China”**, in which China’s economy, politics and engagement with the world follow the trends seen at the outset of Xi’s third term in office. It is a ‘muddling through’ scenario in which China neither makes impressive progress nor faces existential crisis.

“Shaky China” is an unstable ‘status quo’ scenario. However, significant changes in some of the underlying factors could create pathways to cross over into one of four more extreme scenarios:

- **Confrontational China:** In this scenario, tensions over Taiwan escalate to a point where the grey-zone conflict is heightened enough to make open military conflict feel increasingly likely. This generates extreme bifurcation and significant de-coupling between China and the West.
- **Successful China:** In this scenario, China is perceived to achieve key goals in Xi’s agenda: all-encompassing party-state control, a shift to sustainable green growth, technological independence, and regime security and global influence rivalling the United States. China’s success is aided by the West’s huge homegrown problems.
- **Restrained China:** Here, China’s internal weaknesses, plus coalition-building by the United States and likeminded countries, hamper Beijing’s efforts to diversify the economy, maintain growth, achieve technological independence, build external coalitions or pursue an effective global power play.
- **Reformist China:** In this scenario, China’s internal crises result in a political course correction. The confrontation between China and the West is reduced amid expectations of a return to “reform and opening up”, if under new circumstances.

Exhibit 1



LIKELIHOOD OF SCENARIOS

All scenarios are possible. More extreme scenarios, which are theoretically possible (e.g. democratic reforms, a revolution, a collapse of the system) were considered during the process, but not included.

Possibility does not mean that a scenario will be realized in full. Trajectories and perceptions of them also matter. For instance, even if China does not become a global leader in future technologies, a breakthrough in a single technology could lead to a perception that China is on track to achieving this goal. A general reassessment of investment patterns might follow. Likewise, a continued perception of escalation also creates facts in the form of military spending or new alliances.

Graph 1 takes the degree of socioeconomic stress (internal and external) and centralized control and authority as the key indicators of the likelihood of different scenarios. The top right quadrant indicates current levels. “Shaky China” covers the broadest range of different levels of stress and centralization. Should socioeconomic stress rise even further, both a “Confrontational China” or a “Restrained China” become more likely, depending on external developments. A “Successful China” becomes more realistic if the CCP were to prove extremely successful at mitigating socioeconomic stress and achieving industrial policy breakthroughs (especially if boosted by an external crisis facing the West). A “Reformist China” would imply significant decentralization of power and currently seems almost impossible.

DEALING WITH A SHAKY CHINA

Xi has done away with many of our assumptions about China during the last ten years. Many strategies that governments and businesses developed in the 1990s and early 2000s were built on the conviction that China would continue to open up – perhaps not in a linear fashion, but along an overall trajectory of greater integration with the world economy and global political frameworks. At the beginning of Xi's third term, it is clear that this was wishful thinking. Many now see China not as the market of the future but as the cluster risk of the future.

European policy makers and private businesses alike need to understand the realities of a more “Shaky China” and the possibility of a shift into more extreme scenarios. The risk exposure of individual actors and opportunities associated with different scenarios, vary greatly. Whatever their situation, three steps are needed: an analysis of risks and opportunities; a reassessment of preparedness and mitigation measures; and tracking the potential triggers that could bring a change in China's trajectory.

ANALYZING OPPORTUNITIES AND RISKS

In Europe, policy makers and private businesses alike need to find a new balance between China-related risks and opportunities. Every scenario comes with its own specific opportunities and risks. Also, every individual actor – a national or a subnational government, a business or a university - has different risk exposure, or may perceive specific opportunities. Understanding these risks and opportunities and their strategic implications needs an individual analysis. What we provide here is a broad overview from the perspective of European policy makers and corporates.

Shaky China: As this is the “dynamic status quo” scenario, *European governments* face risks from volatile bilateral relations with China. Concerns include the politicization of economic relationships and supply chain dependencies. With the United States and China exerting substantial pressure, European states risk pursuing reactive policies rather than proactive policy making. This could lead them to overlook the opportunity that the “Shaky China” scenario presents; namely that there is still time, and room, for maneuvers to increase resilience, improve competitiveness, expand the mitigation toolbox and build alliances. *European companies* can pursue their China business strategies along recent trajectories (with signals about an increasingly constrained business environment already factored in). But they need to be aware of risks arising from more intense competition from Chinese companies, both in China’s market and third countries.

Confrontational China: This scenario entails the most detrimental disruption of the status quo. *European governments* and global institutions would face the need to react to global economic and supply chain crises; a global security crisis; and a global political crisis – all at the same time. Countries around the world would be under intense pressure to “choose sides” between the United States and China. For Europe, this would mean an obvious, though not pain-free, choice in favor of the transatlantic partnership. A very thin silver lining might lie in the opportunity to re-shore some business operations to Europe. *European companies* would be confronted with the massive effects of a global economic and financial crisis. Sanctions and political pressure could force corporates into sudden decoupling from China. The very few beneficiaries would be defense and security-related industries because defense expenditures would rise in European, and likeminded, countries.

Successful China: This scenario, in which China is perceived to be relatively more stable, resilient and future-oriented than the West, comes with the risk of a gradual erosion of the existing world order. *European governments* would be confronted with an increasingly assertive China that – together with Russia – moves to reshape global institutions according to its own interests. Economic dependencies on China would rise and would be increasingly weaponized. Also, China would exert increasing pressure on Western values and political systems. *European governments* that previously supported China’s course (at the cost of European and Western unity), stand to gain short-term benefits from privileged ties with Beijing, but would also lose their longer-term room to maneuver. *European companies* would need to operate in a world market where, increasingly, China is the technology leader that sets standards, dominates supply chains and aims to replace Western companies with Chinese ones. Businesses would face rising, often unfair competition in China and third markets, except for some short-term benefits and niche opportunities in industries where China urgently needs foreign technology.

Restrained China: This scenario is implicitly or even explicitly pursued by mainstream US China policy; it could create high political and economic costs on the European side of the Atlantic. *European governments* might find it harder to pursue an independent agenda vis-à-vis an emboldened United States. The risk of military escalation in the Pacific region may require increased defense spending. Partial decoupling from China would bring high costs and rising inflation. Nevertheless, a “Restrained China” scenario would also come with significant political opportunities: stability due to a strong alignment between likeminded countries; diminishing Chinese challenges to the global order and institutions; and more room for engagement with the Global South. *European companies* would suffer from their China business shrinking; partial (forced) decoupling; and the risk of secondary sanctions. The benefits include less economic and technological competition from China, a more level playing field in the West and better opportunities in the Global South.

Reformist China: Here, confrontation between China and the West would ease. *European governments* and companies would have far more opportunities than risks. These include more stable political relations with China; renewed opportunities for pursuing cooperation and a partnership agenda. Lower tensions between China and the United States could yield greater political leeway for Europe. The risks would lie in over-enthusiasm and renewed naïveté towards China's reforms and ambitions. A more pragmatic "Reformist China" is not necessarily a weaker or more Western oriented China. *European companies* would still experience strong competition from Chinese companies, but could compete in a more reliable, open business environment, which is more encouraging for long-term engagement.

PLANNING PREPARATION AND MITIGATION MEASURES

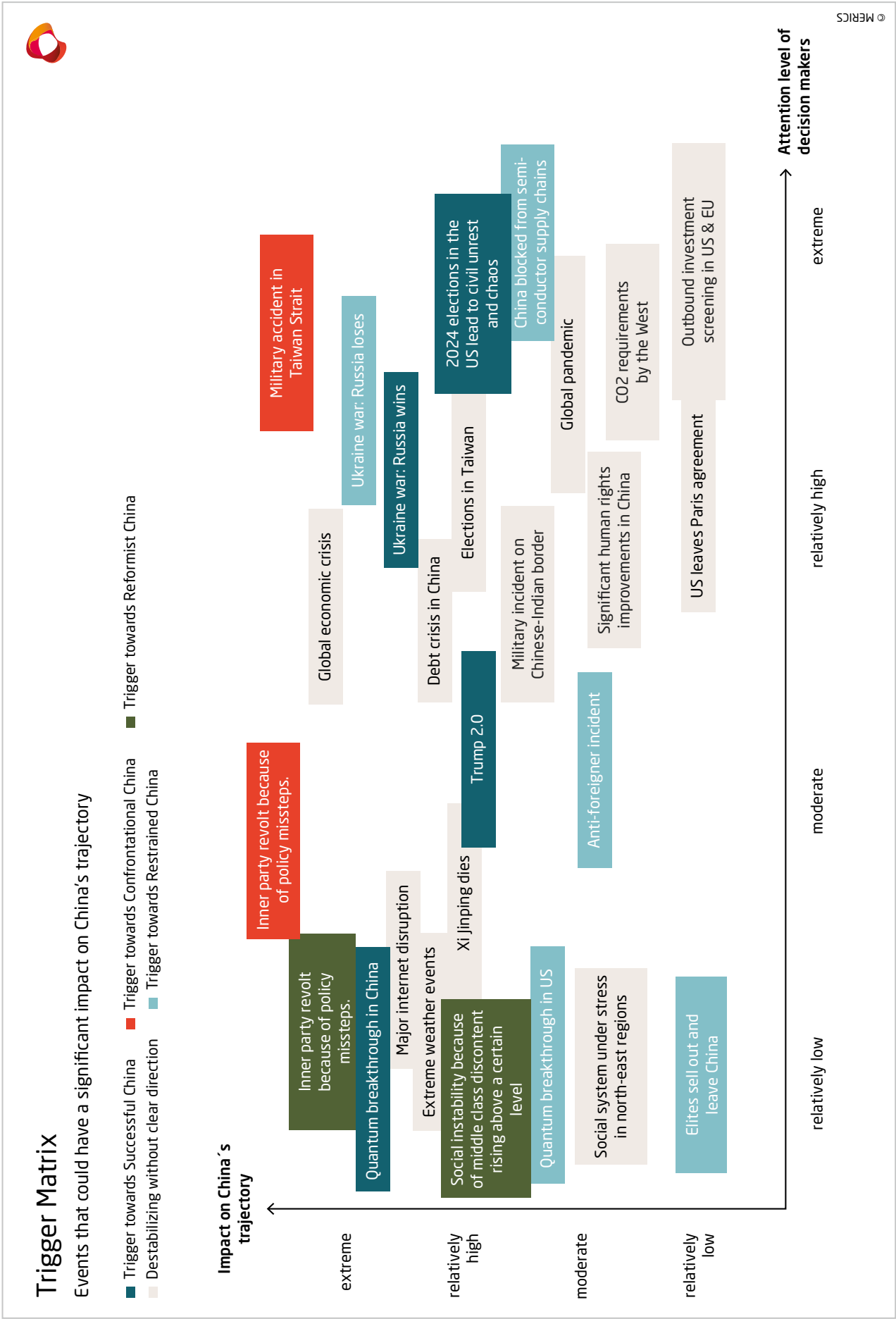
To prepare for the risks we have outlined, policy makers and private enterprises alike need a full-fledged portfolio of mitigation measures. In the EU, measures are currently being discussed and developed around the concept of "de-risking", endorsed and mainstreamed by EU Commission President Ursula von der Leyen in her March 2023 speech on China.

To build robust strategies for a "Shaky China" that could move into various more extreme scenarios, actors need to consider various pathways rather than preparing for a single scenario. Preparation and mitigation measures should therefore be discussed and implemented as a package, even if some are more relevant to some scenarios than others.

Preparation and mitigation measures for European governments include

- Analyzing and creating transparency about supply chain dependencies (in particular, for critical raw materials)
- Taking measures to bolster supply chain resilience (e.g. through diversification, re-shoring)
- Pursuing measures to radically improve Europe's economic and technological competitiveness
- Providing political support for diversification of markets for European businesses
- Making better use of existing defensive instruments in the European economic security toolbox (e.g. investment screening, economic coercion instrument)
- Developing new instruments to expand Europe's economic security toolbox (e.g. through outbound investment screening)
- Creating momentum for Global Gateway and other initiatives to engage more with the Global South
- Pursuing free trade and investment agreements with likeminded partners and the Global South
- Aligning better with the G7 and other likeminded partners
- Pursuing a proactive Asia Pacific strategy, including developing and supporting guard rails and deterrence measures against military escalation in the region
- Monitoring and protecting against illegitimate Chinese political influence operations
- Engaging with China politically on all levels
- Supporting social, educational and cultural exchanges in all forms that are not politically instrumentalized by China in unacceptable ways

Exhibit 3



Preparation and mitigation measures for European companies

- Analyzing risks and dependencies and creating transparency about them
- Pursuing a global business strategy that can “survive” forced decoupling from China
- Protecting and expanding competitiveness outside China
- Diversifying markets and supply chains (e.g. by investing in parallel supply chain and innovation structures outside China)
- “Enjoying the China success story while it lasts”: Pursuing business opportunities and profits in China, with a clear understanding of the risks involved and factoring in that the success-story can end anytime
- Preparing contingency scenarios for Chinese dominance of industry

TRACKING TRIGGERS

The third step in dealing with a “Shaky China” – besides analyzing risks and opportunities and implementing mitigation and preparation measures - lies in tracking change and potential shifts from the baseline scenario to other, more extreme scenarios. Many developments happen gradually, and major movements only become visible in hindsight. Nevertheless, a China that is under considerable socioeconomic stress and where major decisions are increasingly centralized, might be more likely to experience sudden developments. At the same time, internal or external shocks could push China further into new directions. The same can be said for major Chinese successes.

Policy makers and businesses should develop forecasting and monitoring exercises to identify triggers that could have significant impact. Again, relevant triggers vary for different actors. The following chart gives an overview of triggers that could turn out to be significant and deserve the attention of decision makers:

Table 1

Overview of scenario shifts, risks and opportunities and preparation and mitigation measures

	SHAKY CHINA	CONFRONTATIONAL CHINA
NECESSARY CONDITIONS	(status quo)	Escalation in the Taiwan Strait
DRIVING FACTORS	(status quo)	Military and political confrontation between the US and China
MAIN RISKS (FROM A EUROPEAN PERSPECTIVE)	For governments: <ul style="list-style-type: none"> • Volatile bilateral relations with China • Politicization of economic relations and supply chain dependencies • External pressure (by China and US) leads to reactive not proactive policy making For companies: <ul style="list-style-type: none"> • Supply chain risks (in particular for critical raw materials) • Rising competition by Chinese companies in China and the Global South 	For governments: <ul style="list-style-type: none"> • Global economic and supply chain crises • Global security crisis • Global political crisis and bloc-building • Pressure to choose sides in a bifurcated world For companies: <ul style="list-style-type: none"> • Economic, financial and supply chain risks • Sudden forced decoupling from China • Pressure to choose sides in a bifurcated world
MAIN OPPORTUNITIES (FROM A EUROPEAN PERSPECTIVE)	For governments: <ul style="list-style-type: none"> • Still some time and room for maneuver to increase resilience, improve competitiveness, develop mitigation toolbox and build alliances. For companies: <ul style="list-style-type: none"> • Business opportunities in China along recent trajectories (factoring in growing constraints in many industries) 	For governments: <ul style="list-style-type: none"> • Re-shoring of production to Europe For companies: <ul style="list-style-type: none"> • High demand for defense and security related industries to equip Europe and likeminded countries
MAIN PREPARATION AND MITIGATION MEASURES (PARTICULAR RELEVANCE, BUT PART OF A TOOLBOX ACROSS ALL SCENARIOS)	For governments: <ul style="list-style-type: none"> • Analyze dependencies and create transparency • Diversification • Improve competitiveness and resilience • Better use defensive instruments and develop new instruments to expand economic security toolbox For companies: <ul style="list-style-type: none"> • Analyze risks and dependencies and create transparency • Diversification of markets and supply chains • “Enjoy the China success story while it lasts”: Pursue business opportunities and profits in China, but factor in that the success-story may end anytime 	For governments: <ul style="list-style-type: none"> • Guard rails and deterrence against military escalation For companies: <ul style="list-style-type: none"> • Pursue a global strategy that can withstand forced decoupling from China



SUCCESSFUL CHINA	RESTRAINED CHINA	REFORMIST CHINA
Chinese advances in technology and economy/Homegrown crisis of the West	Broad coalition of US and likeminded partners to contain China's rise	Crisis in China leads to a course correction
Technological break throughs, a shift towards a new, sustainable development model, and all-pervasive party-state control	Western alienation from China and growing risk perception	Economic crisis in China
For governments: <ul style="list-style-type: none"> Chinese dominance in global affairs China reshapes global institutions and the global order, together with Russia Rising dependencies and weaponization of economic relations Pressure on Western values and political systems For companies: <ul style="list-style-type: none"> China becomes a global technology leader Rising, often unfair competition in China and third markets, that seeks to replace Western companies 	For governments: <ul style="list-style-type: none"> US dominance and less room for EU to pursue an independent agenda Rising risk of military escalation Increased defense spending Inflation due to high cost of partial decoupling from China For companies: <ul style="list-style-type: none"> Significantly less business on the Chinese market; partial (forced) decoupling Risk of secondary sanctions 	For governments: <ul style="list-style-type: none"> Over-enthusiasm and renewed "naïveté" about China's reforms For companies: <ul style="list-style-type: none"> Continued strong competition from Chinese companies
For governments: <ul style="list-style-type: none"> Short-term benefits for European companies that have supported China's course and undermined unity For companies: <ul style="list-style-type: none"> Short-term benefits and niche opportunities for companies with technologies that China needs 	For governments: <ul style="list-style-type: none"> Stability and strong alignment within the West Less Chinese challenges to global institutions and the global order More opportunities for engagement with the Global South For companies: <ul style="list-style-type: none"> Less economic and technological competition from China Level playing field in the West and better opportunities in the Global South 	For governments: <ul style="list-style-type: none"> More stable political relations Renewed opportunities for cooperation and partnership agenda More room for maneuver for Europe from lowered tensions between US and China For companies: <ul style="list-style-type: none"> Return to a more reliable long-term open business environment in China
For governments: <ul style="list-style-type: none"> Dramatically improve economic and political resilience in Europe. Massive investments and regulation efforts to improve Europe's technological competitiveness Monitor and protect against illegitimate political influence Create momentum for Global Gateway For companies: <ul style="list-style-type: none"> Protect and expand competitiveness outside China Prepare contingency scenarios for Chinese dominance of industry 	For governments: <ul style="list-style-type: none"> Strong alignment of G7 and like minded partners Pursuit of free trade and investment agreements Engaging new partners in the Global South For companies: <ul style="list-style-type: none"> Increase resilience towards supply chain, sales or market access shocks from China. Invest in parallel supply chains and innovation structures outside China 	For governments: <ul style="list-style-type: none"> Political engagement with China on all levels Support of social, educational and cultural exchanges in all forms that are not politically instrumentalized by China in unacceptable ways For companies: <ul style="list-style-type: none"> Pursue business opportunities with a clear understanding of the risks involved.

Scenario Methodology

The scenario method is a useful tool to prepare for the unpredictability of future developments. It can help us to take advantage of the resulting opportunities, while minimizing risks and perhaps even turning them into opportunities. The goal is to enhance capacity to act strategically rather than merely reacting.

The scenarios described in this study were developed at MERICS in 2022, with methodological guidance from the Fraunhofer Institute for Systems and Innovation Research (ISI). The scenarios described here do not imply an expectation that any of them will occur in their pure form. However, they identify key factors, analyze their interactions and seek to create plausible, coherent pictures of the future.

Methodologically, the scenarios were developed in several steps. The initial question was: "How might China develop during the five years of President Xi Jinping's third term in office, which lasts till 2027?" Over several workshops, this question was broken down a) into sub-areas relevant to overall developments b) for which reasonably precise assumptions or mini-scenarios could be developed. From the initial 40 areas, a set of 15 key factors was selected that could be used to draw a reasonably comprehensive picture of China's development. They include political factors (such as the political system or China's role in the world), economic factors (such as growth paths or domestic and foreign economic developments) and technological factors (such as China's technological independence).

For each of these 15 variables, workshops were held to develop and discuss several future assumptions that were as clear-cut as possible. Although extreme and disruptive developments were also considered, only assumptions that seemed more realistic and probable were included in the further elaboration stage. For instance, in workshops on China's political system, the idea that a revolution might push the CCP out of power was played with. However, any such event seemed too unlikely and its pathway too unpredictable to make it worthwhile planning for this eventuality. Only upheavals that are conceivable under CCP rule were included in the process of further elaboration (such as a return to collective leadership after the end to the Xi era, whenever that might happen).


A subsequent influence and consistency analysis assessed the likelihood of individual manifestations occurring together. Did they favor each other? Were they mutually exclusive? Or did they have no influence on each other? For example, was it conceivable that China would engage in a military conflict over Taiwan in the coming years while simultaneously ending its rivalry with the United States? Given current developments on both sides, this was all but ruled out in the next five years. The assumptions made in the consistency analysis can be traced in this overview.

Subsequently, software was used to check for consistent combinations across the multitude of factors, to identify scenarios containing a largely consistent set of future assumptions that are free of major contradictions. From these, the five scenarios outlined in this publication were developed in further workshops and are presented here.

Exhibit 4

Factor Influence Matrix

0 = (almost) independent
 1 = some influence
 2 = strong interdependence



	China-US relations	China's role in blocs and coalitions	China's hard power projection	China's economic governance model	China's domestic economic sustainability	China in the global economy	China's macro growth path	China's technological independence	China's innovation capacity	China as a digital actor	China's political system	China's stability and social policy	Cross-strait relations	Energy system and supply	Food and water systems and supply
	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
1 China-US relations		2	2	0	0	1,5	1	2	0,5	0	1	0,5	2	0,5	0,5
2 China's role in blocs and coalitions	2		2	0,5	0,5	2	0,5	2	0,5	1,5	0,5	0	2	1	0,5
3 China's hard power projection	2	2		0	0	1	1	2	0,5	0	0,5	0,5	2	0	0
4 China's economic governance model	1,5	1,5	0		2	2	2	1,5	2	1,5	1	1	0,5	0	0
5 China's domestic economy sust.	0	0	0	2		1,5	2	0,5	1,5	0	1,5	2	0	1	0,5
6 China in the global economy	1,5	2	0,5	1	2		2	2	1	1,5	0	1	0,5	1,5	1
7 China's macro growth path	1	1,5	1,5	1	2	1		0,5	2	0	2	2	0,5	2	1
8 China's technological independence	2	2	1	0	0,5	2	0,5		2	1	0	0,5	1,5	0	0
9 China's innovation capacity	2	1,5	1,5	1,5	2	1,5	2	2		1,5	0,5	0,5	0,5	1	0,5
10 China as a digital actor	1	1	0	0	1	2	1	0,5	1,5		0	0,5	0	0	0
11 China's political system	2	2	2	2	1	1	1,5	1	1,5	1		2	2	0,5	0,5
12 China's stability and social policy	0,5	0,5	0,5	0,5	1	0	0,5	0	1	0,5	0,5		0,5	0	0
13 Cross-strait relations	2	1	2	0	0	0	0,5	1,5	0,5	1	0,5	0,5		0	0
14 Energy system and supply	0	1	0	0	1,5	1	1,5	1	0	0	0,5	0,5	0		0
15 Food and water systems and supply	0	2	2	0	0,5	1	0,5	0	0	0	0,5	1	0	0	

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Exhibit 5

Scenario Methodology



■ Shaky China ■ Successful China ■ Restrained China ■ Reformist China ■ Confrontational China

FACTOR	FUTURE PROJECTION A	FUTURE PROJECTION B	FUTURE PROJECTION C	FUTURE PROJECTION D	FUTURE PROJECTION E
1 China-US relations	US dominance	Chinese dominance	Great Power Truce	Indirect military conflict	
2 China's role in blocs and coalitions	Fragmentation and case-by-case coalitions	US-led bloc vs. China-led bloc	Dysfunctional multilateralism		
3 China's hard power projection	Regional dominance	Increased power projection	Power projection in new domains	Military conflict	
4 China's economic governance model	"Xi Jinping System" of party-state economy	Decentralized state-guided economy	Return to liberal reforms		
5 China's domestic economic sustainability	Continued imbalance	Green, healthy growth and demand	Debt-fueled, unsustainable growth	War-time economy	
6 China in the global economy	Mixed success in diversification and value-chain upgrading	Successful diversification and value-chain upgrade	Diversification and value-chain upgrades blocked		
7 China's macro growth path	4% GDP growth - Muddling through	4-5% - Sustainable, healthy growth	2% - Slow, but healthy	2% - Slow and chaotic	0% - External crisis
8 China's technological independence	Two standards, dual circulation	China on track to economic independence	China cut off	Back to global unity	
9 China's innovation capacity	Progress continues, but slows	Innovative breakthroughs	Stalled innovation capacity	Bifurcation: two separate innovation ecosystems	
10 China as a digital actor	Splinternet	China sets global standards	Chinanet		
11 China's political system	Leadership transition struggles	Greater centralization of leadership	Collective leadership		
12 China's stability and social policy	Stability through surveillance	Repression, but passive resistance			
13 Cross-strait relations	Beijing increases pressure on Taiwan	Escalation below the conflict threshold	A more independent Taiwan	Cross-Strait talks	Military conflict
14 Energy system and supply	Much coal, little renewables	Breakthrough in renewables	Small insecurities and disruptions		
15 Food and water systems and supply	Securing food and water at any cost	Securing supply without controversy	Partial cooperation	"Feed your friends"	

Exhibit 6

Assumption consistency analysis			1 China-US relations				2 China's role in blocs and coalitions			3 China's hard power projection				4 China's economic governance model			5 China's domestic economic sustainability			
			A	B	C	D	A	B	C	A	B	C	D	A	B	C	A	B	C	D
1 China-US relations	A	US dominance																		
	B	Chinese dominance																		
	C	Great Power Truce																		
	D	Indirect military conflict																		
2 China's role in blocs and coalition	A	Fragmentation and case-by-case coalitions	0	0	0	-1														
	B	US-led bloc vs. China-led bloc	0	0	0	0														
	C	Dysfunctional multilateralism	-2	1	0	1														
3 China's hard power projection	A	Regional dominance	-1	1	0	1	2	1	1											
	B	Increased power projection	0	1	0	1	1	1	1											
	C	Power projection in new domains	0	0	0	0	1	1	0											
	D	Military conflict	0	0	-1	2	1	0	1											
4 China's economic governance model	A	"Xi Jinping System" of party-state economy					1	1	0	0	0	1	0							
	B	Decentralized state-guided economy					0	0	0	0	0	0	0							
	C	Return to liberal reforms					0	0	0	0	-1	0	-1							
5 China's domestic economic sustainability	A	Continued imbalance	0	0	0	0	0	0	0	0	0	0	0	2	0	-1				
	B	Green, healthy growth and demand	0	2	0	-2	0	1	0	0	0	0	-1	-1	1	1				
	C	Debt-fueled, unsustainable growth	0	-1	0	0	0	0	0	0	0	0	0	2	0	-1				
	D	War-time economy	-1	-1	-2	2	1	0	0	0	0	0	2	2	-2	-2				
6 China in the global economy	A	Mixed success in diversification and value-chain upgrading	0	1	0	0	0	0	0					1	0	-1	1	0	-1	0
	B	Successful diversification and value-chain upgrade	-1	2	0	0	1	1	0					0	0	0	-1	1	-1	-2
	C	Diversification and value-chain upgrades blocked	1	-2	-2	2	0	-1	0					2	-1	-2	0	-2	1	2
7 China's macro growth path	A	4% GDP growth - Muddling through	0	1	0	-1	0	1	0	1	1	1	0	1	-1	0	1	-2	2	0
	B	4-5% - Sustainable, healthy growth	0	2	0	-2	0	2	0	1	2	1	-1	-2	-1	2	-2	2	-2	-2
	C	2% - Slow, but healthy	0	0	0	-2	0	2	0	1	0	0	-1	0	0	2	0	1	-2	-2
	D	2% - Slow and chaotic	1	-1	0	0	0	0	0	0	-1	0	0	-2	1	-2	1	-2	-1	0
	E	0% - External crisis	0	-2	0	0	0	0	0	0	-2	0	0	0	0	0	1	0	-2	0
8 China's technological independence	A	Two standards, dual circulation												1	0	-2	0	0	0	1
	B	China on track to economic independence												0	-1	-1	2	-2	2	2
	C	China cut off												1	0	-2	2	-1	2	2
	D	Back to global unity												-2	-1	2	0	2	0	-2
9 China's Innovation Capacity	A	Progress continues, but slows	0	-1	1	0	0	0	0	0	0	0	0				1	0	0	0
	B	Innovative break-throughs	0	1	1	0	0	0	0	1	1	1	1				-1	2	-1	-1
	C	Stalled innovation capacity	2	-2	0	0	0	1	0	-1	-1	-2	-1				1	-1	1	0
	D	Bifurcation: two separate innovation ecosystems	0	-1	-2	1	0	1	1	0	0	0	0				1	-1	1	1
10 China as a Digital Actor	A	Splinternet					1	1	-1	1	0	1	0							
	B	China sets global standards					-2	-1	-1	1	1	2	-1							
	C	Chinanet					1	2	0	0	0	0	1							
11 China's Political System	A	Leadership transition struggles	1	0	0	0								0	0	0	0	0	0	0
	B	Greater centralization of leadership	0	2	0	0								2	-1	-2	2	-1	2	0
	C	Collective leadership	0	0	0	-1								0	0	0	-1	1	-1	0
12 China's stability and social policy	A	Stability through surveillance	0	0	0	0	1	1	0	0	0	0	0	1	0	-1				
	B	Repression, but passive resistance	1	-1	-1	0	0	0	0	0	0	0	0	1	0	-1				
13 Cross-strait relations	A	Beijing increases pressure on Taiwan	0	0	1	0	2	1	2	2	1	0	-2	0	0	0	0	0	0	-2
	B	Escalation below the conflict threshold	0	1	2	-2	2	2	0	-2	-2	2	-2	1	0	0	0	0	0	-2
	C	A more independent Taiwan	1	-2	1	-2	-1	-1	-1	-2	-2	0	-2	0	0	0	0	0	0	-1
	D	Cross-Strait talks	-2	2	0	-2	0	0	0	0	0	2	-2	1	0	0	0	0	0	-2
	E	Military conflict	0	2	-2	2	-1	2	2	0	0	-2	2	1	-1	-2	1	-1	1	2
14 Energy system and supply	A	Much coal, little renewables	0	1	1	1	0	0	0	1	1	1	1	1	1	1	0	-2	1	1
	B	Breakthrough in renewables	0	1	0	-1	0	0	0	0	0	0	-1	0	0	0	0	2	0	0
	C	Small insecurities and disruptions	0	-1	-1	0	0	0	0	-1	-1	0	0	0	0	0	0	-1	0	1
15 Food and water systems and supply	A	Securing food and water at any cost	0	-1	0	2								1	0	0	0	1	0	0
	B	Securing supply without controversy	0	2	1	-2								0	0	1	0	0	0	-2
	C	Partial cooperation	1	2	1	1								0	0	0	0	0	0	-1
	D	"Feed your friends"	0	0	1	-2								1	-1	-1	0	0	-1	0

[illegible]

Scenario Descriptions



Shaky China



This is the baseline scenario: China will continue along its current trajectory. Xi Jinping struggles to manage the country's numerous challenges, most critically a slowing economy.

This is the baseline scenario in which China's economy, politics and engagement with the world follow the trends seen at the outset of Xi Jinping's third term in office. It is a muddling through scenario: China neither makes impressive progress, nor faces an existential crisis.

In this scenario, mixed signals make it hard for analysts to determine if China is on track to meet the goals of becoming a "modern socialist country" in 2035 and reach "rejuvenation" in 2049; whether growth has peaked; or if China is heading into deep trouble. There will be success stories (perhaps more supercomputers, impressive advances in space, or demonstrations of military power) that Beijing will proudly present to its people and the world as proof that China under Xi remains on the rise. At the same time, there will be failures and atrocities (perhaps insolvencies at banks or real estate developers, financial and job stress, or yet more repression of ethnic minorities and religious groups). Any news of these will be censored in China but will unsettle many in Europe or the United States. Xi's "New Era" will be haunted by old problems. The prominence given to "stability and control" in his agenda underscores that the system stands on shaky the ground.

SCENARIO OUTLINE

The greatest headaches for China's leadership lie in its slowing economy, the ripple effects it creates and the difficulties of shifting to a more sustainable economic model. Even if GDP could be expected to grow at around 4 percent annually, the price for such relatively stable expansion would be high. Growth remains unbalanced and dependent on non-sustainable routes to economic expansion, such as infrastructure investment and high exports. China's party state continues to have a strong hand in the economy, issuing tight guidance on specific industries and key technologies. Doubling down on industrial policy and investment is likely to weigh down overall economic efficiency still further. All companies are expected to fulfill state objectives, with the party insisting on patriotism and redistribution through policies associated with ideas such as "Common Prosperity".

China has had mixed success with efforts to diversify its export markets and access to key imports such as critical raw materials or high-tech components. Exports of medium-tech products remain the core of China's economic model. There has been some value chain upgrading and success in some high-tech technologies, but overall China continues to lag behind in key high-tech industries. Where Beijing feels its economic security is at stake, it carefully regulates competition with foreign companies, giving domestic companies time to develop their own technology ("dual circulation"). Beijing has high ambitions for China to become an innovation powerhouse and has seen progress in some areas of applied research, but China remains uncompetitive in basic research. Where the government invests a lot of resources and shields innovators from foreign competitors, they manage to innovate. This is not enough to sustain China's economy, nor to make it more innovation-driven in the long run. In the Global South, China continues to gain influence as a provider of high-tech products such as digital infrastructure and set norms. In digital industries, China has become a tech leader in surveillance, but its internet remains largely isolated from the world wide web, leading to a Chinese "splinternet". Parallel standards interoperability and data flows remain critical issues and stand in the way of meaningful international cooperation.

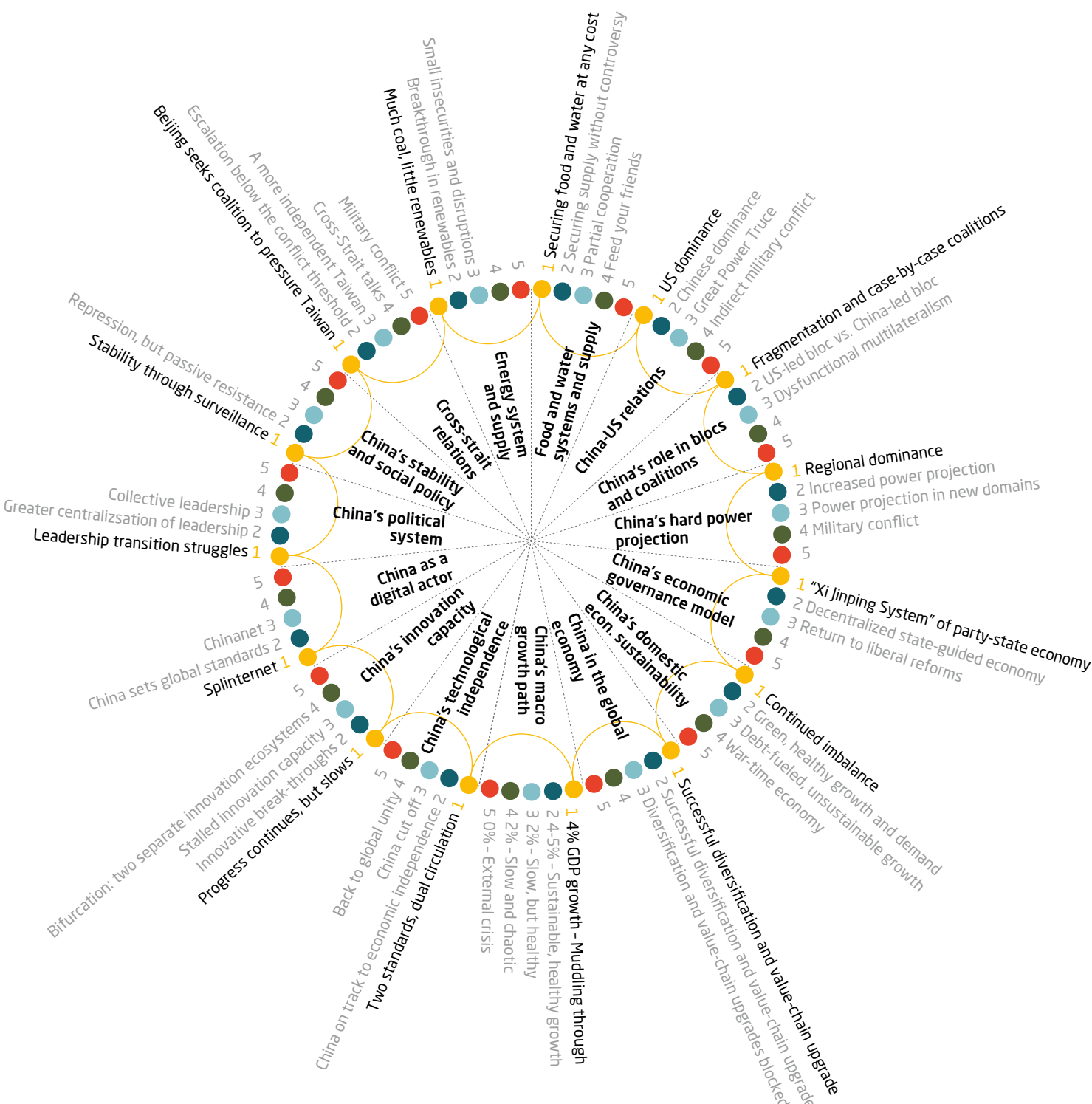
Exhibit 7

Scenario overview: Shaky China

Factors and future projections



Shaky China Successful China Restrained China Reformist China Confrontational China



Politically, Xi remains unchallenged, but is under high pressure to deliver. What the Chinese population cares about most, besides economic growth and opportunities, is Beijing's social policies, such as reforms of the health, pensions or education systems. Xi has outlined a mix of new policies to provide better public services coupled with effective surveillance to contain discontent. If this mix proves "good enough" to maintain stability, Xi may have sufficient political power to extend his reign yet again at the 21st Party Congress. However, he will then be 73 years old and under greater pressure to reveal a path to an orderly succession. The party leadership will inevitably become preoccupied in one way or another with thinking about what comes after him.

The international sphere will be fiercely contested but continue to be dominated by the United States and its likeminded allies. Both sides share the perception they are in a great power rivalry that will shape the world for decades. But Beijing grudgingly accepts that – at least for now – the United States remains too powerful to be openly challenged. Both sides are trying to reduce their dependencies on the other, e.g. in technologies or critical supplies. But they are also making efforts to manage their competition to prevent the many brewing conflicts from escalating into an uncontrollable crisis that neither Beijing nor Washington wants.

The continuing rivalry between the two superpowers has a price for the international order. Institutions are weakened, even as most global institutions continue to follow the established rules and Western countries put up an effort to prevent China from changing them. Instead of broad international agreements, unilateral laws and mini-lateral agreements generate fragmentation. Frameworks such as China's "Belt and Road Initiative", the "Global Development Initiative" or the "Global Security Initiative" will continue to attract followers and partners in the Global South, but few will tie themselves exclusively to China. A welcoming attitude towards China's economic engagement is not necessarily mirrored in security cooperation.

As a military power, China is establishing itself as the most influential actor in its direct neighborhood. This is not enough to meet Beijing's ambitions, but it helps expand and test its influence in the region. China may show more willingness to engage in regional military conflicts, e.g. over territorial disputes with India. China's military build-up continues, with the aim of achieving dominance in the South China Sea and the Taiwan Strait in particular. Military pressure on Taiwan is increasing. Beijing uses its political, military and economic muscle to push other countries in the region to accept its ambition of "complete reunification". At the same time, the United States is building its own coalition (e.g. with Japan, Australia, Philippines) to push back against Beijing.

POTENTIAL IMPLICATIONS FOR EUROPE

As this is the "dynamic status quo" scenario, *European governments* face risks from volatile bilateral relations with China. Concerns include the politicization of economic relationships and supply chain dependencies. With the United States and China exerting substantial pressure, European states risk pursuing reactive policies rather than proactive policy making. This could lead them to overlook the opportunity that the "Shaky China" scenario presents; namely that there is still time, and room, for maneuvers to increase resilience, improve competitiveness, expand the mitigation toolbox and build alliances. *European companies* can pursue their China business strategies along recent trajectories (with signals about an increasingly constrained business environment already factored in). But they need to be aware of risks arising from more intense competition from Chinese companies, both in China's market and third countries.

Confrontational China



In this scenario, tensions over Taiwan have come to a point where the grey-zone conflict is escalating and an open military conflict seems imminent. This leads to extreme bifurcation and far-reaching de-coupling between China and the West.

This scenario does not attempt to model a war over Taiwan. Obviously, a military conflict involving China and the United States could have catastrophic global consequences: the ultimate, extreme outcome would be World War III, which should not be discarded as mere dystopian science fiction. Nevertheless, we stop short of trying to imagine the course an actual full-blown war would take and instead anticipate the dynamics in and around China that must be expected if tensions were to rise to a point where a war seems imminent.

Different pathways could lead to a situation that can be read as a point of no return. (If this is hard to envisage, remind yourself of the build-up of tensions before Russia's 2022 attack on Ukraine.) Signals that an escalation will be hard or impossible to avoid might include Chinese military exercises modeling an invasion, massive cyber-attacks on Taiwan, propaganda preparing the Chinese people for a war or offensive lobbying by Beijing to rally its international allies behind it, most importantly Russia. Likewise, US assertiveness in the Pacific, including more deployments of forces, deliveries of weapons systems to Taiwan or official recognition of Taiwan's political leaders could also lead to an escalation. Spiral dynamics are at play. Such tensions could drag on for months or even years, but any spark or accident could set in motion military plans that all parties have in place.

SCENARIO OUTLINE

In a "Confrontational China" scenario, the rivalry (and, in this case, open conflict) between China and the United States becomes the defining force shaping global affairs both politically and economically.

Both Beijing and Washington would use all available means to get other countries to choose sides and to show their support militarily, politically and economically, by cutting ties to the other side wherever possible. The decoupling, which has been part of political rhetoric for years but has only materialized in limited ways, could become a force sweeping across all sectors - from tourism to academic cooperation to joint efforts against climate change. Multilateral institutions such as the UN or G20 could quickly become largely dysfunctional.

The realization that the world may be about to head into a military escalation over Taiwan would have catastrophic effects on the global economy. The United States and its allies would use sanctions and every kind of political pressure to cut China off from large parts of the global economy. An open-ended breakdown in supply chains would likely trigger a global recession, including a financial markets crash and massive problems for corporate financing. China would be hit hard, suffering from flat or negative economic growth.

Western sanctions and pressure would also largely cut off China from global technology and innovation ecosystems. It would be prevented from acquiring the materials and talent needed for key technologies. China's progress towards value-chain upgrading or technology sovereignty in areas such as semiconductors would be halted, laying bare its dependency on imports of high-tech systems and components.

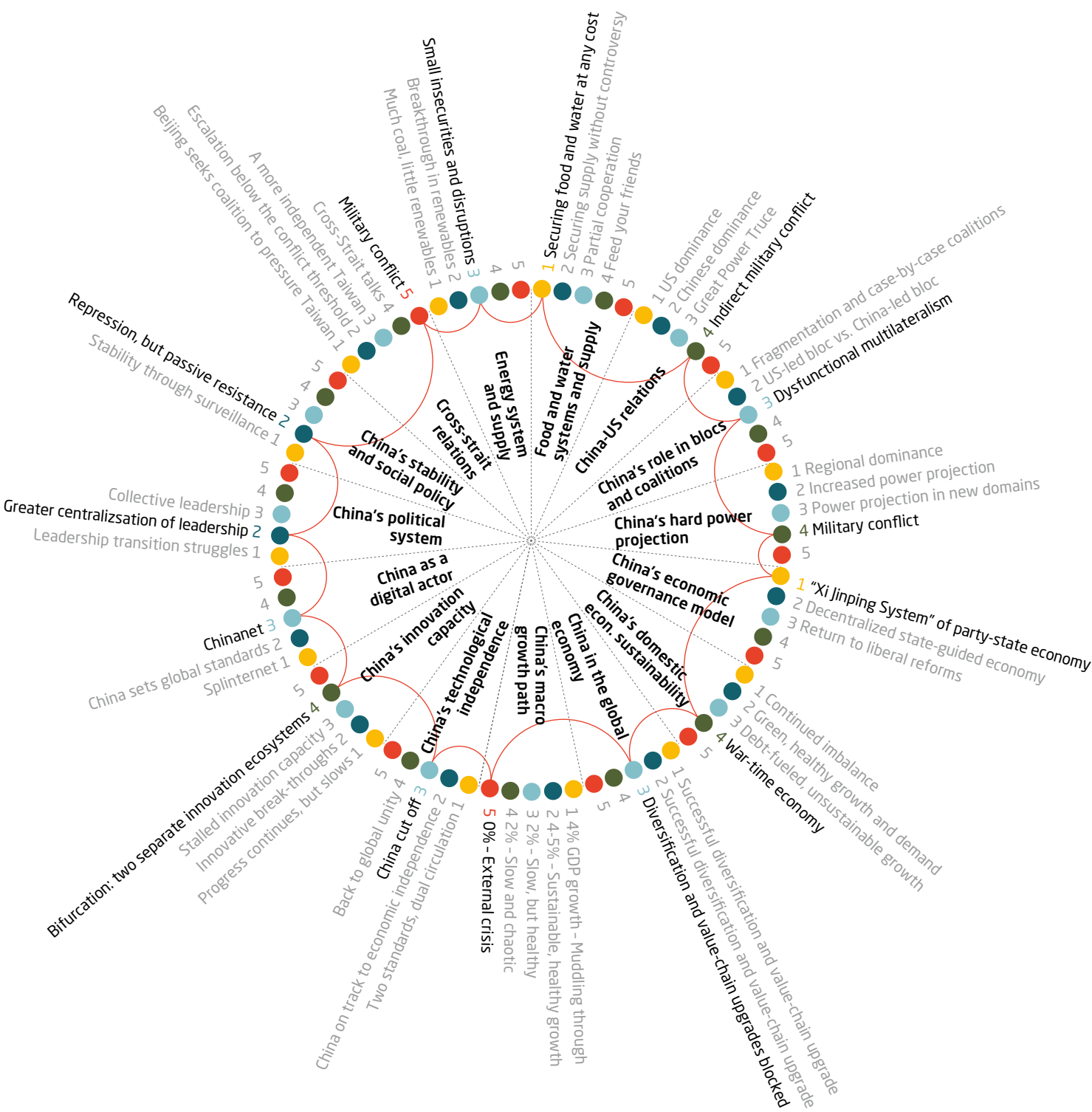
Exhibit 8

Scenario overview: Confrontational China

Factors and future projections



Shaky China Successful China Restrained China Reformist China Confrontational China



China would have to further intensify its efforts towards self-reliance. Even if it managed to join forces with other countries dissatisfied with the United States, China's innovation system would suffer severely from losing its links with the rest of the world. The world of technology would experience a radical bifurcation, as the West would expel Chinese-designed standards from most industries. China's tech firms would develop domestic solutions to comply with Chinese regulation. China's netizens would live in an almost completely isolated "Chinanet".

China's government would do its best to camouflage such vulnerabilities by partly shifting to a war-time economy: it would reorient sections of the economy along war-time principles, such as pushing high quantitative growth through the military-industrial complex by building weapons and military supplies. At the same time, China is large enough to buffer against many shortages by prioritizing supplies to strategically important areas, such as the major metropolises.

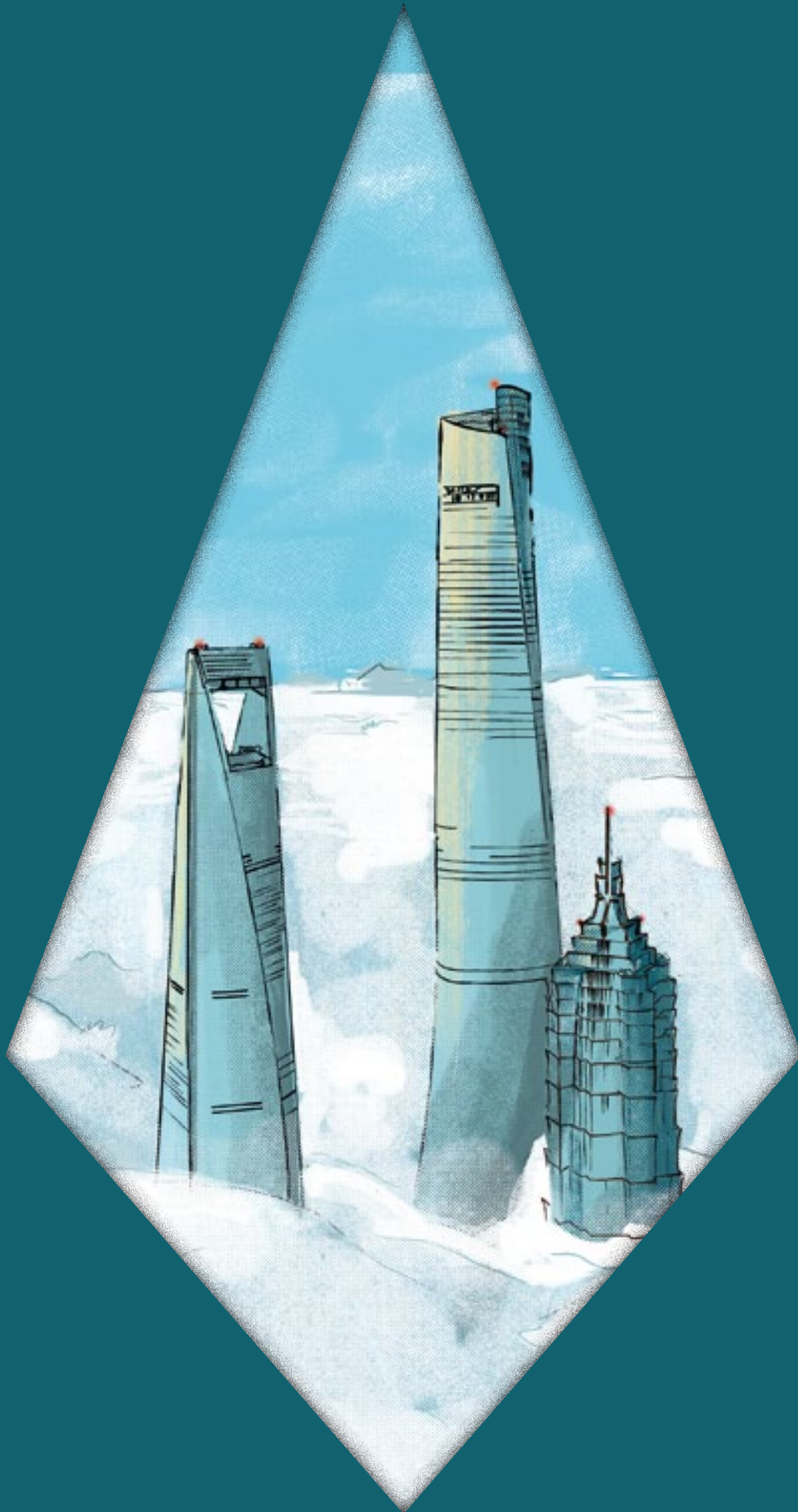
What would this mean for China's political system? Probably little change. China has been in a resilience and struggle mode for years, making preparations to stay functional in exactly this kind of situation. Xi Jinping would likely double down on policies of stability and control by further centralizing key government functions and steering the country from within a very small circle of trusted allies.

Socially, an economic crisis, supply shortages, travel restrictions and a harsh political climate would lead to widespread dissatisfaction. Unemployment would rise, particularly youth unemployment. Parts of the urban middle class and even the economic elite would feel alienated. To maintain stability, the CCP would turn to the toolbox of surveillance and social repression that it has developed so well and used to keep social tensions at bay during the Covid-19 pandemic.

POTENTIAL IMPLICATIONS FOR EUROPE

This scenario entails the most detrimental disruption of the status quo. *European governments* and global institutions would face the need to react to global economic and supply chain crises; a global security crisis; and a global political crisis – all at the same time. Countries around the world would be under intense pressure to “choose sides” between the United States and China. For Europe, this would mean an obvious, though not pain-free, choice in favor of the transatlantic partnership. A very thin silver lining might lie in the opportunity to re-shore some business operations to Europe. *European companies* would be confronted with the massive effects of a global economic and financial crisis. Sanctions and political pressure could force corporates into sudden decoupling from China, similar to their exit from the Russian market in 2022. The very few beneficiaries would be defense and security-related industries because defense expenditures would rise in European, and likeminded, countries.

Successful China



In this scenario, China is seen to achieve key goals in Xi Jinping's ambitious agenda: greater technological independence, sustainable green growth and global influence rivalling the United States. The West's huge homegrown problems aid China's success.

China's ambitions must be taken seriously. It is worth remembering that China has time and again surprised the world (including itself) by being more successful than many thought possible. This fact should be set against mainstream analysts' consensus view at the outset of Xi Jinping's third term of a country with rising socioeconomic challenges that are unlikely to be overcome with his policy toolbox of increased centralization and control.

China doesn't need to fulfill all its ambitions in order to be viewed as the more successful world power. Success is not necessarily measured in absolute terms: relative success could be enough to put China on a trajectory to surpass the United States as the dominant power, even inside the 5-year time frame of this scenario exercise. A home-made crisis in the Western world could play into China's hands. Political and economic troubles in the United States (e.g. triggered by large-scale social unrest after the 2024 presidential elections) or the EU (e.g. triggered by the political, economic and social spillovers from wars in Europe's neighborhood) could produce a situation where China is perceived as relatively more stable, resilient and future-oriented. Such perceptions matter. In a world dominated by great power rivalry, countries and companies watch closely which power seems on the more promising – or less troubled – pathway.

SCENARIO OUTLINE

The three necessary preconditions for the shift into a "Successful China" scenario would be i) a significant crisis for the West; ii) sufficiently tangible Chinese success stories that suggest China has an edge in major future developments and iii) a successful power play with the Global South. Such success stories might come from a combination of technological breakthroughs and advances in the shift to a more sustainable development model and leadership in green technologies.

Innovative breakthroughs in basic research and applied innovations in industries could create growth and give China a global technological edge. A fundamental upgrade in China's innovation capacities would take more than five years. However, a few high-profile advances could help to create the perception that China is on track to becoming an innovation powerhouse. Technological breakthroughs would also help put China on the path towards a high degree of economic security with both tech sovereignty and tech leadership in key areas. China's government would be able to overcome chokepoints or engineer around them to avoid dependence on other countries. For China to reach this degree of independence in a relatively short time, a precondition would be that foreign technology providers cooperate largely on China's terms, whether willingly or through coercion. China would then find it easier to set global standards, bolstered by support from developing countries and scant resistance from developed countries. The more that Chinese innovations become attractive to the rest of the world, the more China will be able to export high-tech products and capture greater value-added within China.

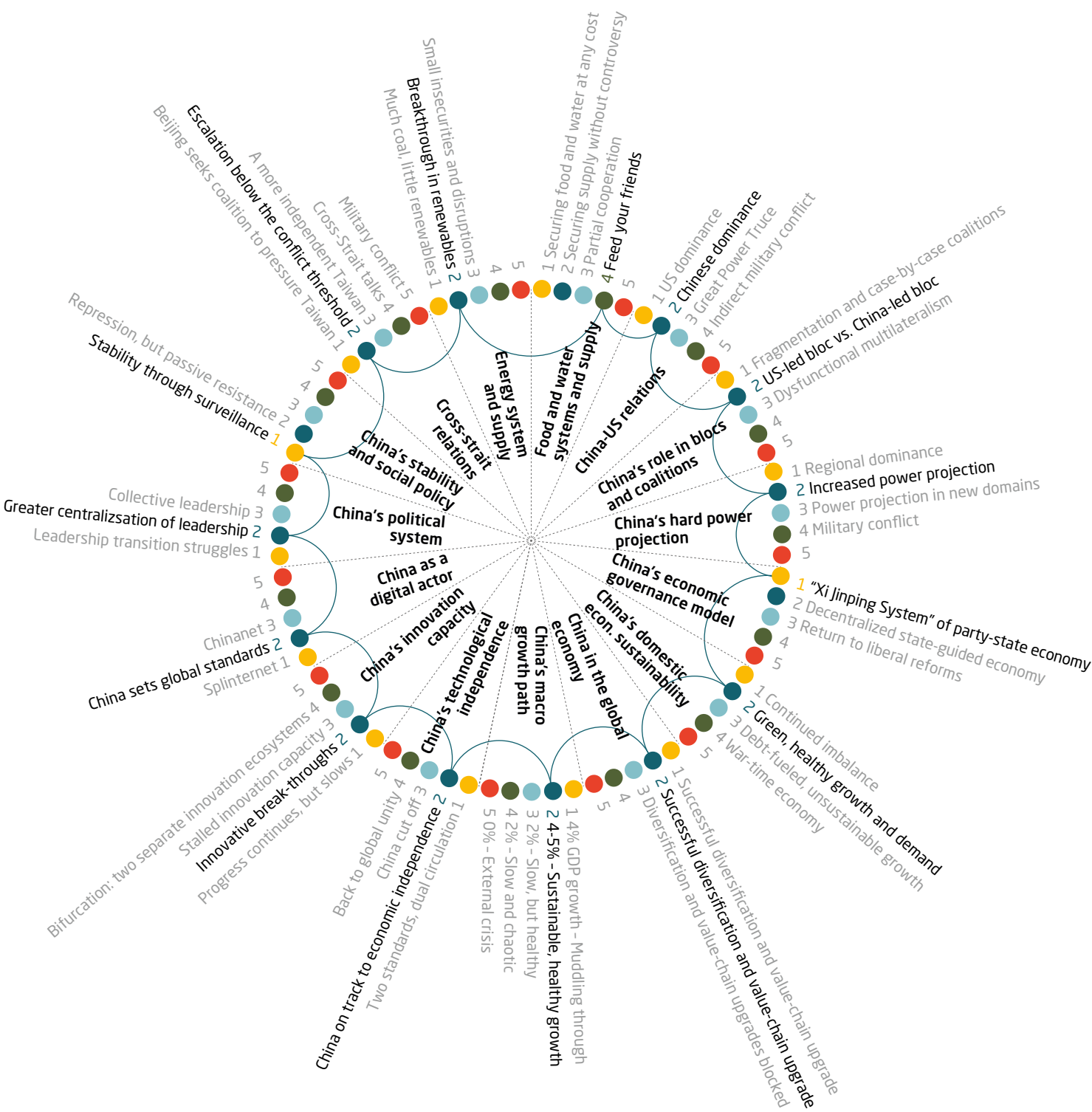
Exhibit 9

Scenario overview: Successful China

Factors and future projections



Shaky China Successful China Restrained China Reformist China Confrontational China



Another impactful signal that China is on the road to success would be strong evidence of significant progress in shifting its economy to a more sustainable development model and global leadership in green technologies. Indicators would be major investments in green infrastructure and green consumption patterns. GDP growth rates would reflect sustainable and healthy growth (roughly 4 percent) that can improve livelihoods in the long term.

On the global stage, China would increasingly be seen as the dominant power, coming out “on top” in rivalry with the United States and starting to rewrite global rules. China’s dominance cannot be expected to find broad acceptance immediately. The world would split into two blocs that view each other primarily as adversaries: A US-led block with G7 countries at the core versus a “coalition of the unsatisfied” led by China (with support from Russia). But it would be China that is more successful in solidifying its influence in the Global South and in international forums, and it may succeed in exporting specific aspects of the China model (including a deep-rooted surveillance state).

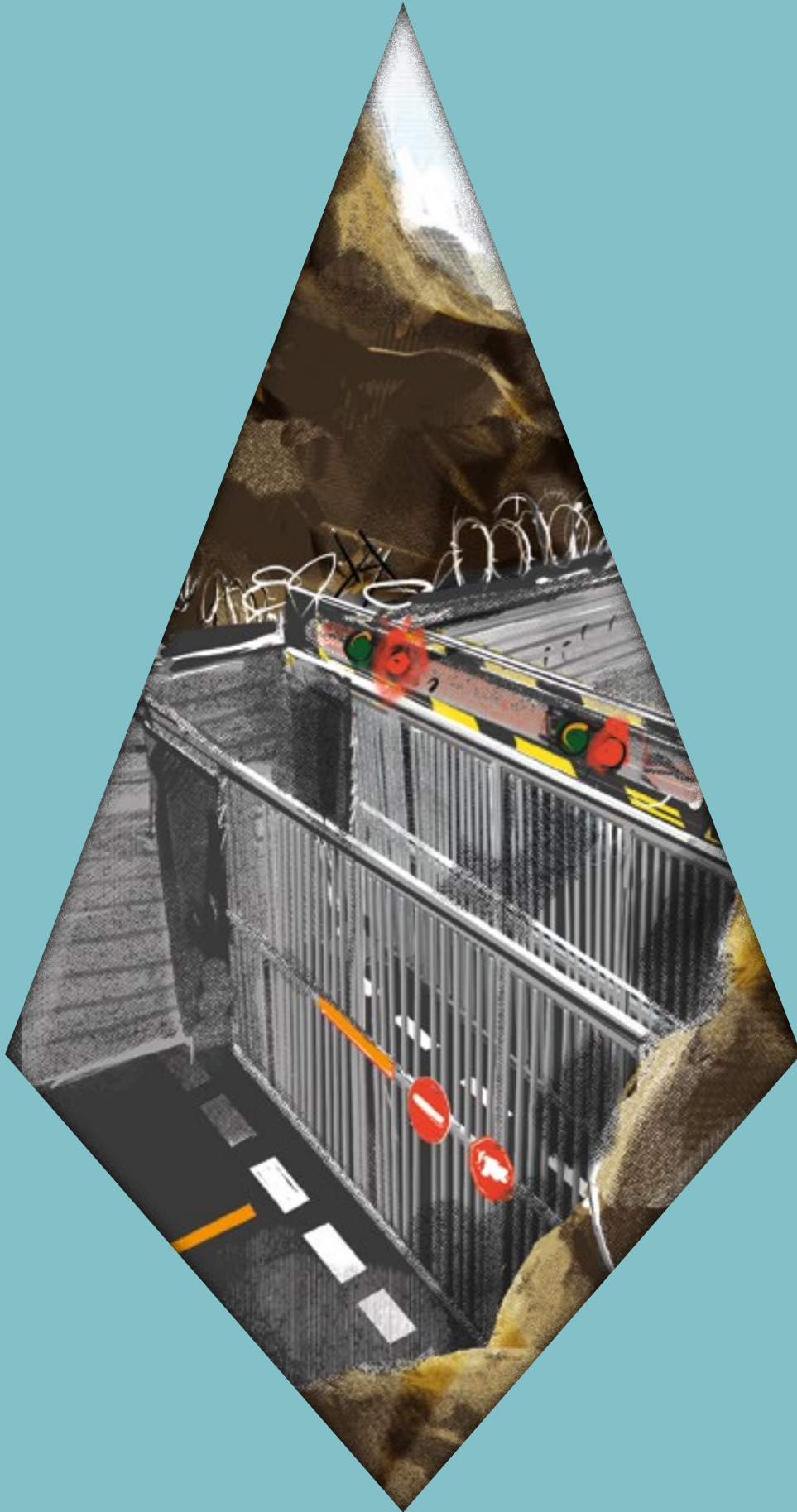
Militarily, China would increase its power projection, expanding both its capabilities and willingness to use traditional military capacity. This could include more intense intelligence gathering, additional overseas military facilities and abandonment of principles of non-interference and non-use of force in international relations. In the Taiwan conflict, Beijing would successfully keep pushing red lines, e.g. by taking control of some islands in the Taiwan Strait. At the same time, China would expand its hybrid warfare and project self-confidence that it can eventually tilt the military balance in the Taiwan Strait, while continuing to bide its time.

China’s success would go a long way towards cementing the authority of Xi personally and the political system he has installed. It would be propagandized (not without merit) that China’s system of one-party rule and a party-state economy, which takes a very active role in steering the economy and innovation system, can produce better results than Western democracies and market economies. This would surely provide Xi with the political power to centralize leadership even further and extend his tenure at the 21st Party Congress in 2027 in a “Helmsman” or “Party Chairman” role.

POTENTIAL IMPLICATIONS FOR EUROPE

This scenario, in which China is perceived to be relatively more stable, resilient and future-oriented than the West, comes with the risk of a gradual erosion of the existing world order. *European governments* would be confronted with an increasingly assertive China that – together with Russia – moves to reshape global institutions according to its own interests. Economic dependencies on China would rise and would be increasingly weaponized. Also, China would exert increasing pressure on Western values and political systems. *European governments* that previously supported China’s course (at the cost of European and Western unity), stand to gain short-term benefits from privileged ties with Beijing, but would also lose their longer-term room to maneuver. *European companies* would need to operate in a world market where, increasingly, China is the technology leader that sets standards, dominates supply chains and aims to replace Western companies with Chinese ones. Businesses would face rising, often unfair competition in China and third markets, except for some short-term benefits and niche opportunities in industries where China urgently needs foreign technology.

Restrained China



In this scenario, China is in trouble: External pressure (from the United States and likeminded countries) and internal problems hamper China's efforts to diversify its economy, maintain growth and achieve technological independence.

This is the scenario that China's leadership has long been afraid of – and that many US policy makers are implicitly (or even explicitly) working towards: a “Restrained China” which is under tremendous pressure from the United States and likeminded countries and increasingly unable to successfully pursue its political, economic and technological agenda. On the sidelines of the National Peoples' Congress in March 2023, Xi Jinping complained that “Western countries led by the United States have contained and suppressed us in an all-round way, which has brought unprecedented severe challenges to our development”. While many in the United States avoid the loaded term “containment”, it is official policy to compete with China in all areas, including its military ambitions and its quest for technological independence. At the same time, China's own problems, in particular slow growth, an unbalanced economy and lack of innovation power, plus an over-emphasis on ideology and centralized decision making, can seriously hamper China's development and lead to the country restraining itself.

SCENARIO OUTLINE

A necessary precondition for a shift into this scenario would be for the United States to succeed in forming a large alliance of middle powers, including the EU, Japan and key actors in East Asia and Latin America, with the shared aim of slowing and containing China's development. For the United States and its partners, such an approach would bring massive economic and political costs. A move towards this scenario is therefore best imaginable if triggered by disruptive events. While we do not explore what would need to happen for such a coalition to take shape, it seems reasonable to envisage something similar to the G7 countries' sanctions against Russia after it launched its full-scale invasion of Ukraine.

In this scenario, the international community splits into two blocs that view each other primarily as adversaries: A dominant US-led block with G7 countries and other likeminded partners at the core versus a “coalition of the unsatisfied” led by China and supported by Russia. As a military power, China's ability to project traditional military capacity stalls, but Beijing focuses on building up non-traditional military capabilities (e.g. cyber warfare). Beijing would continue grey-zone operations against Taiwan below the threshold of an open conflict. Meanwhile, international support for Taiwan might grow, opening new room for maneuver, for instance membership of international institutions. Beijing would see this as an open provocation. Either way, tensions and fears about escalation in the Taiwan Strait would remain high.

Economically, this scenario puts China under tremendous pressure. The disruption of large parts of its international trade would force the government to bolster whatever internal sources of growth it can find. Even if China managed to avoid a recession and reach modest growth (around 2 percent), its economic expansion would be chaotic, unsustainable and debt-driven. Under stress, the central government might have to give up some of its control over the economy, e.g. by decentralizing more decision-making power back to the provinces and municipalities or by easing regulation of industries vital to growth.

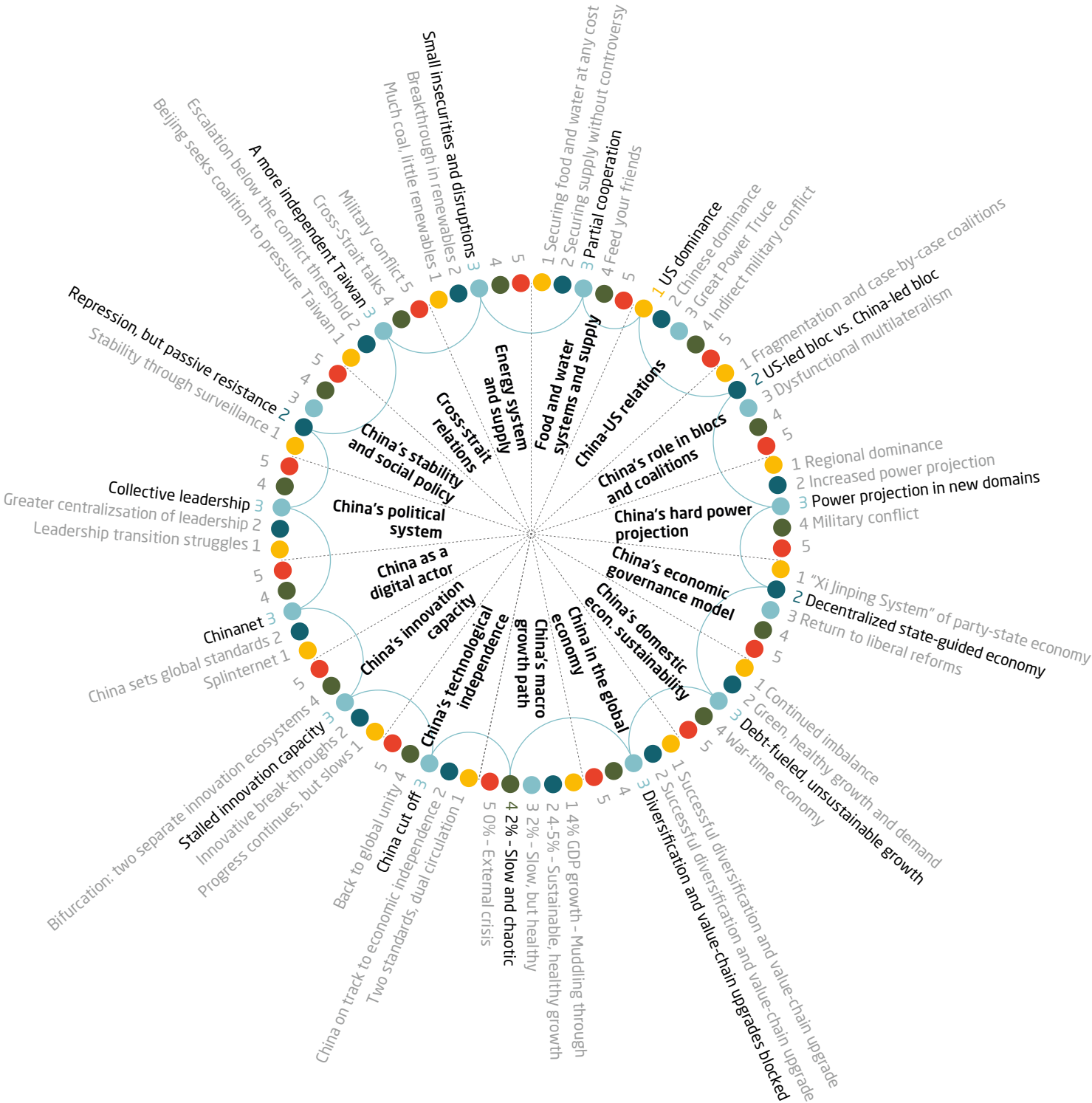
Exhibit 10

Scenario overview: Restrained China

Factors and future projections



Shaky China Successful China Restrained China Reformist China Confrontational China



While the government could release some of the short-term economic pressure, the technological consequences would be severe and damaging. In a “Restrained China” scenario, the United States and its allies would successfully block China’s value chain upgrades and pursuit of independence in key technologies. China would be isolated from cutting edge technology and the global innovation ecosystem. International companies operating in China would have need to withhold their latest technologies from China for fear of being sanctioned. The Chinese economy would have to rely on home-grown innovation. Although China has leading technology in some areas, its overall progress in many fields, including semiconductors, would be halted, along with its efforts to set standards globally. China’s economy risks falling into a middle income trap. Digitally, China would also be largely isolated.

The economic stress would increase social tensions and discontent. State propaganda would paint China as the victim of Western containment. Massive surveillance and direct social repression would silence any criticism of the leadership’s course. Within the party leadership, Xi would likely face a struggle to avoid challenges to his authority. Many in the party would hold him personally responsible for China’s troubles and openly or covertly start planning for the post-Xi era. This might possibly see a return to the collective leadership system that he has worked hard to discard.

Intense socioeconomic pressures and the likelihood of challenges to Xi’s authority, make this a dangerous scenario. There is a direct pathway to an escalation in the Taiwan Strait and the “Confrontational China” scenario. However, Western proponents of a coalition to counter China’s rise argue that external pressure is what is needed to trigger an internal course correction, putting the system on a “Reformist China” path.

POTENTIAL IMPLICATIONS FOR EUROPE

This scenario is implicitly or even explicitly pursued by mainstream US China policy; it could create high political and economic costs on the European side of the Atlantic. *European governments* might find it harder to pursue an independent agenda vis-à-vis an emboldened United States. The risk of military escalation in the Pacific region may require increased defense spending. Partial decoupling from China would bring high costs and rising inflation. Nevertheless, a “Restrained China” scenario would also come with significant political opportunities: stability due to a strong alignment between likeminded countries; diminishing Chinese challenges to the global order and institutions; and more room for engagement with the Global South. *European companies* would suffer from their China business shrinking; partial (forced) decoupling; and the risk of secondary sanctions. The benefits include less economic and technological competition from China, a more level playing field in the West and better opportunities in the Global South.

Reformist China



In this scenario, China's internal crises result in a political course correction. Confrontation between China and the West starts to ease amid hopes of a new "Deng-Xiaoping-moment" and a return to pragmatism.

This scenario would undo some of the features of the "Xi Jinping-system" that have put China in such fierce opposition to the West. A "Reformist China" implies a course correction and return to "reform and opening up". Just as Deng Xiaoping's generation decided Mao had over-reached in his zealous pursuit of a Communist paradise, this scenario anticipates that the CCP could come to a similar conclusion about Xi's "road to rejuvenation", seeing it as a blind alley rather than a route to restore China's glory.

Although many in the West would like to see a return to a "Reformist China" and the "good old days", it appears the least likely of the five scenarios in this study. It runs counter to Xi's efforts to secure centralized authority and control. Nonetheless, many Chinese leaders and diplomats know that many foreign politicians and businesses still want to hear and believe that the era of "reform and opening up" continues and will remain China's modus operandi. But even if the party decided to change course, a new reform push is unlikely to resemble what happened four decades ago, or what many in the West want or expect. The party might pragmatically discard some of Xi's more extreme policies, e.g. towards technological self-reliance, while staying firm in areas where China is successful. A new "Reformist China" might become less of a rival and more of a partner again, but it would remain a fierce competitor.

SCENARIO OUTLINE

An internal crisis in China that calls for an urgent and fundamental course correction is a necessary precondition for a "Reformist China" scenario. It is relatively easy to imagine how such a crisis might arise. Rising socioeconomic stress means it is far from certain how effective Xi's policy toolbox - focused on centralization and control - will be. Experiences from China's handling of the Covid-19 pandemic show what powerful repressive mechanisms the party has put in place to prevent public discontent or internal rifts becoming visible. Alternatively, a situation where Xi exits the political stage (for whatever reason) could also trigger dynamics that create room for a course correction.

Whatever the pathway into a "Reformist China" scenario, the party would discard parts of the highly-centralized "Xi Jinping system" and reverse course to adopt the collective leadership model of the post-Mao era. A reshuffle at the top of the CCP hierarchy would be accompanied by some ideological shifts. Xi might end up with the same score card as Mao, "70 percent right, 30 percent wrong". Regardless of personnel changes at the top, the party's social governance mode would remain a mix of social policies that provide better public services and extensive surveillance to contain discontent. Maintaining stability and securing the party's leading role would stay top of the political agenda. However, reform signals would go a long way towards reconciling those who have become alienated from the system and China's direction, especially in the urban middle classes.

A "Reformist China" economic policy could see a return to more liberal reforms, like some of then-Premier Zhu Rongji's reforms in the 1990s and early 2000s. The market would regain a more important role, with the government focused on regulation and rule-setting. The shift would not rebalance the Chinese economy overnight, but it might initiate a

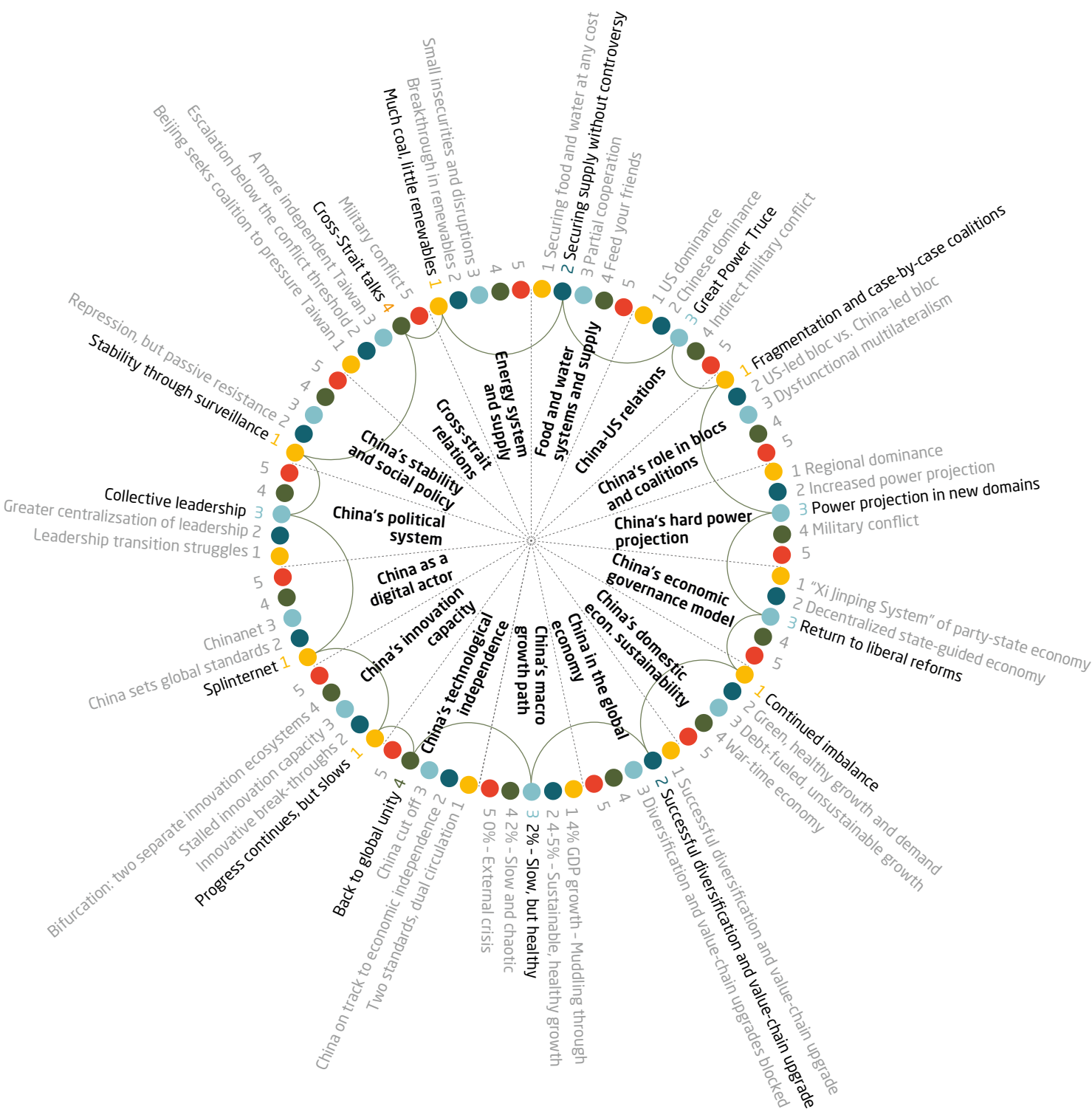
Exhibit 11

Scenario overview: Reformist China

Factors and future projections



Shaky China Successful China Restrained China Reformist China Confrontational China



controlled deceleration of the economy towards slow, but healthier, growth. Under these circumstances, even low growth figures of around 2 percent could be seen as “taking a hit” to implement reforms, trimming unhealthy growth and expanding sustainable sectors.

China’s approach to innovation and technology would undergo similar liberalization and re-integration into global ecosystems. China’s government would proclaim the vision that with better integration, China could become more attractive to the rest of the world, build up exports of high-tech products and capture far more value-added within China. China’s quest for independence and tech-supremacy would become less acute. In return, Western countries would become less opposed to providing China with cutting-edge technology and more ready to trust in cooperation for mutual gain. China would be able to gain greater influence as an innovation partner, make progress in some areas of applied research and even set norms in certain industries, in particular for the global south. In digital economies, China would still maintain its own “Splinternet”, with data flows and exchange remaining a critical issue.

In the international sphere, a “Reformist China” could turn the tide of intensifying Sino-US rivalry. Washington and Beijing might arrive at an agreement to cease treating each other as adversaries, in favor of a “Great power truce”. The erosion of the international order and its institutions could be slowed, even if both sides continued competing for partners and coalitions and tried to strike unilateral and mini-lateral agreements. Being mindful of international perceptions and the need to deflate tensions, China would put less emphasis on projecting and expanding military power in traditional domains. Nevertheless, Beijing would continue to build up non-traditional military capabilities and pursue close military cooperation with Russia. Vis-à-vis Taiwan, Beijing would continue its grey-zone operations, though it would be less insistent on pushing red lines and less aggressive in its language. With receptive political counterparts in Taipei, Beijing might even reopen cross-Strait talks.

POTENTIAL IMPLICATIONS FOR EUROPE

Confrontation between China and the West would ease. *European governments* and companies would have far more opportunities than risks. These include more stable political relations with China; renewed opportunities for pursuing cooperation and a partnership agenda. Lower tensions between China and the United States could yield greater political leeway for Europe. The risks would lie in over-enthusiasm and renewed naïveté towards China’s reforms and ambitions. A more pragmatic “Reformist China” is not necessarily a weaker or more Western oriented China. *European companies* would still experience strong competition from Chinese companies, but could compete in a more reliable, open business environment, which is more encouraging for long-term engagement.

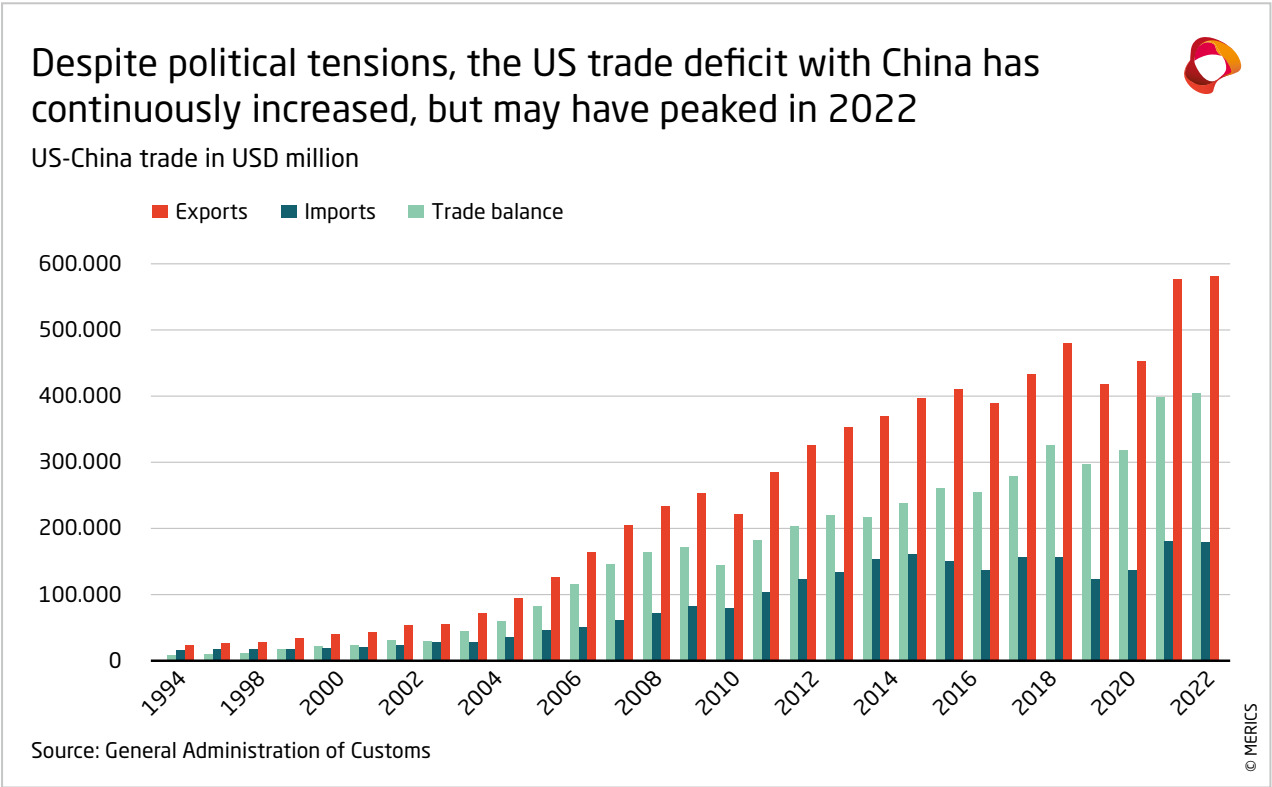
China-US relations

STATUS QUO

China’s leadership considers itself in long-term strategic competition with the United States. The Chinese Communist Party (CCP) is convinced that any US administration will work to prevent China’s rise, orchestrate an international alliance to curb its influence, discredit its political system and undermine stability. The CCP leadership believes China’s political system (which it has baptized “whole-process people’s democracy” to reject a binary choice between democracy and autocracy) will prove more effective than US democracy in the long run, and that the United States is a declining power. For now, China must live with US dominance, notably US military supremacy in the Asia Pacific and US economic and technical pre-eminence. Beijing aims to maintain stable, predictable relations with the United States. Meanwhile, it is trying to improve China’s resilience towards risks such as US efforts to block China from access to certain technologies or capital. Beijing is developing its own retaliatory toolkit against US sanctions or trade restrictions. Growing US-China tensions are generating mutual suspicion and hostility among ordinary citizens of both countries.

DRIVERS AND DYNAMICS

Beijing wants to decrease dependencies on the United States. Having seen the G7 apply sanctions on Russia for its attack on Ukraine, the CCP leadership wants to protect China against similar pressures. This is particularly true of the financial sector as well as the tech sector where Beijing has noted Russia’s isolation from the Swift banking transfers system and frozen foreign reserves.



US-China relations in the coming years are highly contingent on US politics. The relationship's specifics will hinge upon who holds power in Washington, though there is a far stronger bipartisan consensus on strategic challenges vis à vis China than previously. To counter US dominance, China aims to expand ties with the Global South; it will shape its own networks of partnerships and alliances, deploying the twin wrappers of Beijing's Global Security Initiative and Global Development Initiative.

FACTOR ASSUMPTIONS

What might China-US relations look like in 2027?



FUTURE PROJECTION	DESCRIPTION	SCENARIO
US dominance	The status quo assumption: The US-led West seeks to protect the global order. Bilateral relations are characterized by US attempts to contain China's political, economic and technological advances, either openly or implicitly. Washington seeks to generate support, though many countries (in particular those in the Global South) are reluctant to give it.	<div>■ Shaky China</div> <div>■ Restrained China</div>
Chinese dominance	<p>China appears to be on a more successful trajectory than the US – at least in relative terms. China is widely perceived as being on course to come out 'on top' in the great power rivalry with the US and rewrite the global order.</p> <p>This would be a considerable shift, though it is highly unlikely that China could reach dominance by 2027. More likely is that Chinese dominance becomes the accepted trajectory among most politicians and business leaders by 2027. This scenario might be triggered by instability, large-scale social unrest or civil-war-like chaos after the 2024 US presidential elections. Likewise, a massive EU crisis - perhaps caused by economic recession and election-wins for right-wing populists – could deliver a blow to the US-led Western alliance.</p>	<div>■ Successful China</div>
Great Power truce	The US and China manage their competition and establish effective guardrails against an escalation that could endanger global stability and world peace. Both sides reduce dependencies and show good will to stop treating each other as adversaries.	<div>■ Reformist China</div>
Indirect military conflict	The grey zone conflict over Taiwan escalates into military conflict. Our assumptions stop short of a full China-US war. Instead, we see Washington providing and mobilizing military support for Taiwan while avoiding joining any war itself.	<div>■ Confrontational China</div>

Note: Other assumptions considered as theoretically possible or wild cards, but excluded from the final scenarios as unlikely within a five-year time-frame or impossible to plan for: Complete decoupling (only "red phone" crisis communication); a shift towards cooperation between the two big powers ("Chimerica"); or a direct China-US war (the danger of a military confrontation is too large to ignore, but planning for consequences of such a global war is beyond the scope of this scenario exercise.)

China's role in blocs and coalitions

STATUS QUO

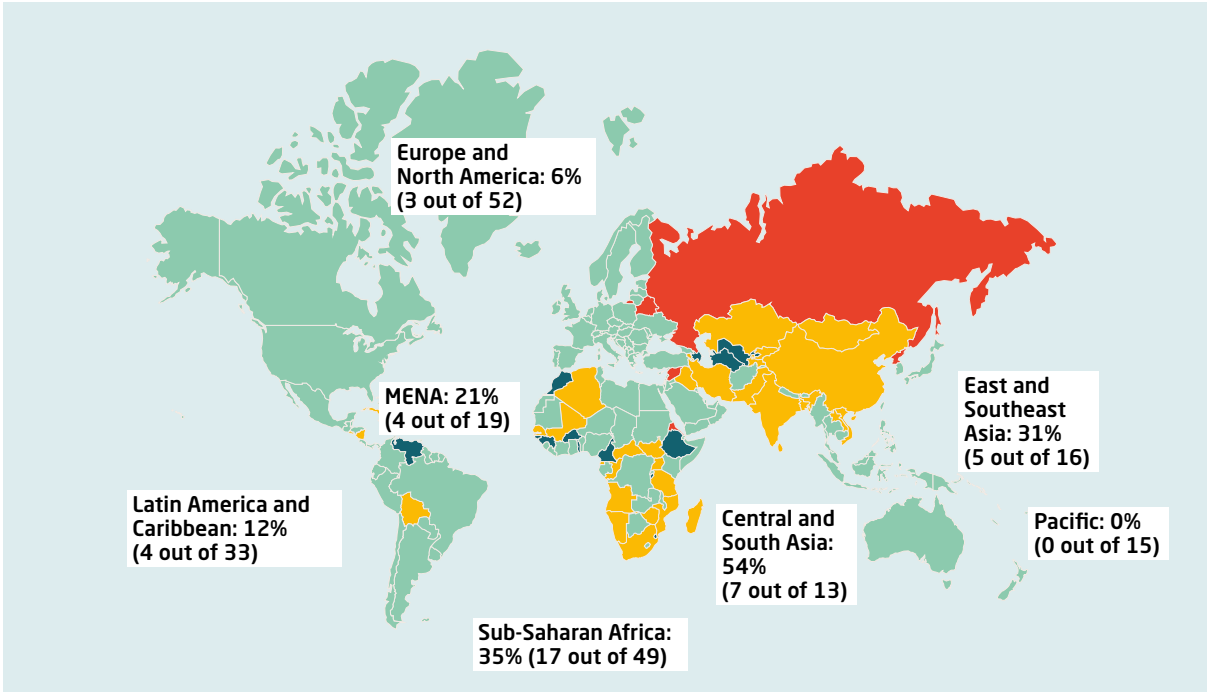
Beijing assumes a leading or co-leading role in coalitions it has participated in forming, such as BRICS or the SCO, and is now pushing to expand those frameworks, especially in the Global South. In firmly-established bodies such as the UN, China exerts influence within the existing structures, aiming to shape them to suit its interests. China is evolving alternative global governance structures as it upgrades its foreign policy paradigm. It is broadening out from the mainly economic focus typified by the Belt and Road Initiative (BRI) to promote security-related initiatives, like the Global Security Initiative, with supporting narratives that are anti-Western or anti-US. So far, this shift does not appear to be particularly successful. However, even if China is not yet able to shift geopolitical alignments across the Global South, it finds a receptive audience for its narratives.

China aspires to lead the Global South economically and politically



Percentage of countries by region that voted “no” or abstained in March 2022 UN General Assembly resolution condemning Russia’s invasion of Ukraine. Almost all of these countries also support China’s Global Development Initiative (GDI).

■ Approve ■ Against ■ Abstain ■ Absent



Sources: United Nations, China's Ministry of Foreign Affairs, MERICS

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DRIVERS AND DYNAMICS

China increasingly declares its ambition to lead in global governance issues and shows determination to shape a post-Western order. China aims to set new rules and shape existing norms to its advantage, but not necessarily to uproot the current order as a whole. The CCP leadership's perceptions are shaped by their belief that China is rightfully re-emerging as a global power.

FACTOR ASSUMPTIONS

What might China's role in blocs and coalitions look like in 2027?



FUTURE PROJECTION	DESCRIPTION	SCENARIO
Fragmentation and case-by-case coalitions	The status-quo assumption sees the international order and its institutions weakened and fragmented. Different standards are emerging, so unilateral and mini-lateral laws and agreements are sidelining multilateral international agreements. International conflicts and global issues are handled via case-by-case coalitions. Beijing's pressure on third countries yields some results, but less than hoped for. Third countries' welcome for China's economic engagement does not extend to military engagement.	■ Shaky China ■ Reformist China
US-led bloc vs. China-led bloc	The world splits into two blocs viewing each other as adversaries: a US-led bloc with G7 countries at the core versus a "coalition of the dissatisfied" led by China (with Russian support). Sometimes framed as "democracy versus autocracy", the blocs do not align straightforwardly around forms of government. China solidifies its influence in international forums and manages to export specific aspects of the China model to some states in the Global South, such as massive surveillance or narratives about the effectiveness of one-party rule.	■ Restrained China ■ Successful China
Dysfunctional multilateralism	International institutions such as the UN de facto collapse under the impact of escalating global tensions.	■ Confrontational China

Note: Other assumptions considered as theoretically possible, but excluded from the final scenarios as unrealistic, at least within the 5-year time-frame: a global order largely dominated by China; one in which China is isolated and largely pushed out of global institutions; or a "G2 world" where the United States and China reconcile and co-manage international affairs.

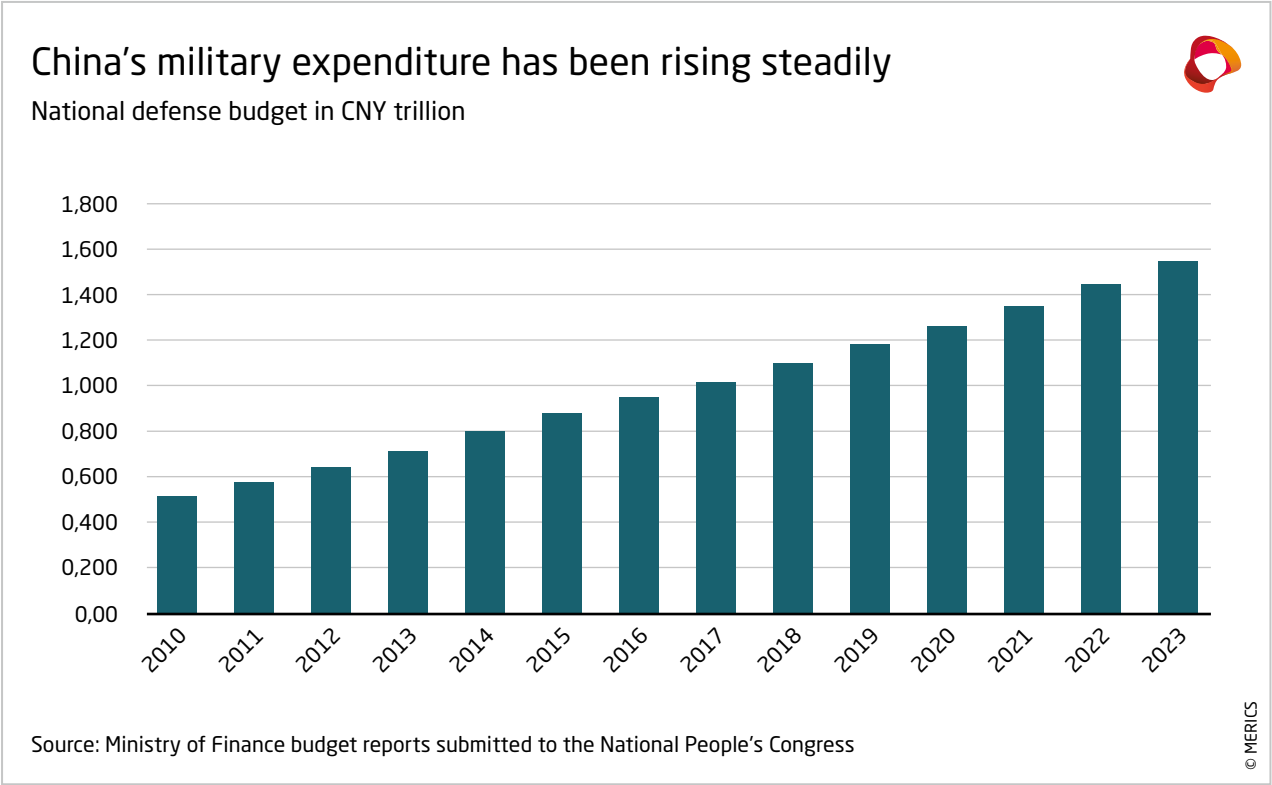
China’s hard power projection

STATUS QUO

China’s foreign policy has become more assertive under Xi Jinping. The CCP believes it has a “period of strategic opportunity” to assume a more central role in international affairs. Yet, it also feels under siege by hostile Western forces. It sees attempts to contain its rise and threats to its core interests and national security in the US presence in the Indo-Pacific, transatlantic cooperation, the QUAD, AUKUS etc. The CCP has established a centralized and unified national security system built around the concept of “comprehensive national security” to tackle threats proactively and preemptively.

DRIVERS AND DYNAMICS

Gaining control over Taiwan and achieving military dominance in its neighborhood are the main objectives behind China’s massive military build-up. These goals require a military that can fight and win wars. China is seeking to project power to defend its interests beyond its neighborhood, e.g., by establishing military bases overseas, and increasing military-to-military cooperation with other countries. It is using platforms such as the Shanghai Cooperation Organization (SCO) or its Global Security Initiative to establish a security framework under Beijing’s leadership and export its views on global security architecture. Russia’s war in Ukraine and the West’s response (sanctions, weapons supply to Ukraine) might further accelerate China’s efforts to expand its hard power, especially its nuclear capabilities.



FACTOR ASSUMPTIONS

What might China's hard power projection look like in 2027?



FUTURE PROJECTION	DESCRIPTION	SCENARIO
Regional dominance	China appears to be willing to engage in regional military conflicts, e.g., territorial conflicts with India. Beijing is broadly perceived as the dominant power in its direct neighborhood, even if the US retains the upper hand in the Indo-Pacific region. China will continue its military build-up, focused on achieving dominance in the South China Sea and Taiwan Strait. Military pressure on Taiwan will increase, along with the likelihood of an attack.	■ Shaky China
Increased power projection	China significantly expands its capabilities and willingness to use traditional military capacity in the region and beyond. Intelligence gathering becomes more intense. China abandons principles of non-interference and non-aggression in international relations. China builds more overseas military facilities.	■ Successful China
Power projection in new domains	Power projection in traditional military capacity stalls. Beijing focuses on building non-traditional military capabilities (e.g., cyber warfare). In Taiwan, it pursues grey-zone operations below the threshold of open conflict. China pursues close military cooperation with Russia.	■ Reformist China ■ Restrained China
Military conflict	Beijing openly prepares for a conflict involving military strikes against Taiwan and – rhetorically at least – threatens a full-scale invasion. For this scenario exercise, we stop at the point where war is imminent or being launched.	■ Confrontational China

Note: Other assumptions considered theoretically possible, but not included in the final scenarios: an official 'mutual defense' military alliance between China and Russia (not feasible within five years); a rift between Beijing and Moscow; or Chinese military interventions abroad (perhaps via humanitarian interventions)

China's economic governance model

STATUS QUO

In recent years, China has become more centralized. Statism has got stronger, at the expense of the private sector. The government now adopts a 'whole nation' approach to development in which private companies must serve state goals. Traditional designations like 'state-owned enterprises' versus 'private enterprises' are increasingly unimportant under Xi's party- and state-guided system.

Xi Jinping's agenda tries to solve long-standing structural problems



New formulation of policies at the 20th Party Congress

Policy objective	1 Reduce inequality	2 Strengthen SMEs	3 Reform the pension system	4 Promote regional development	5 Liberalize capital account
Historic policy	Various Policies e.g. Minimum wage introduction (2004)	SME Promotion Law (2003)	Several measures since 2009, e.g. New Rural Social Pension Schemes	Go West (1999), Rise of Central China (2004)	Qianhai Pilot (2012)/Shanghai Pilot FTZ (2013)
Current policy	Common Prosperity (2021)	Opinions to Promote SMEs (2019)	14th FYP for Human Resources and Social Security (2021)	Dual Circulation Strategy (2020)	Shanghai FTZ (2019)
Xi's 20th Party Congress Report	"The system of income distribution is the foundational system for promoting common prosperity."	"We will support the development of micro, small, and medium enterprises."	"We will improve the unified national management system for basic old-age insurance funds and develop a multi-tiered and multi-pillar old-age insurance system."	"There are still wide gaps in development and income distribution between urban and rural areas and between regions."	"We will promote the internationalization of the CNY in an orderly way."

Source: MERICS

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DRIVERS AND DYNAMICS

The external policy environment is highly unpredictable, given unfolding rifts between China and the West over trade and technology, and unity among G7 nations over the Ukraine war. China's technology sector crackdown, which hobbled a private-sector-dominated growth driver, shows how distinctions between private and state are blurring. Instead, all firms are now charged with fulfilling state objectives. Market oriented reforms are taking a back seat, amid greater emphasis on resilience, self-sufficiency and stability.

FACTOR ASSUMPTIONS

What might China's governance model look like in 2027?



FUTURE PROJECTION	DESCRIPTION	SCENARIO
"Xi Jinping System" of party-state economy	The status quo assumption: Economic centralization and state influence continue to expand. All companies must fulfill state objectives. China uses market mechanisms to direct the economy, combined with redistributionist policies ("Common Prosperity"). More party-directed industrial policy and investment are likely to erode the economy's efficiency.	<ul style="list-style-type: none"> ■ Shaky China ■ Successful China ■ Confrontational China
Decentralized state-guided economy	Under pressure, China increasingly decentralizes state influence over the economy. Similar to the way Bo Xilai in his time as Chongqing party secretary had a high degree of control over his area, local leaders may recover significant autonomy to orchestrate growth. Statism remains dominant but power shifts from central to local level. Another version would be for company conglomerates to gain power and play a similar role as in post-Soviet Russia, setting the rules of the game for the overall economy.	<ul style="list-style-type: none"> ■ Restrained China
Return to liberal reforms	Under extreme economic pressure, Beijing returns to liberal economic reforms similar to Zhu Rongji's in the 1990s and early 2000s. The market resumes a more important role, while government focuses on regulation and rule-setting.	<ul style="list-style-type: none"> ■ Reformist China

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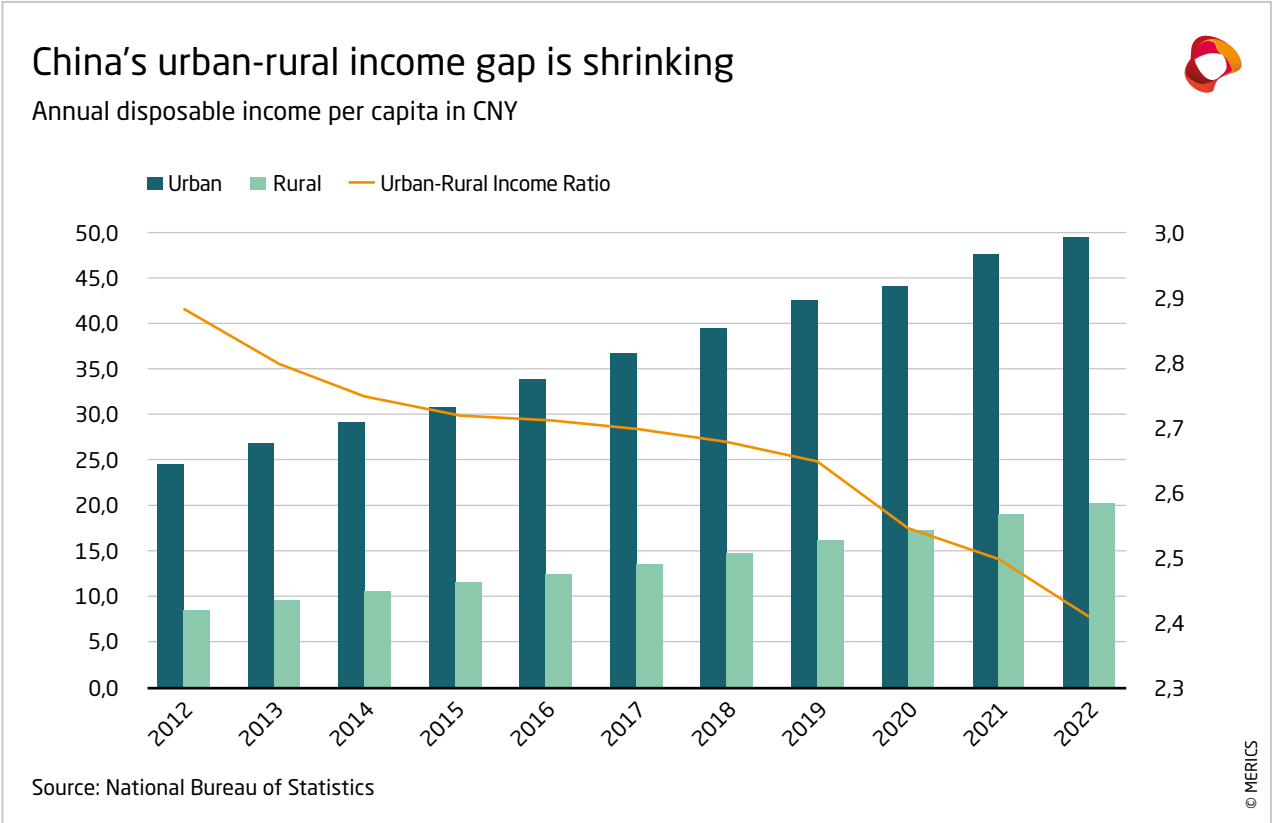
China's domestic economic sustainability

STATUS QUO

China is struggling to shift towards a more sustainable development model driven by consumption and innovation. Whenever things get hard, the government keeps returning to bad habits, resorting to heavy supply-side stimulus to boost stalling GDP growth, though in the last decade it has become slightly more mindful of financial risk build up. There is wide consensus that China's period of relatively easy catch-up growth is ending. China's current growth model, fueled largely by exports, investment and debt, is not sustainable. The government has long called for a shift to an economy that is more driven by domestic demand, but it has failed to give up the kind of state control the current model allows. Any such change implies leaving a larger share of wealth to consumers, who might not spend their incomes as Beijing wants them to.

DRIVERS AND DYNAMICS

The party-state's declared wish to overcome long-standing structural challenges is at odds with how Beijing generally intervenes in the economy. In his 20th Party Congress report, Xi Jinping was explicit about tackling oft-mentioned key problems, such as reducing inequality, strengthening SMEs, reforming pensions, promoting regional development, and liberalizing China's capital account. This begs the question of whether Xi's third term can prove itself different from so many previous generations of leadership. Will any of these goals finally be realized?



Xi will have to overcome many of the challenges that stalled past reform efforts, such as strong vested interests, a perennial focus on stability, the many real risks that could undercut development, and certain factors unique to China's style of policymaking and implementation. However, in a third term, an increasingly powerful and authoritarian Xi could use his unquestioned strength to push an agenda through, no matter the vested interests or risks to stability. Similarly, his exclusively loyalist politburo may be able to hold frank conversations that wouldn't happen if 'rivals' listened in. Or it could just as easily become an echo-chamber of yes-men.

Finally, Xi's grip on power may give him the best opportunity to advance the hard reforms that China needs. However, Xi will have to do so amid unprecedented challenges not faced by his predecessors. At home, Xi faces slower growth and less demand for more infrastructure. Meanwhile, the many, complex risks from abroad include escalating tension between Beijing and Tokyo, tensions over Taiwan, and with the United States and EU (to name just a few).

FACTOR ASSUMPTIONS

What might China's domestic economic sustainability look like in 2027?



FUTURE PROJECTION	DESCRIPTION	SCENARIO
Continued imbalance	The status-quo assumption: China muddles through in the current way. Growth remains mostly export-driven; the economy stays dependent on non-sustainable ways of generating growth.	■ Shaky China ■ Reformist China
Green, healthy growth and demand	China shifts towards a green economy, with domestic demand significantly driven by green consumption. Growth is moderate, but of high quality, and improves people's livelihoods.	■ Successful China
Debt-fueled, unsustainable growth	In a crisis, China's leaders revert to bad habits. They stress quantitative growth targets that are only reachable in unbalanced and unsustainable ways. China's economy remains dependent on exports, coal and construction. As China's gains from catch-up growth are mostly exhausted, this growth path becomes ever more costly.	■ Restrained China
War-time economy	China prepares for – or even starts – a big military conflict, and reorients large parts of the economy using war-time principles. This would yield high quantitative growth with the military-industrial complex building weapons and supplies for the war effort.	■ Confrontational China

Note: Other assumptions considered as theoretically possible wild cards, but not included in the final scenarios: qualitative, green growth coupled with very high growth rates. This seems extremely unrealistic, especially within five years.

China in the global economy

STATUS QUO

China continues its slow upgrading away from low-value added products, helped by having more competitive domestic companies, and regional value-chains. China's asymmetric, mercantilist integration into world trade continues to spread, even as the relative importance of foreign trade to China's economy is decreasing. China has strengthened its position as the world leading trade powerhouse, even in the face of US restrictions on trade and technology exports. Neither US-led restrictions nor Beijing's own efforts to rebalance the country's economy towards domestic consumption have dented the growth of Chinese exports, which now stand at almost 20 percent of the global export total. As imports have been less dynamic, China's external trade surplus has reached USD 900 billion for goods alone.

On the financial side, China has slowed its investments in developing countries. Meanwhile, China has become the focus of hot-money inflows and large scale foreign direct investments (FDI). In 2021, FDI reached a new peak of USD 340 billion, thanks to market opening measures carefully targeted at large firms in priority sectors where China lacks know-how. China seems to have returned to its old practice of recycling those net inflows of hard currency into US treasury bonds. This time, the build-up is not conducted by the central bank to the benefit of the official FX reserves, but by state-owned commercial banks, fueling suspicions of an unofficial mandate to conduct stealth state interventions on the FX markets.

DRIVERS AND DYNAMICS

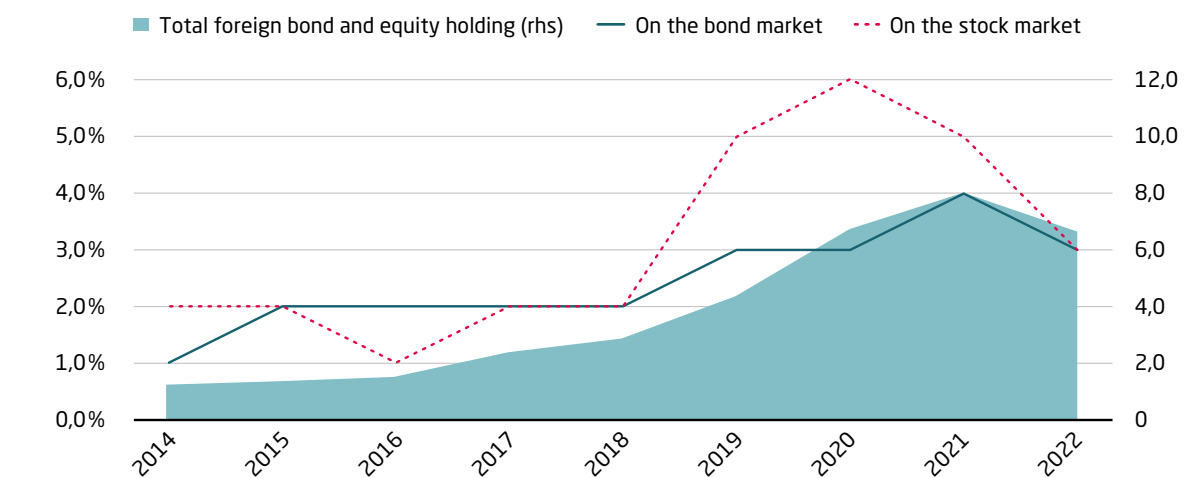
China's economic security concerns increasingly impact its role in the global economy. China's self-sufficiency drive brings pressure to localize, so as to reduce dependency on foreign technology. China's role in global supply chains has been impacted by supply chain shocks (due to strict Covid controls until late 2022) and by wider decoupling dynamics.

China's centrality to trade globalization – in terms of scale – is likely to slowly decrease, while value-chain upgrades and regional integration will increase. Strict capital controls will limit the yuan's position in global finance. Trade tensions and systemic competition in third markets will put more hurdles in front of China's internationalization efforts and could bring a backlash from Western countries. The discussion on trade in most advanced economies has shifted away from growth and efficiency towards securitization, combined with a more assertive stance towards China. Discussion in China mirrors these concerns, but with a clear focus on how to attract high-quality foreign investments in prioritized sectors and develop self-sufficiency in multiple sectors. Chinese exports cannot be expected to continue the same strong growth as over the past years, given the impact of inflation on consumption in the main destination markets for Chinese products. Still, growing involvement in regional value-chains and slow upgrading on the back of targeted opening up and trade agreements will likely continue.

Foreign investors expand footprint on mainland financial markets



Foreign investors on the mainland financial markets (share; total value in million CNY)



Source: CEIC

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FACTOR ASSUMPTIONS

How might China's role in the global economy look in 2027?



FUTURE PROJECTION	DESCRIPTION	SCENARIO
Mixed success in diversification and value-chain upgrading	The status-quo assumption: Mixed success for China's strategy to diversify its export markets and access to high-tech. China manages some value chain upgrading but continues to export mostly medium-tech products (despite impressive achievements in some technologies). Commodity exports remain key to China's model.	<div style="display: flex; align-items: center;"> <div style="width: 15px; height: 15px; background-color: #FFD700; margin-right: 5px;"></div> Shaky China </div>
Successful diversification and value-chain upgrades	Beijing succeeds in shifting from an export-led system to a consumption-driven system. Chinese innovation becomes more attractive globally. China exports increasingly high-tech products and captures more value-added within China. Trade relations with OECD countries are intense, but South-South collaboration thrives.	<div style="display: flex; flex-direction: column; align-items: center;"> <div style="display: flex; align-items: center; margin-bottom: 5px;"> <div style="width: 15px; height: 15px; background-color: #0056b3; margin-right: 5px;"></div> Successful China </div> <div style="display: flex; align-items: center;"> <div style="width: 15px; height: 15px; background-color: #556b2f; margin-right: 5px;"></div> Reformist China </div> </div>
Diversification and value-chain upgrades blocked	The US and its allies successfully block China's value chain upgrading. China stays very dependent on commodity exports and high-tech imports. It remains vulnerable to global economic woes and US efforts to contain it.	<div style="display: flex; flex-direction: column; align-items: center;"> <div style="display: flex; align-items: center; margin-bottom: 5px;"> <div style="width: 15px; height: 15px; background-color: #add8e6; margin-right: 5px;"></div> Restrained China </div> <div style="display: flex; align-items: center;"> <div style="width: 15px; height: 15px; background-color: #ff0000; margin-right: 5px;"></div> Confrontational China </div> </div>

Note: Other assumptions considered as theoretically possible wild cards, but not included in the final scenarios: China, through intensive industrial policy, pooling of resources and indigenous innovation becomes world leader in a specific technology that the United States and allies depend on ("Assassin's mace technologies"). Or political tensions escalate to the point where China imposes an "artificial lockdown" to hurt the rest of the world: China would isolate its economy further from international markets; the world economy would suffer, but so would China.

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China's macro growth path

STATUS QUO

China is trying to change its growth model, shifting to a controlled deceleration after 40 years of high growth and entering a period of increased volatility. Growth numbers get much attention, but only tell a small part of the story. Growth composition is more important. Since at least 2012, Beijing has been trying to exit a debt and real-estate fueled growth cycle in favor of a more sustainable model that is innovation-intensive and consumption-based. It has had limited results. Beijing has tried hard to limit debt, especially after 2016. Those efforts seem to have paid off, stabilizing the debt-to-GDP. However, the pandemic response reversed some of this progress. Regulators have made some substantial gains in bringing more market forces into China's financial markets and improving the business environment (especially on intellectual property and anti-monopoly). More recently, regulators have tightened the screw on the real-estate market, curbing the sector to a point that appears unsustainable for the overall dynamics of the economy. However, the broad imbalances of the Chinese economy remain and may well have increased.

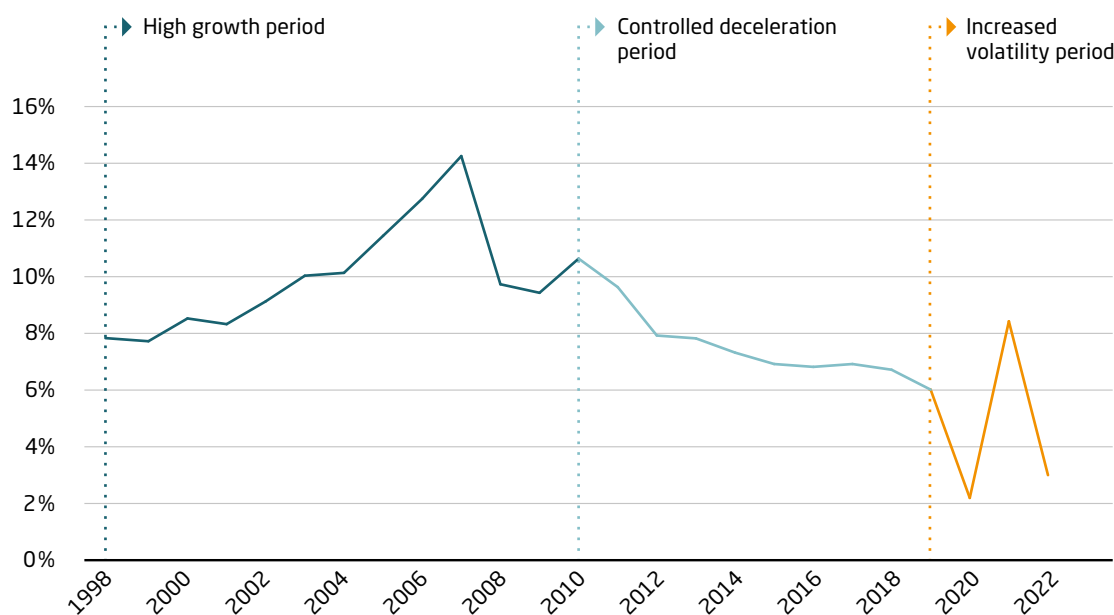
DRIVERS AND DYNAMICS

The era of catch-up growth is coming to an end. Beijing's standard recipe against economic slumps has been to roll out massive stimulus to boost GDP growth, while juggling financial risk build-up. Now, in a more volatile period, downward pressures on the economy are amplified by stagnating reforms and mounting structural issues. These include an ageing population, the top-heavy role of real-estate in the overall economic mix, the lack of sustainable public finances and low productivity.

Growth still relies on construction, state-driven investments, and exports, while consumption and entrepreneurs are still constrained. The flurry of tighter rules and enforcement in recent years, coupled to the erratic zero-Covid policy and a growing emphasis on ideology, has depressed those Beijing most needs in order to pursue its new development model, namely entrepreneurs and households. The lack of substantial pro-social reforms has impeded any rebalancing towards domestic demand, as households prefer to save. State-owned enterprise reform has also stalled over the years. The prioritization of security over growth does not bode well for sustainable growth.

China has moved from a high-growth period to a phase of significantly slower and more volatile growth

Chinese GDP, YoY



Source: National Bureau of Statistics

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FACTOR ASSUMPTIONS

What might China's macro growth path look like in 2027?

FUTURE PROJECTION	DESCRIPTION	SCENARIO
4 % GDP growth – Muddling through	Base-line-scenario: Growth numbers appear relatively high, but fundamental imbalances remain.	Shaky China
4-5 % – Sustainable, healthy growth	The most optimistic scenario from Beijing's perspective, it assumes that China manages to maintain relatively high growth during a quick shift to a new growth model.	Successful China
2 % – Slow, but healthy	Controlled deceleration as GDP growth takes a hit so the party state can implement reforms, cut out unhealthy growth and expand sustainable sectors.	Reformist China
2 % – Slow and chaotic	China's economy suffers under external and internal pressure.	Restrained China
0 % – External crisis	If China appears to be entering a large-scale military conflict, sanctions from the US and its allies will cut it off from much of the global economy.	Confrontational China

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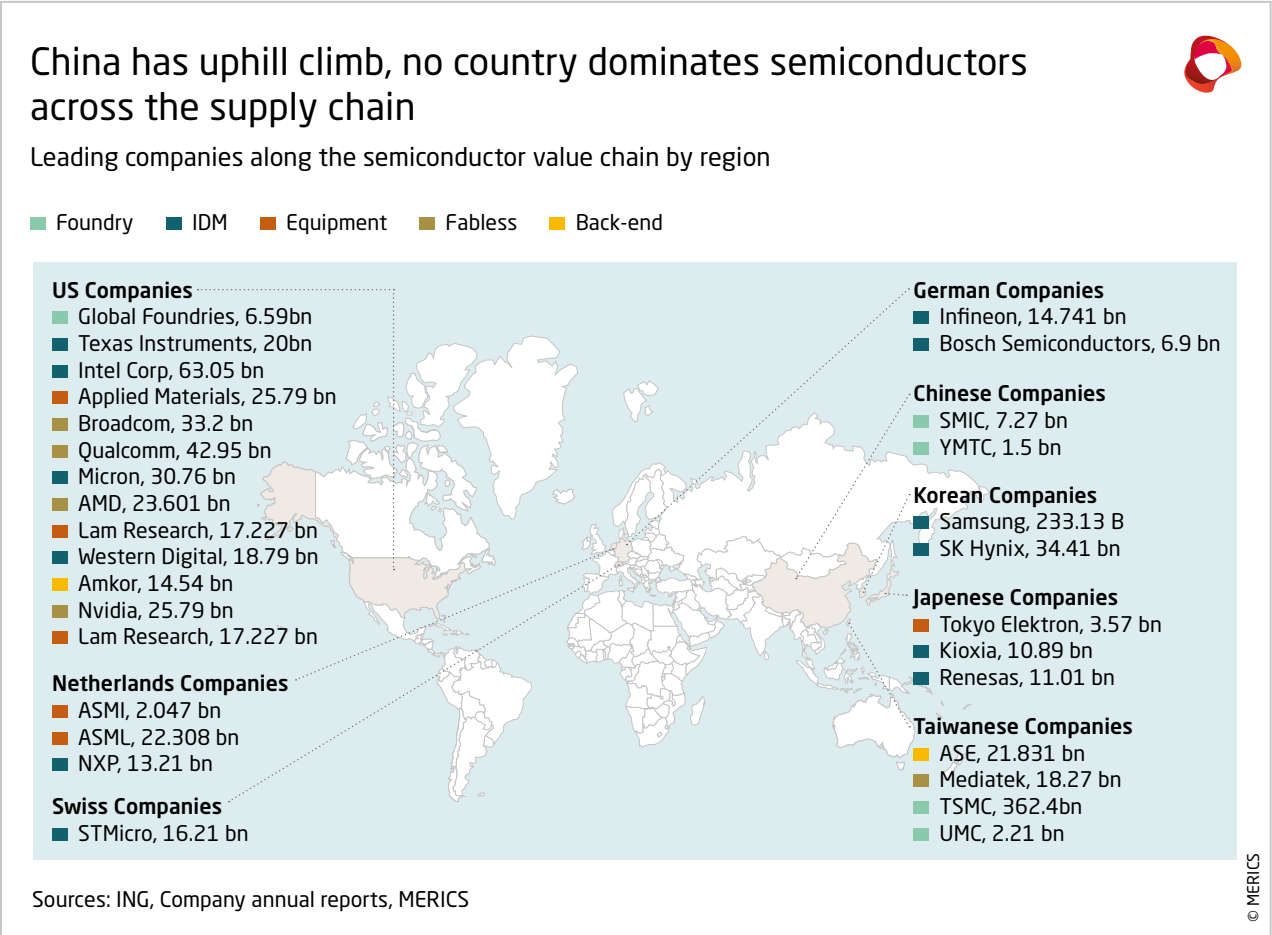
China's technological independence

STATUS QUO

China's policy aims for self-sufficiency by 2035. Although already less dependent on foreign technology than Germany, China's deficits are particularly high in strategic, high-tech sectors. In 2017, the government identified 35 chokepoints, including advanced lithography machines for making microchips. Beijing is willing to incur significant costs to nationalize technology. It pushes China's homegrown Kylin computer operating system, wants to replace all government computers with domestically manufactured ones, and has huge state guidance funds for chips and other key tech. However, this government-led effort is not without problems. Chip sector guidance funds were the subject of a major corruption investigation in August 2022. China's state-driven approach has produced high-profile successes, but it has been rife with abuses and has fallen far short of the government's stated goals.

DRIVERS AND DYNAMICS

Technological independence has taken on a new urgency for China since the West showed unity in imposing sanctions on Russia. Beijing is trying to break the 35 chokepoints, and also to establish its own chokepoints to create a system of mutually assured destruction.



The United States and EU are developing new tools to limit tech transfer to China, concerned with items such as cutting-edge semiconductors and machinery that would allow China to advance its own semiconductor industry. In October 2022, the United States unilaterally imposed export restrictions on a wide range of products across the chip supply chain. After hesitating, both Japan and the Netherlands, which are the other big players in semiconductor manufacturing equipment, have implemented similar restrictions. These target high-tech semiconductors and the machinery to make them. China's self-sufficiency drive seems sure to accelerate, especially as fresh rounds of export restrictions are likely on quantum, green technology and biotech.

FACTOR ASSUMPTIONS

What might China's technological independence look like in 2027?



FUTURE PROJECTION	DESCRIPTION	SCENARIO
Two standards, dual circulation	The status-quo assumption: China is still behind in key high-tech industries but pursues ambitious plans to catch up. Beijing leverages China's huge domestic market to insulate it from outside competition in key areas for economic security. Domestic companies are protected to have time to develop their own technology. Yet, many of these companies are exporters, and part of global value chains.	■ Shaky China
China on track to economic independence	China seems on track for a high degree of economic security, via a mix of tech sovereignty and tech leadership in key areas. Beijing leverages its huge capital investment in innovation to stifle economic chokepoints or sidestep them, avoiding dependence on other countries. A precondition for this scenario is that foreign technology providers cooperate largely on China's terms.	■ Successful China
China cut off	China is cut off from global technology and innovation ecosystems. The US and allies ensure China cannot acquire the materials and talent for tech sovereignty. China's progress is halted in most technology areas, including semiconductors.	■ Restrained China ■ Confrontational China
Back to global unity	China and the US both see the value of a globalized supply chain for high tech. They cooperate for mutual gain, rather than compete. China's quest for independence becomes less acute and Western countries worry less about providing cutting-edge technology. This shift could be triggered by an economic crisis, or a huge environmental or health emergency that forces rapid cooperation.	■ Reformist China

Note: Other assumptions considered theoretically possible, but not included in the final scenarios: Mini-lateralism, where China is able to leverage its dominant market position, use "Space Station Diplomacy" and other high-tech diplomatic efforts to convince countries to join issue-specific "coalitions of the willing": the market share captured, capital and talent available are sufficient for China's continued progress in tech.

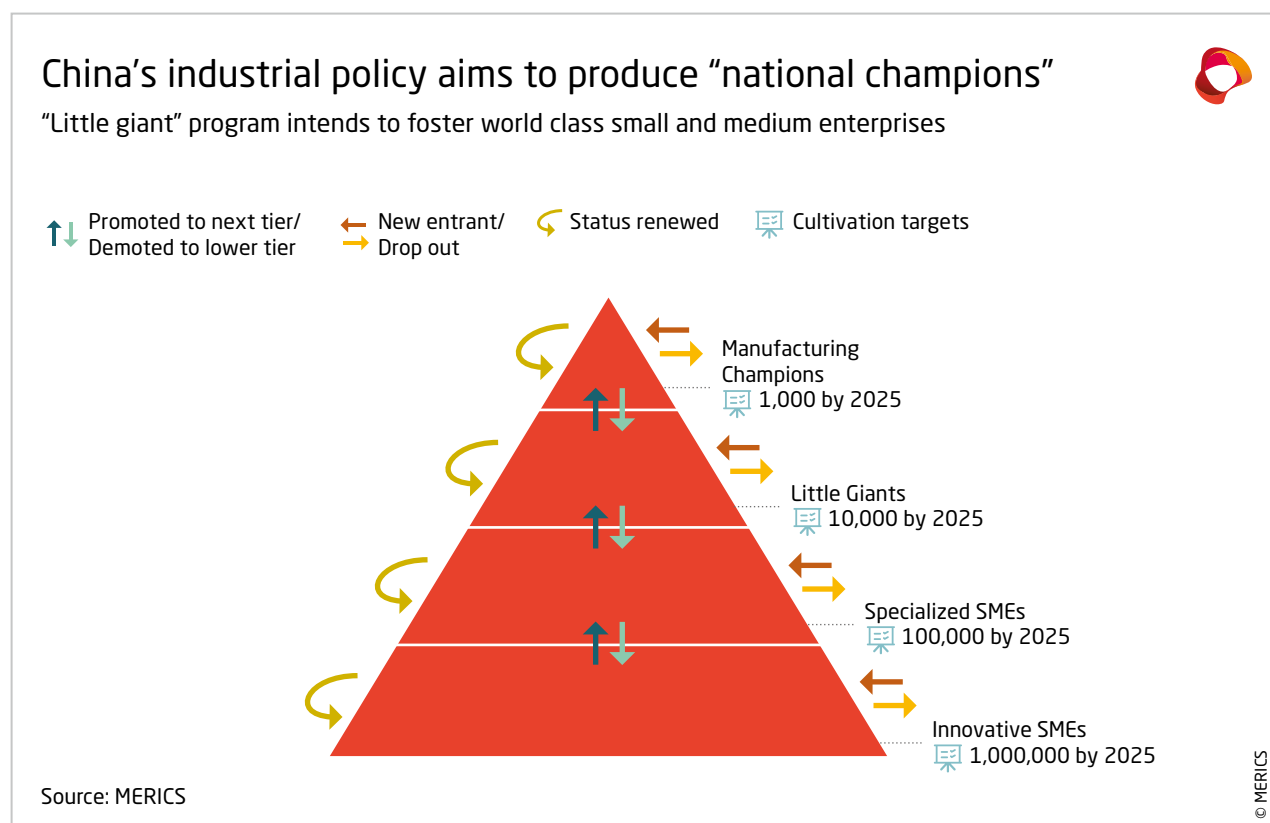
China's innovation capacity

STATUS QUO

China is leading the world in quality academic papers and patents, and has tech successes in high-speed rail, ICT (5G), digital tech (AI, TikTok), green tech (PV, NEVs, batteries, UHV), quantum and (some) biotech. Most successes are in applied rather than basic research. China is investing hugely in its innovation capacity, taking a state-driven approach. This progress is costly and by some accounts uneconomic; productivity may actually be declining.

DRIVERS AND DYNAMICS

China's government is once again politicizing all walks of life, including innovation. All inventions are nationalized, and firms are supposed to focus on dual-purpose technology and on releasing the economic chokepoints Beijing has identified. China has reorganized its innovation system across an innovation chain, seeking to take breakthroughs from basic research to commercialization in a shorter time. China's past innovation growth rested heavily on access to foreign talent, know-how and investment, all of which have been made more difficult since the zero-Covid policy accelerated China's decoupling from the world. Since China reopened in late 2022, it is unclear how far foreign involvement is welcome in China's innovation and how far foreigners are willing to keep contributing to it, given the conversations around research security and China as a systemic competitor in Europe, and even more so the United States.



FACTOR ASSUMPTIONS

What might China's innovation landscape look like in 2027?



FUTURE PROJECTION	DESCRIPTION	SCENARIO
Progress continues, but slows	China's progress continues in some areas of applied research, though it is still uncompetitive in basic research. It is able to innovate in fields with hefty state investment where innovators are shielded from foreign competitors; this is not enough to sustain China's economy. China gains relative influence as an innovation partner for the Global South and in standard-setting.	<div></div> Shaky China <div></div> Reformist China
Innovative breakthroughs	This is China's best-case assumption: it gains a global technological edge by making breakthroughs in basic research, and finds successful industrial applications for the innovations. This creates growth. Productivity increases. A fundamental upgrade of China's innovation capacities would take longer than five years, but a few high-profile advances could generate perceptions of China as a new innovation powerhouse, supporting its drive to set global standards.	<div></div> Successful China
Stalled innovation capacity	China's innovation capacity stalls. It is hurt by more ideological leadership, global containment and becoming unable to use catch-up innovation. As a result, its economy may get stuck in the 'middle income trap'.	<div></div> Restrained China
Bifurcation: two separate innovation ecosystems	China builds an innovation ecosystem separate from the West. Beijing's science diplomacy convinces some other dissatisfied countries to join, though the system is less efficient than the global science and innovation system.	<div></div> Confrontational China

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China as a digital actor

STATUS QUO

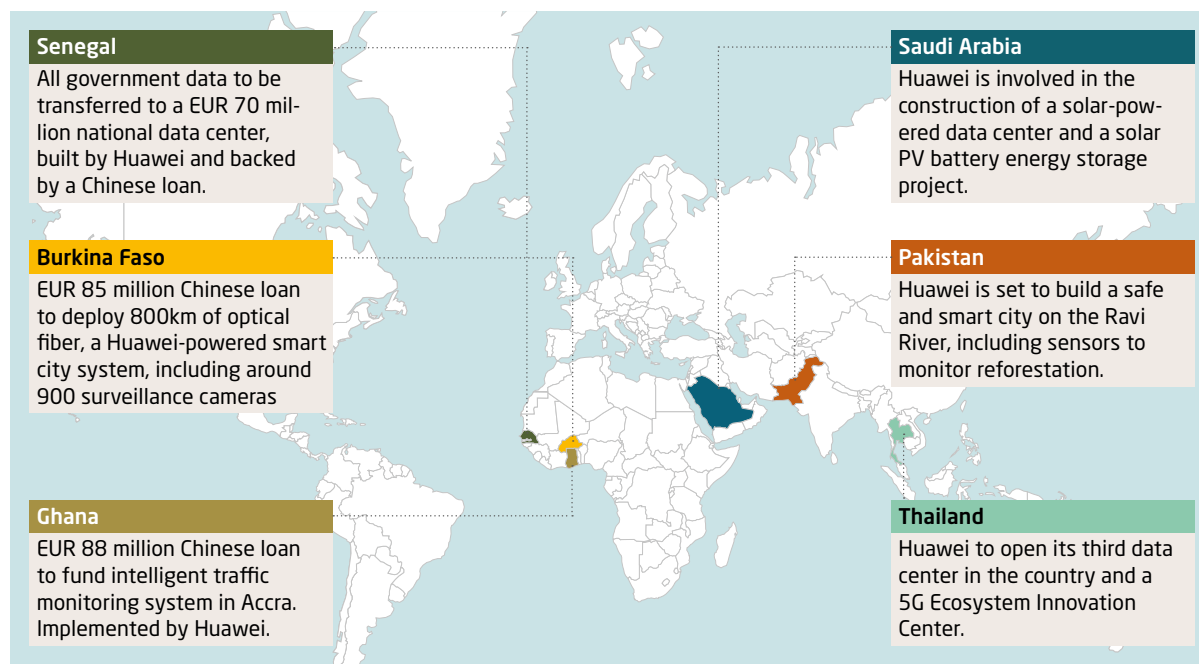
China has world leading technology giants in Internet, ICT equipment and AI, such as Huawei and Bytedance. Chinese digital infrastructure and products span the globe, with a strong footprint in developing and emerging economies. Only advanced economies have put restrictions on China's digital infrastructure and products, and these are narrow in scope. China is developing its cyber and digital governance model. The model's top priority is the protection of regime security from threats emanating from online information flows. China is engaged in pro-active cyber diplomacy, and sees the Fourth Industrial Revolution as an opportunity to claim global leadership and project power. In international cyber forums, China is seeking to position itself as a champion of developing countries and for nation states to have a greater role in standard-setting.

DRIVERS AND DYNAMICS

Beijing seeks advantages from tech firms' global expansion, creating geopolitical, security and human rights risks. Major Chinese ICT firms such as Huawei export their technology, often funded by the Chinese government. In doing so, they push for new protocols that are designed for censorship and application-specific networking, i.e. allowing content discrimination. China is active in standard-setting, especially in ICT, where it pushes for a greater role for nations in standard-setting, going against the multi-stakeholder model of internet governance. China and the EU are increasingly competing for their vision of digital development in the world, with China's Digital Silk Road and the EU's Global Gateway. China's vision of the Internet is increasingly at odds with the Western vision of the Internet, with application-specific networking and content discrimination baked in. With China's export of surveillance technology and Internet technology, China's vision is becoming embedded in the backbone of the Internet, especially in the Global South.

China aspires to be a global provider of digital solutions

Selected examples for public services and utilities



Note: Selection of announced or completed projects implemented and/or funded by Chinese actors, 2020-2021
Source: MERICS

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FACTOR ASSUMPTIONS

What might China's role as a digital actor look like in 2027?



FUTURE PROJECTION	DESCRIPTION	SCENARIO
Splinternet	Instead of one global internet, a number of smaller “splinternets” emerge. China becomes tech leader in surveillance. Parallel technical standards emerge in different regions, and interoperability and data flows are only supported within trade alliances.	<div>■ Shaky China</div> <div>■ Reformist China</div>
China sets global standards	China increasingly sets global standards, aided by support from developing countries and less resistance from developed countries.	<div>■ Successful China</div>
Chinanet	Chinese standards are not accepted globally, leading to a bifurcation. The Chinese internet becomes largely isolated. Chinese tech firms develop their own solutions to comply with domestic regulation.	<div>■ Restrained China</div> <div>■ Confrontational China</div>

Note: Other assumptions considered as theoretically possible, but not included in the final scenarios as unlikely, especially within five years: Chinese high-tech firms adopt a major outward investment strategy to invest in Western companies, with Chinese state support; or a major global disruption of the internet prompts all governments to join forces on cybersecurity and vulnerability.

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China's political system

STATUS QUO

When Xi Jinping clinched an unprecedented third term in power at the 20th Party Congress in October 2022, he and his allies gained ideological hegemony. No other factions are represented in the seven man top leadership group (the Politburo Standing Committee). Political activity is driven by ideology, by party loyalty and personal loyalties. In society at large, “rule by law” codifies party norms and integrates CCP rule into economic and institutional life. Xi appears to have a mandate and a power base to push through issues that were previously stalled due to politics. The risk of undivided power is that problematic norms and policies will not easily be challenged.

A key feature of Xi's system of political management is centralized policy steering driven by incentives and supervision. It fosters campaign-style policy implementation (which can be erratic and inefficient), while diminishing local policy innovation and flexibility. Xi's political victory in 2022 left open the possibility that he might rule for five more years after 2027.

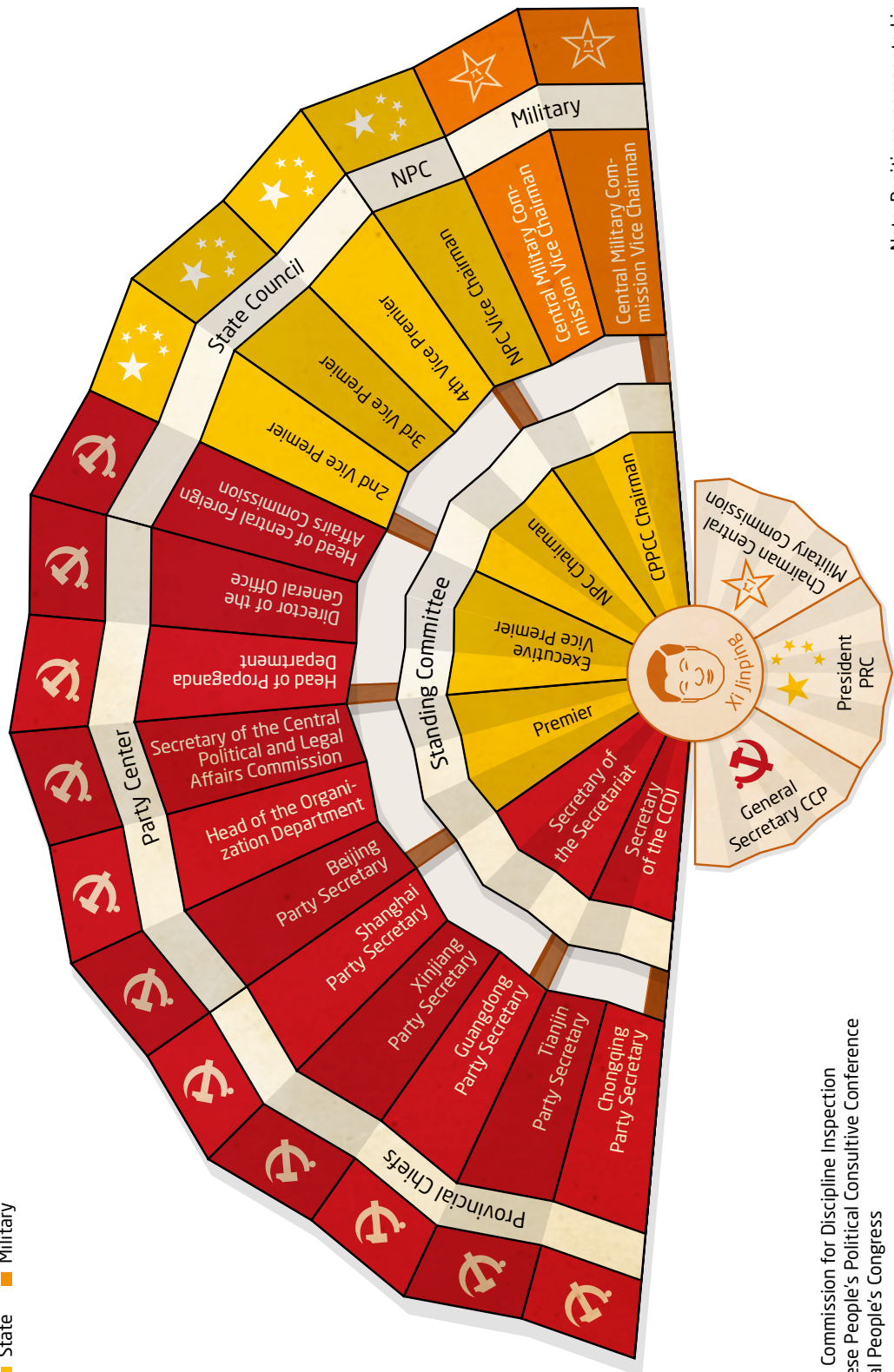
DRIVERS AND DYNAMICS

As economic opportunities shrink and “patriotic duties” become more demanding, the foundations of decades-long “elite embeddedness” and loyalty to the system are shifting. Institutionalization of discipline and supervision measures ensure compliance with the center. As the party state expands its reach throughout society (the private sector, media, education, and civil society), there seems to be less room for alternative positions and course corrections.

Fan of power

Selected examples for public services and utilities

■ Party ■ State ■ Military



CCDI: Central Commission for Discipline Inspection
 CPPCC: Chinese People's Political Consultative Conference
 NPC: National People's Congress

Source: MERICS

Note: Positions represented in Politburo of 20th Central Committee in 2023

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FACTOR ASSUMPTIONS

What might China's political system look like in 2027?



FUTURE PROJECTION	DESCRIPTION	SCENARIO
Leadership transition struggles	The status quo assumption: Xi pursues the political agenda he set out at the 20th Party Congress, but with limited success on structural challenges. Even if he seeks to extend his rule beyond 2027 when he will be 74-years old (likely, as long as he is in good health), his rule is inevitably time-limited, so succession issues will arise. Xi might lay out his own succession plan or party factions and political coalitions may maneuver for influence. A power struggle would make for inefficient governance as factions push disagreements over responses to structural challenges, domestic and external risks. Similar developments may also play out if Xi leaves the political stage in 2027.	■ Shaky China
Greater centralization of leadership	If Xi manages to use his mandate to push through difficult reforms in line with the agenda he set out at the 20th Party Congress, he may have sufficient power to further centralize leadership at the 21st Party Congress in 2027. This could mean smaller party committees, fewer ministries or more parallel structures that hold the de facto power (e.g. commissions), implying more power for less people, and functional centralization through better monitoring. A major external conflict or war could also increase the party core's dominance, meaning more and faster resource mobilization in priority areas as defined by the party leadership (which could be considered good or bad). Theoretically, these trends could still apply even if Xi were ousted by a successor who favors the same political structures.	■ Successful China ■ Confrontational China
Collective leadership	Xi has discarded the collective leadership model of the post-Mao era. A return to a more collective kind of CCP rule could be triggered by external events (such as war or extreme hostility that shakes up internal alliances) or if Xi's model fails to deliver on its promises and on the CCP's priorities of stability and control. Whatever the trigger, a return to collective leadership is hard to imagine while Xi is in charge. It would need shifts in ideology and a major reshuffle at the top of the party.	■ Restrained China ■ Reformist China

Note: Projections about the future of China's political system are among the most important factors in this scenario exercise. The three projections above do not include all options that are theoretically possible, merely what seems feasible within five years. Other more extreme assumptions discussed include the overthrow of CCP rule by a democratic revolution; a military coup leading to a military national security state; or a return to constitutionalism.

China's stability and social policy

STATUS QUO

Government reforms blend better public services with even more intense surveillance to contain discontent. The pandemic has driven a major build-up of surveillance since 2020. However, Covid controls fomented significant social tensions over lost income and government overreach, expressed in a wave of protests in late 2022. Even after many Covid controls such as the “health code” were dropped, the government’s surveillance toolbox remains in place, ready for use when needed.

China struggles with a multitude of social problems that will continue to create tensions in coming years, including a rapidly aging society, income inequality, a slowing economy and massive youth unemployment. With its “Common Prosperity” concept, the CCP has signaled that it sees the challenges, but the current political agenda fails to address their root causes.

DRIVERS AND DYNAMICS

Slower economic growth means greater competition for resources between the social policy agenda and China’s security apparatus. Pressures on social systems (healthcare, social security) are rising fast, driven by demographic aging, which appears more rapid than expected. Inequality and socio-economic issues become more pronounced and create risks to the CCP’s performance-based legitimacy.

FACTOR ASSUMPTIONS

What might China's stability and social policy look like in 2027?



FUTURE PROJECTION	DESCRIPTION	SCENARIO
Stability through surveillance	The status quo assumption: The CCP blends new social policies that provide better public services with effective surveillance to contain discontent. This mix is “good enough” to maintain stability.	<ul style="list-style-type: none"> Shaky China Successful China Reformist China
Repression, but passive resistance	The CCP leadership fails to manage major social problems such as youth unemployment. To maintain stability, surveillance is increasingly coupled with direct social repression. This leads to massive frustration and, at the least, passive resistance by individuals.	<ul style="list-style-type: none"> Restrained China Confrontational China

Note: Other assumptions considered as theoretically possible, but not included in the final scenarios as unlikely within five years, included impressive steps towards a functioning welfare state that deals well with inequalities, or large-scale coordinated resistance and public uprisings.

Comprehensive national security checklist

Imagine you are a Chinese cadre or official. Your task is to comprehensively safeguard national security. Consider each type of security and apply them in your area of competence.



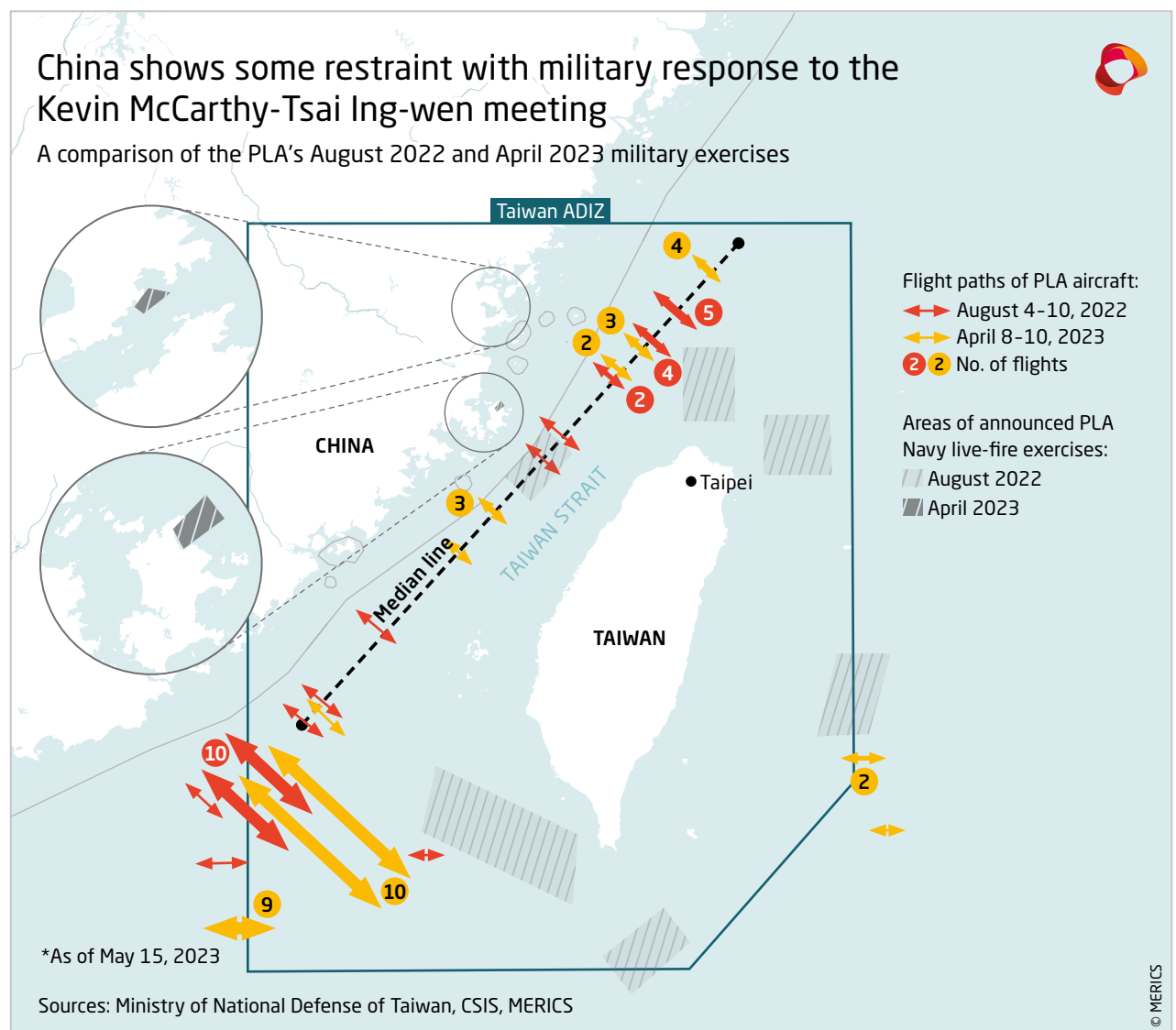
Source: MERICS

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Cross-strait relations

STATUS QUO

Cross-Strait tensions are at an all-time high, as economic coercion and airspace incursions have become Beijing's norm towards its "Taiwan problem". Beijing is pushing to remove well-established constraints, such as the median line midway across the Strait. The PRC and Taiwan are de facto in a grey-zone conflict. PRC pressure on Taiwan is matched by growing support from the United States and its allies, who seek to uphold the status quo and push back China's ambitions. Among Western politicians it is now normal to draw parallels between Russia's war in Ukraine and the PRC's threats to Taiwan as an attack on the global order that must be prevented. In its August 2022 White Paper, called "The Taiwan Question and China's Reunification in the New Era", the CPP reiterated peaceful reunification was the "first choice" but said it did not rule out using force. Beijing's vision of how much autonomy Taiwan can expect post-reunification seems to be "Hong Kong 2.0", meaning strong interference in Taiwan's affairs rather than the version of "one country, two systems" that Hong Kong lived under until 2020.









DRIVERS AND DYNAMICS

China and the United States agree on the need for guardrails to keep tensions over Taiwan from spiraling out of control. However, tensions have escalated to the point that mistakes or accidents could have dramatic effects. Taiwan’s 2024 presidential elections seem certain to be accompanied by escalating friction, especially if voters choose the Democratic Progressive Party (DPP). Beijing calls the DPP secessionist and has refused to engage with its leaders. Taiwanese public opinion is increasingly critical towards Beijing, with a majority of over 60 percent surveyed identifying as solely Taiwanese, one third as Taiwanese Chinese and only a fraction as solely Chinese. For comparison, in 2007, identification as solely Taiwanese or as Taiwanese Chinese both stood at a level of around 44 percent.


FACTOR ASSUMPTIONS

What might cross-strait relations look like in 2027?



FUTURE PROJECTION	DESCRIPTION	SCENARIO
Beijing increases pressure on Taiwan	The status quo assumption: Beijing uses its political, military and economic muscle to push other countries in the region to accept its ambitions for “complete reunification”. At the same time, the US builds its own coalition to push back (e.g., with Japan, Australia) against Beijing.	 Shaky China
Escalation below the conflict threshold	Beijing successfully keeps pushing at red lines, perhaps taking control of some islands in the Taiwan Strait. Beijing also expands its hybrid warfare. It looks increasingly confident that it will eventually tilt the military balance in the Taiwan Strait but continues to bide its time.	 Successful China
A more independent Taiwan	A weakened China (because of an internal crisis or effective US pressure) could bring Taiwan a wider degree of independence (e.g., by being allowed to join international institutions).	 Restrained China
Cross-Strait talks	A change of government in Taiwan, coupled with less aggressive language from Beijing, could lead to renewed cross-Strait talks, as happened under previous Kuomintang (KMT) governments in Taiwan. Beijing would spin such talks as steps towards peaceful reunification.	 Reformist China
Military conflict	A military conflict over Taiwan seems imminent. In this scenario exercise, we did not consider different war scenarios. We stopped at the point where military conflict looks likely and China, Taiwan and other powers are preparing for severe escalation.	 Confrontational China

Note: Other assumptions considered as theoretically possible but not included in the final scenarios were a non-military reunification where China regains Taiwan peacefully, or full-blown Sino-US war over Taiwan.



Energy system and supply

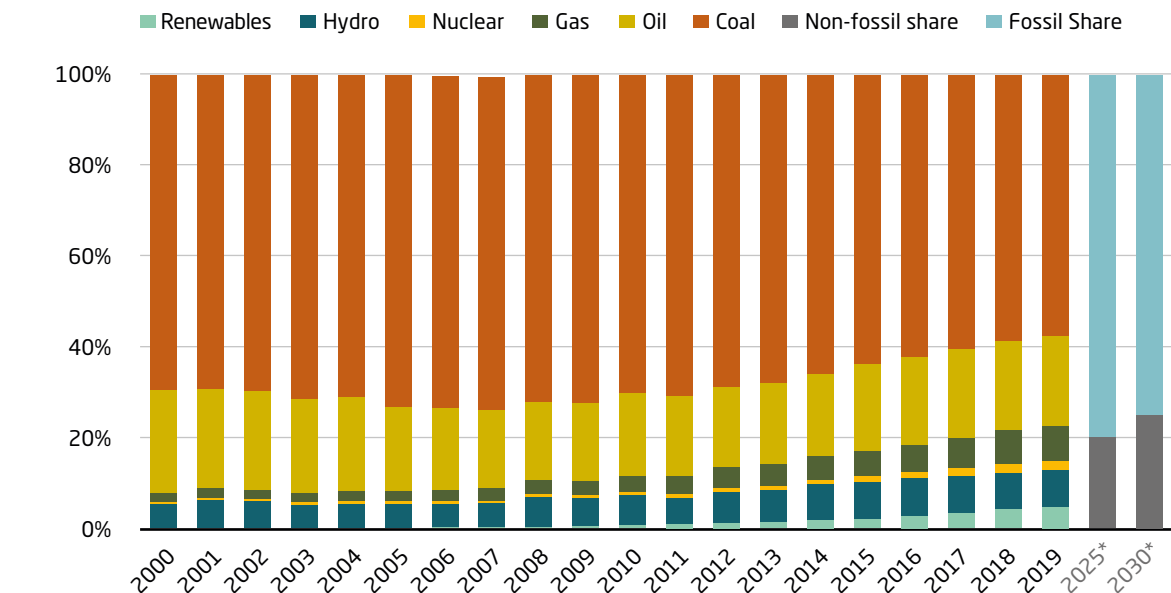
STATUS QUO

China, like the rest of the world, has deep concerns about energy security. Externally, the shock to global energy markets from Russia's invasion of Ukraine continues to roil commodity markets. At home, the heat waves and droughts affecting China's key water sources are taking out normally predictable hydropower sources, which account for roughly 16 percent of electricity production. China has resources to become self-sufficient in domestic thermal coal (still around 60 percent of electricity production), hydropower and renewable sources. But this will take years – especially in renewables - because capacities need to be increased. China is heavily reliant on imports of natural gas and crude oil – just under half of China's 2021 natural gas was imported, while reliance on imported crude is even higher, at 72 percent of total consumption in 2021. Beijing has directed diplomatic efforts to establish energy ties with countries in the neighborhood, especially with Russia.

The 14th Five-Year Plan (2021-2025) lays out ambitious plans to drive decarbonization and indigenous tech innovation. China is striving for global leadership in green technologies and sustainable solutions, where it is building on past successes (e.g., in wind, solar and e-mobility).

China's energy mix remains predominantly coal driven

Total energy supply by source in Terajoules (TJ)



*Plan

Source: IEA

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DRIVERS AND DYNAMICS

In October 2021, Xi himself called for greater efforts to develop energy self-reliance, particularly in the oil and gas industry. As he put it, “The rice-bowl of energy must be in our own hands”. Since then, China’s three main oil and gas champions have drastically increased their capital investment in projects at home and abroad. China is seen as the main beneficiary of Russia’s declining exports to European countries and is pushing Moscow to build more pipelines to China.

Beijing has put a strategic bet on reaching a sustainable future through technological breakthroughs that are state-guided and funded. It seeks a green transformation at home and global tech leadership across the board, from renewables to environmental protection equipment. Cooperation on climate change and green technologies remains one of the few areas where partnerships between China and Western countries continue to thrive. Yet, competition for green tech and manufacturing processes is intense.

FACTOR ASSUMPTIONS

What might China’s energy system and supply look like in 2027?



FUTURE PROJECTION	DESCRIPTION	SCENARIO
Much coal, little renewables	This is the status quo assumption: China remains very dependent on coal and on imports of oil and gas. Good relations between Beijing and Moscow largely secure China’s supplies. China makes progress on renewables, but resource and industrial capacities are too constrained for the energy transition to advance substantially.	<ul style="list-style-type: none"> Shaky China Reformist China
Breakthrough in renewables	China successfully makes a major push towards green energy, with breakthroughs in new technologies, production processes and energy system integration. Driven by its big market and massive government funding, China manages to become the dominant global provider of green tech and new energy solutions. China continues to need fossil fuels because of limited or denied access to critical raw materials (CRM) and it gets fossil fuels from Russia and other oil and gas exporters.	<ul style="list-style-type: none"> Successful China
Small insecurities and disruptions	China’s energy system suffers from regular disruptions, e.g., regional black-outs. China has difficulties securing fossil fuel supplies, e.g. because of diplomatic problems with Russia or because of extreme weather events.	<ul style="list-style-type: none"> Restrained China Confrontational China

Note: Other assumptions considered in the scenario process as theoretically possible wild cards, but excluded from the final scenarios: A total energy supply collapse, e.g. triggered by a complete halt in the supply from Russia.

Food and water systems and supply

STATUS QUO

Food and water security are politically sensitive issues in China. Beijing has a long-standing target of 95 percent national self-sufficiency in key grain production, and needs few imports for food security. Supply is achieved through a mix of protectionism and stabilizing factors. Resilience is maintained by massive state-run grain reserves. The size of China's grain reserves is a state secret, but 2022 estimates put them at roughly 69 percent of total global reserves of corn; 60 percent of rice; and 51 percent of wheat.

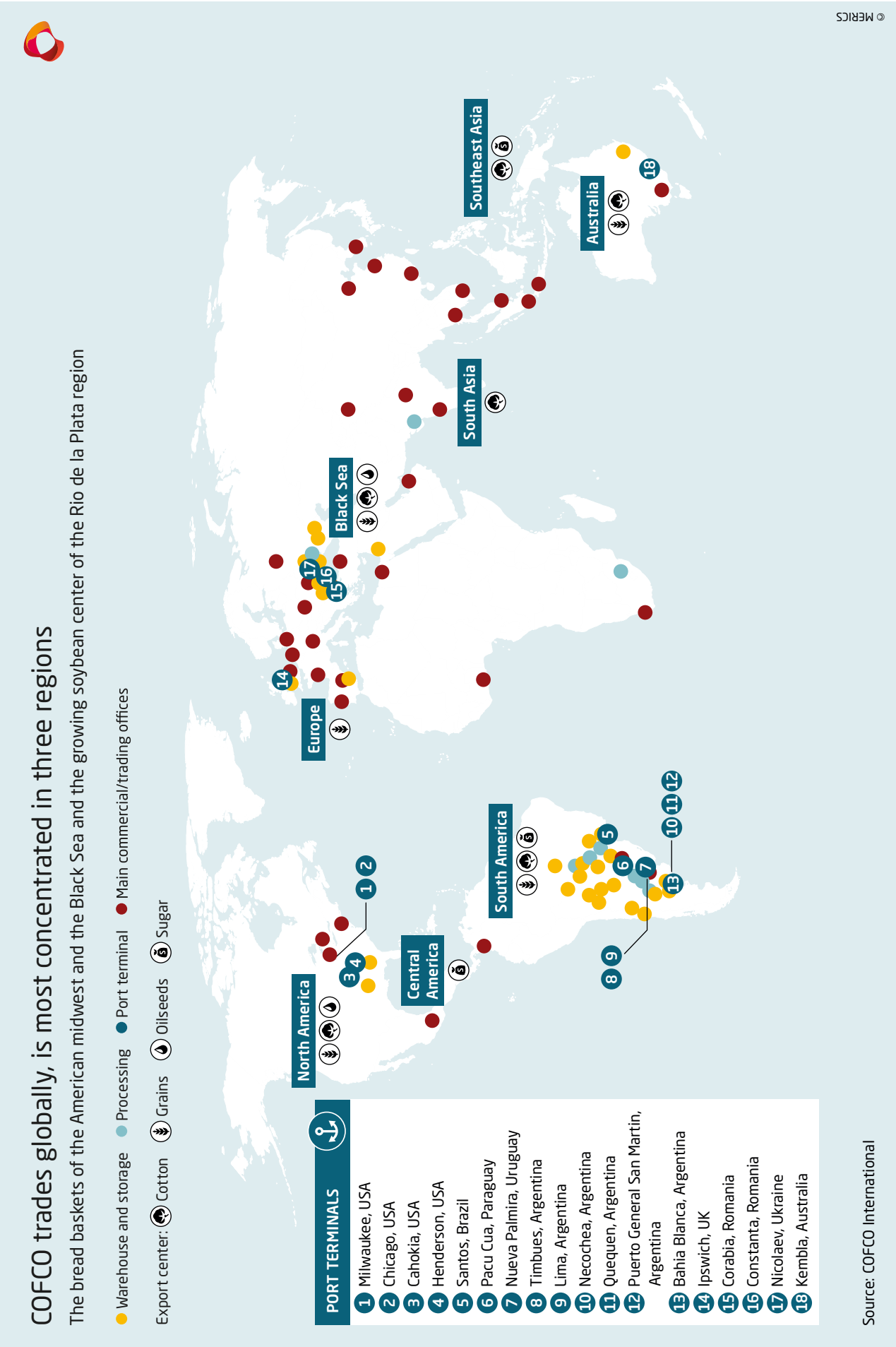
However, China does have impending risks to its domestic food security. Soil exhaustion, pollution, and rising problems with fresh water resources had reduced total arable land to 1.28 million square kilometers by late 2019, nearly 6 percent less than in 2009. Meanwhile, the Chinese Academy of Social Sciences (CASS) has estimated that urbanization and an ageing rural workforce could bring a grain supply gap of about 130 million tons by the end of 2025 (SCMP). Beijing may well decide that it must continue expanding imports and reserves for China's own future food security, even at the expense of global food supplies and prices in a time of crisis. This could hurt China's reputation in developing countries and tarnish its self-image as a generous contributor to South-South cooperation.

China also faces severe water problems. It contains less than 6 percent of the world's water resources, and they are distributed unevenly across China. Water-abundant southern China is prone to floods, while the north is arid and increasingly suffers water shortages.

DRIVERS AND DYNAMICS

China could play a significant role in mitigating the risk of a global food crisis with its purchasing decisions and use of its grain reserves. Beijing could help to offset higher food prices in the developing world by expanding its donations to the World Food Programme (WFP) and other food aid schemes. Such actions would have a financial cost but would not damage China's own food security position. However, Beijing is likely to be cautious about using its reserves to stabilize global food prices due to the sensitivities surrounding domestic food security. The 1959-61 Great Famine remains in living memory.

In 2022, the National Development and Reform Commission and the Ministry of Water Resources released the first five-year plan for water security in order to strengthen China's national water security capability by 2025.



FACTOR ASSUMPTIONS

What might China's food and water system and supply look like in 2027?



FUTURE PROJECTION	DESCRIPTION	SCENARIO
Food and water supply secured regardless of cost	China secures food and water resources for its own population at considerable political cost, e.g., excessive stockpiling; or controversies over control of farmland and China's agricultural imports from more needy countries.	■ Shaky China ■ Confrontational China
Supply secured without controversy	China manages to secure food and water resources without much political controversy.	■ Reformist China
Partial cooperation	China cooperates with other countries on critical issues, e.g. with India on water	■ Restrained China
"Feed your friends"	From a position of relative power, China acts as a provider of food resources for political allies.	■ Successful China

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