

It is becoming clear that this campaign is unlike anything seen under Presidents Jiang Zemin and Hu Jintao. Both carried out anti-corruption drives during their first year in office and periodically throughout their tenures as a means to strengthen their position within the Party and bureaucracy and to remind the public, however impotently, that Beijing still cared about its well being. But that was housekeeping. This appears to be different: longer, stronger, more comprehensive and more effective.

With this in mind, we ask: What is the fundamental purpose of Xi's anti-corruption campaign? An attempt to answer this question will not tell us China's political future, but it will tell us something about Xi's strategy -- not only for consolidating his personal influence within the Party, government and military apparatuses, but also and more important, for managing the immense social, economic, political and international pressures that are likely to come to a head in China during his tenure. Getting to the heart of the anti-corruption campaign -- and therefore understanding its inner logic and direction -- provides insights on the organization and deployment of political power in China and how those things are changing as the Party attempts to remake itself into an entity capable of ushering China safely through the transformation and crises to come.

The Campaign Continues

The announcement July 29 of a formal investigation into retired Politburo Standing Committee member Zhou Yongkang marked something of an end to the first major phase of Xi's anti-corruption campaign. By all accounts, Zhou was one of the most powerful men in China throughout the 2000s. During his tenure on the Standing Committee, Zhou controlled the country's domestic security apparatus, a pillar of the Chinese government's power. Prior to that, he had served as Party secretary of Sichuan province, an important inland industrial center and breadbasket with historically strong regionalist tendencies. And before Sichuan, Zhou chaired state-owned China National Petroleum Corp., the country's most powerful energy firm and the direct descendent of the Ministry of Petroleum. Zhou was known to sit at the apex of at least these three power bases, and his influence likely extended deep into many more, making him not only a formidable power broker but also, at least in the case of his oil industry ties, a major potential obstacle to reform. Certainly, Zhou and his vast networks of influence and patronage were not the sole targets of the Xi administration's crackdown, but he and his associates, including former Chongqing Party Secretary Bo Xilai, widely seen as an early competitor of Xi, formed its central axis.

Now begins another phase. There are indications that it will center on the military. There are other signs that it will target Shanghai, the primary power base of Jiang Zemin and the locus of financial sector reform in China. Further neutralization of Zhou's allies in energy and public security will likely be necessary as the Xi administration seeks to accelerate market-oriented reforms in the oil and natural gas sectors and to reinforce its internal security footprint in peripheral regions like Xinjiang as well as the Han Core. But ultimately, it is unclear which individuals and networks will anchor the next phase. The possibilities are as numerous as the Xi administration's myriad near- and medium-term policy goals.

The question of who or what will be targeted next is subordinate to that of why. Not why, specifically, they will be targeted, but why the campaign must and will continue. This brings us back to our question regarding the fundamental purpose of the anti-corruption campaign. It may be impossible to divine, beyond mere speculation, its future on a tactical level -- that is, what will come in three, five or eight months' time. But the direction of the campaign so far, combined with other actions by Xi, such as the formation of a unified National Security Council chaired by Xi himself and his apparent wresting of the reins of economic and social reform from Premier Li Keqiang, suggest that some other and deeper shift is underway, one for which the anti-corruption campaign is at once a vehicle and a symptom. Stratfor believes this shift involves nothing less than an attempt to rework not only the way the Communist Party operates but also the foundations of its political legitimacy.

To understand why, we look first not at Xi and what he has done thus far but at China and what it will undergo over the next decade. This will give us a sense of the external constraints and pressures of which Xi's administration is no doubt aware and to which it has no option but to respond. These constraints and pressures, more than any other factor, will shape Xi's actions and the Communist Party's evolution in the years to come.

A World Constrained

Over the next decade, the defining constraints on China will emanate from within. They are fundamentally economic in nature, but they cannot be disassociated from politics and society.

China is in the midst of an economic transformation that is in many ways unprecedented. The core of this transformation is the shift from a growth model heavily reliant on low-cost, low value-added exports and state-led investment into construction to one grounded in a much greater dependence on high value-added industries, services and above all, domestic consumption. China is not the first country to attempt this. Others, including the United States, achieved it long ago. But China has unique constraints: its size, its political system and imperatives, and its profound regional geographic and social and economic imbalances. These constraints are exacerbated by a final and perhaps greatest limit: time. China is attempting to make this transition, one which took smaller and more geographically, socially and politically cohesive countries many decades to achieve, in less than 20 years.

The bulk of this work will take place over the next 10 years at most, and more likely sooner, not because the Xi administration wants it to, but because it must. The global financial crisis in 2007-08 brought China's decadeslong export boom cycle to a premature close. For the past six years, the Chinese government has kept the economy on life support in the form of massively expanded credit creation, government-directed investment into urban and transport infrastructure development and, most important, real estate construction. In the process, local governments, banks and businesses across China have amassed extraordinary levels of debt. Outstanding credit in China is now equivalent to 251 percent of the country's gross domestic product, up from 147 percent in 2008. Local governments alone owe more than \$3 trillion. It is unknown -- deliberately so, most

likely -- what portion of outstanding debts are nonperforming, but it is likely far higher than the official rate of 1 percent.

Despite claims that China's investment drive was and is irresponsible -- and certainly there are myriad anecdotal cases of gross misallocation of capital -- it nonetheless fulfills the essential role of jumpstarting the country's effort to "rebalance" to a new, more urban and more consumption-based economic model. But the problem, again, is time. China's real estate sector is slowing. Sales, home prices and market sentiment are falling, even in the face of continued expansion of the overall credit supply. The days of high growth in the housing construction sector are numbered and prices, along with overall activity, are on a downward trend -- one that can and will be hedged by continued high levels of investment and credit expansion, but not one that can be stopped for long. Real estate and related construction activity will remain the crucial component of China's economy for the foreseeable future, but they will no longer be the national economic growth engines they were between 2009 and 2011.

This means that in the next few years, China faces inexorable and potentially very rapid decline in the two sectors that have underpinned economic growth and social and political stability for the past two or more decades: exports and construction. And it does so in an environment of rapidly mounting local government and corporate debt, rising wages and input costs, rising cost of capital and falling return on investment (exacerbated by new environmental controls and efforts to combat corruption) and more. Add to these a surge in the number of workers entering the workforce and beginning to build careers between the late 2010s and early 2020s, the last of China's great population boom generations, and the contours emerge of an economic correction and employment crisis on a scale not seen in China since Deng came to power.

The solution, it would seem, lies in the Chinese urban consumer class. But here, once more, time is China's enemy. Chinese household consumption is extraordinarily weak. In 2013, it was equivalent to only 34 percent of gross domestic product, compared to 69-70 percent in the United States, 61 percent in Japan, 57 percent in Germany and 52 percent in South Korea. In fact, it has fallen by two percentage points since 2011, possibly on the back of the anti-corruption campaign, which has curbed spending by officials that appears to have been erroneously counted as private consumption. There is reason to believe that household consumption is somewhat stronger than the statistics let on, but it is not nearly strong enough to pick up the slack from China's depressed export sector and depressive construction industries. China's low rates of urbanization relative to advanced industrial economies underscore this fundamental incapacity.

Whatever the Chinese government's stated reform goals, it is very difficult to see how economic rebalancing toward a consumption- and services-based economy succeeds within the decade. It is very difficult to see how exports recover. And it is very difficult, but slightly less so, to see how the government maintains stable growth through continued investment into housing and infrastructure construction, especially as the real estate market inevitably cools. This leaves us with a central government that either accepts economic recession or persists in keeping the economy alive for the sake of

providing jobs but at risk of peril to its reform initiatives, banks and local governments. The latter is ugly and very likely untenable under the current political model, which for three decades has staked its claim to legitimacy in the promise of stable employment, growth and rising material prosperity. The former is absolutely untenable under the current political model.

The pressures stemming from China's economy -- and emanating upward through Chinese society and politics -- will remain paramount over the next 5-10 years. The above has described only a very small selection of the internal social and economic constraints facing China's government today. It completely neglects public anger over pollution, the myriad economic and industrial constraints posed by both pollution and pervasive low-level corruption, the impact of changes in Chinese labor flows and dynamics, rising education levels and much more. It completely neglects the ambivalence with which many ordinary Chinese regard the Communist Party government.

It also neglects external pressures and risks, whether economic or military. What would another global economic crisis and recession do to China's already hobbled export sector? What would a prolonged spike in oil prices -- the result, perhaps, of deepening crises in Russia or Iraq -- mean for Chinese industry and its change to China's growing army of car drivers? What impact will structural changes in the East Asian and world systems, such as Japan's attempt at a national economic and military revival, have on China's overseas economic and maritime interests, or on Chinese society's confidence in the strength of its military and government? The potential risks, many of them of moderate to high probability, are legion. It takes only one to materialize to dramatically reduce the likelihood that the Communist Party, as currently constituted, survives China's transformation.

The Old Model Breaks Down

Xi knows this. He and his advisers know China's virtually insurmountable challenges better than anyone. They know how little time China has, how fragile the Party's political legitimacy -- its claim to the Mandate of Heaven -- has become over the past three decades and how great the consequences of inaction will be. But they also know how much potentially greater are the consequences of failure. Knowing all these things, they are acting to reconstitute the Party one cautious step at a time.

The anti-corruption campaign is one of those steps. It serves many overlapping functions: to clear out potential opponents, ideological or otherwise; to consolidate executive power and reduce bureaucratic red tape so as to ease the implementation of reform; to remind the Chinese people that the Communist Party has their best interests at heart; and to make it easier to make tough decisions.

Underlying and encompassing these, we see the specter of something else. The consensus-based model of politics that Deng built in order to regularize decision-making and bolster political stability during times of high growth and that effectively guided China throughout the post-Deng era is breaking down. It can no longer hold in the face of China's transformation and the crises this will bring. Simply put, now that its post-1978

contract with Chinese society -- a social contract grounded in the exchange of growth for stability -- is up, the Party risks losing the public support and political legitimacy that this contract undergirded. A new and more adaptive but potentially much less stable model is being erected, or resurrected, from within the old. This model is grounded more firmly in the personality and prestige of the president and more capable, or so Chinese leaders seem to hope, of harnessing and managing the Chinese nation through what could well be a period of turmoil.

This does not necessarily mean a return to Imperial China, nor does it mean a return to the days and methods of the Great Helmsman, Mao. It doesn't even mean the new model will succeed, even remotely. What it means will be decided only by the specific interplay of structure and contingency in the unfolding of history. But it is this transformation that serves as the fundamental, if latent, purpose for Xi's anti-corruption campaign.