



Interview

Lifting the Shroud on China's Defense Spending Trends, Drivers, and Implications

Interview with Andrew S. Erickson and Adam P. Liff

May 16, 2013

Andrew S. Erickson (U.S. Naval War College) and Adam P. Liff (Princeton University) assess trends in China's defense spending within the wider context of China's military development and transparency, as well as its broader strategic and national interests.

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By Nathaniel Austin

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In March, the Chinese government announced another multibillion-dollar increase of its defense budget. In order to gain a more nuanced understanding of the latest budget's implications, NBR asked Andrew S. Erickson (U.S. Naval War College) and Adam P. Liff (Princeton University) to assess trends in China's defense spending within the wider context of China's military development and transparency, as well as its broader strategic and national interests. Erickson and Liff are the authors of "Demystifying China's Defense Spending: Less Mysterious in the Aggregate," to be published in a forthcoming issue of the China Quarterly.

In March, the Chinese government announced another multibillion-dollar increase of its defense budget.

Looking back over the last decade, what does the trend of increasing defense spending reveal about

China's interests and priorities? How does this trend support China's strategic aims?

China announced its latest official projected defense budget as 720.2 billion yuan (roughly \$114 billion), a 10.7% nominal increase over the previous year. This continues a trend of nominal double-digit spending increases since 1989 (2010 was the sole exception, likely due to a prioritization of funds to finance a major stimulus package in response to the global financial crisis). Although China's military development started from a relatively low base when large (real) budget increases began in the mid-1990s, over the past decade its defense spending has increased to such an extent that the funding stream of the People's Liberation Army (PLA) is now second in size only to that of the U.S. military—albeit several hundred billion dollars smaller.

Especially since the global financial crisis, the growth in China's military budget is the envy of the defense establishments of most advanced industrial states, whose budgets are either stagnating or declining in absolute terms. In 2012, according to the *Economist*, aggregate global military spending declined by 0.5% to \$1.75 trillion—the first decrease since 1998—and for the first time since 1991 the U.S. proportion of total global spending fell below 40%. This reduced U.S. share is not due to increases in Europe, where many Western and Central European states are also reducing military spending—in fact, 20 of 37 of these states have cut their defense budgets by 10% since the financial crisis. Rather, it is caused largely by surging defense spending in East Asia. And according to the International Institute for Strategic Studies (IISS) the increase in China's military budget accounted for more than 90% of the aggregate increase in region-wide defense spending in 2011–12. Even Japan's recently announced 0.8% defense-budget increase in 2013, which made global headlines, was most noteworthy not for its size—which was very modest, especially relative to China's 10.7% increase—but for the fact that this was the first increase to Japan's defense spending in eleven years. In contrast, during that same period China's nominal defense spending quadrupled. Consequently, according to the U.S. Department of Defense, China's official defense budget in 2012 (\$106.7 billion) dwarfed those of its biggest neighbors—Russia, Japan, and India (\$61.3 billion, \$58.0 billion, and \$45.5 billion, respectively), and was more than triple that of South Korea and an order of magnitude larger than that of Taiwan. In short, China's surging defense spending over the past decade contrasts starkly with that of the United States and many of its security allies and partners, for whom fiscal pressures—especially in the past four years—have kept purse strings relatively tight. It is this relative speed of China's defense spending that further exacerbates concerns about its rapid growth.

Nevertheless, China's civilian leaders clearly see military modernization as a priority that is secondary to overall economic development. Over the past two decades, China's defense budget increases have been roughly consistent with GDP growth and actually have been outpaced by the even more rapid increase of overall government expenditures. Keeping the Communist Party in power, ensuring national survival, and defending vital national interests are even more important to Chinese decision-makers than economic development per se, but at present it

appears that they judge that these core imperatives are achieved adequately at current levels of defense spending. A good indication of Beijing's priorities is evident in the fact that since 2010 official spending on public security has surpassed the official defense budget.

Over the past decade, China's official defense budget has ranged between 1.3% and 1.5% of GDP, and even high-end foreign estimates of China's total defense spending correspond to only 2%–3% of GDP. Thus, it seems abundantly clear that for a variety of reasons, not the least of which are lessons drawn from the Soviet Union's experience with over-prioritization of the military and strategic over-extension, China's leaders will limit defense spending increases to a rate roughly proportional to its economic growth. In short, barring a dramatic economic slowdown or crash, or problems in achieving the three core imperatives listed above, relatively rapid increases to China's defense spending appear to be affordable for the foreseeable future.

What factors are contributing to the rise in Chinese defense spending? How is China spending this money?

Contrary to conventional wisdom in some circles, the main factors driving increases in China's defense spending are no great secret and are acknowledged explicitly by Beijing. China wants to compensate for past austerity and neglect, and to modernize China's military so that it achieves capabilities commensurate with contemporary standards. While a detailed breakdown of China's military budget by service or within service is not available, a general understanding of the PLA's spending priorities and trends can be reached inductively by examining the hardware that has come into use since the late 1990s. This method suggests that Beijing has ramped up military spending to accelerate the PLA's modernization and personnel development in order to secure China's homeland and assert control over contested territorial and maritime claims. In addition, the PLA is undertaking "new historic missions" to safeguard its overseas interests and to improve its international image as a "responsible great power." As China's [2013 defense white paper](#) elaborates, important aspects of this include PLA participation in low-intensity "non-war military operations" such as humanitarian assistance/disaster relief, antipiracy operations, and noncombatant evacuation operations.

With regard to possible combat scenarios, the available evidence suggests that China's defense spending is focused on developing formidable military capabilities to ensure stability on its land and maritime boundaries and to resolve its numerous territorial and maritime disputes in its favor. Aside from borderland disputes with India and Bhutan, all China's outstanding island and maritime claims lie in the "near seas" (the Yellow, East, and South China seas). The question of Taiwan's status, while less volatile since the election of Ma Ying-jeou in 2008, remains foremost in importance. The PLA is developing weapons systems and ways to deploy and employ them that are designed to coerce the disputant, as well as any third-party, should it attempt to intervene in these sensitive disputes. China's goals in this regard are to convince its neighbors that it is in their interests to settle the disputes on terms favorable to Beijing and, toward that end, to deter third-party intervention.

At the same time, however, it also appears that a growing (but uncertain) percentage of the PLA's budget is being allocated toward developing power-projection platforms, such as aircraft carriers, and deploying destroyers and frigates on antipiracy and naval diplomacy missions, as well as toward increasing the ability to safeguard Chinese nationals and interests overseas—a key emphasis of Beijing's 2013 defense white paper. It is important to recognize that these capabilities are coming online gradually and are unlikely to pose a high-end threat to any capable adversary in the foreseeable future. In fact, even from Washington's perspective, China's increasing "far seas" capabilities are largely a positive development. They permit Beijing to provide public goods and help sustain the international system, such as is the case with the fourteen (and counting) task forces deployed operationally to participate in antipiracy in the Gulf of Aden since December 2008. The PLA's growing involvement in these non-war operations should not be written off as insignificant just because it does not involve high-intensity combat. This trend should also be understood as a significant bellwether of China's future military trajectory—just not the high-end part of it.

While investments in military modernization over the past decade mean that China is increasingly fielding formidable military capabilities in its immediate periphery, this is a far cry from developing a global force similar to that of the U.S. military, which is capable of high-intensity modern warfare anywhere in the world. Such missions will remain out of China's reach for many years. That said, capabilities in the cyber and, to some extent, space domains are important exceptions to these geographical limitations on China's power-projection capabilities.

As China places greater emphasis on the roles, missions, and capabilities of the PLA Navy (PLAN), PLA Air Force (PLAAF), and Second Artillery Force, will there be greater inter-service competition or rivalry over resources within China's traditionally ground force-dominated military?

Chinese civilian and military leaders frequently reference China's expanding "maritime rights and interests," precision-guided missiles, informationization and space, and the importance of air superiority, all of which suggest that a decrease in the relative clout of the ground forces is already underway. This trend, however, faces considerable resistance from within the PLA, where the ground forces have been dominant for more than 80 years. After all, the formal name of China's military is the People's Liberation Army. For various reasons—including history, culture, and organization—a rapid reorganization of the intra-PLA hierarchy is unlikely in the near future.

Nevertheless, as China's interests become more global, competition among the PLA's other three services and one branch will probably increase. This inter-service competition—a time-honored tradition in all militaries—is likely to deepen as each service or branch strives to develop capabilities in new domains and claims that its contribution is crucial to China's national interests. Given the PLAN's mostly external geopolitical orientation and operations, it seems best-positioned to capture an increasing percentage of the budget pie in an era of frequent calls from within and outside the Chinese leadership for China to become a global player, responsible stakeholder, and "maritime great power." Already, the 2013 defense white paper emphasizes that "China is a major maritime as well as land country" and is "intensifying blue water training." Transforming the PLAN from its current near seas-specific three-fleet

structure into a “two-ocean” navy (in the Pacific and Indian oceans) would undoubtedly require more and better vessels. Meanwhile, the PLAAF is striving to consolidate control over China’s burgeoning militarily relevant space assets, globe-spanning capabilities which are crucial for 21st-century warfare in any traditional domain—land, sea, or air. Finally, the Second Artillery Force also seeks a greater role in space to complement its highly-advanced nuclear and conventional ballistic missile forces.

A rising tide lifts all boats, and nascent inter-service rivalries within the PLA have been mitigated heretofore by a rapidly expanding defense budget that has allowed civilian and military leaders to avoid many of the difficult, zero-sum funding decisions required of their counterparts in countries with stagnant or declining budgets. Although continued growth in China’s defense spending is likely and an unforeseen deterioration in China’s security environment could of course trigger a rapid surge, the widely expected relative slowdown in the pace of China’s economic expansion, coupled with the worsening of other pressing domestic challenges, will probably cause a gradual reduction in the rate of defense spending increases over the next decade. Such a development, coupled with the diminishing returns of greater spending as the lowest-hanging fruits in the military modernization process are plucked, would force leaders to increasingly make tough choices about which projects to prioritize, which to limit, and which to avoid entirely—an outcome likely to exacerbate inter-service competition for resources.

Additionally, intra-service rivalries may become an increasingly important issue within the PLA if defense spending growth decelerates or stagnates. For example, one of the authors has heard from an informed Chinese source that there is intense opposition to China’s nascent but already expensive aircraft carrier program from some factions within the PLAN, including the submarine service, which view the program as funneling huge resources away from more urgent strategic priorities.

Western governments have often criticized the lack of transparency in China’s military budget. Has Beijing made progress in addressing these concerns?

China has made moderate progress in improving overall military transparency over the past two decades. Unfortunately, much of this progress is visible only to those observers able to exploit the growing open-source (but mostly Chinese-language) literature available online and from Chinese publishers. And despite this progress, there is no question that China still has a long way to go to meet the military transparency standards of other countries at a similar level of military development.

When it comes to the specific matter of China’s defense budget transparency, there are basically two related but analytically distinct issues. First, there is the issue of how accurately the officially announced defense budget figure captures China’s total spending on its military. Second, there is the issue of how much information the Chinese government reveals about how these funds are spent—i.e., how the budget is allocated within the PLA.

With regard to the first issue, it is important to start with a caveat. While China's official defense budget figure does not account for all of its defense-related spending, the same is true (albeit sometimes to a lesser degree) for all nations. There is no universal standard for military budget categorization or transparency. Indeed, while China's transparency concerning all military spending issues is far below the standards of advanced Western democracies, there are many developing nations—including several democracies that are U.S. allies and partners—whose level of military transparency also comes up short. That said, because of the size of its budget and its rapidly advancing capabilities, China is already in a very different category from the vast majority of nations—both developing and developed—and a growing number of observers reasonably contend that it therefore has a responsibility to be more transparent in order to reduce the widespread concerns and uncertainties surrounding its rapid rise.

Nevertheless, over the past two decades the general trend is that an increasing proportion of China's total defense-related spending is "on the books" and captured by the officially announced budget figure. This is reflected in the amount of daylight between the Department of Defense's estimate of China's "total military-related spending" and China's official defense budget. The former has decreased from roughly 3.25 times China's officially announced figure in 2002 to 1.13–1.70 times the official figure in 2011 (but increased to 1.26–2.01 times in 2012).

A similar trend is manifest in estimates by the London-based International Institute for Strategic Studies of China's actual spending, which fell from 1.72 times the official figure in 2006 to 1.41 times the official figure in 2012. Together with the declining RMB-to-dollar exchange rate since 2005, these estimates suggest that the PLA's actual effective buying power is growing more slowly than the headline nominal increases to the official defense budget suggest, and is not increasing at the feverish rates that some observers allege.

In contrast to the salutary trend discussed above, China's growing transparency as it concerns specific spending priorities continues to leave much to be desired. Although Beijing has released biannual defense white papers since 1998 and has submitted some very basic data on intra-PLA allocations to the UN Secretary General since 2008, these limited measures fall far short of the levels of transparency achieved by the United States and its major treaty allies in Northeast Asia and Europe. For example, China still does not release even basic information that would provide insight into intra-PLA spending priorities, including a budget breakdown by service, the total amount spent on weapons imports, or the procurement costs of specific weapons and platforms. The 2013 defense white paper does not mention budget-related issues at all. While the document includes personnel numbers for China's three services for the first time, it does not even state how many personnel the Second Artillery has.

This contrasts sharply with the practices of some other major emerging countries. India, for example, publishes detailed spending breakdowns for its ministry of defense, defense pensions, army, navy, air force, and defense ordnance factories. While India is still sometimes criticized for its own level of defense budget transparency, China would be perceived very differently if it elected to at least offer similar spending details.

In response to foreign (and some domestic) criticisms about its military transparency, Beijing maintains that transparency concerning strategic intentions is more important than transparency concerning specific capabilities. In that spirit, it does indeed make general statements that describe the basic trajectory and objectives of its military development. Yet this does little to assuage the concerns of some that China's stated intentions will change in a crisis. The same is true for Beijing's categorical and abstract statements about these intentions, however sincere they may be at the moment they are expressed. (For example, the 2013 defense white paper states that "China will never seek hegemony or behave in a hegemonic manner, nor will it engage in military expansion.")

In sum, while there is evidence to suggest that China's government is increasingly transparent about how much money it actually spends on defense, details about intra-PLA spending priorities remain very limited, and overall military transparency remains far below the standards of other countries at a similar level of military development.

How can analysts draw meaningful inferences from patterns in China's announced defense spending when so many specific details remain secret and the accuracy of the reported spending is unclear?

Various factors suggest that China's official budget increasingly reflects its defense spending, with the narrowing range of U.S. Department of Defense disparity estimates as the most authoritative data point. Numerous reforms to improve PLA professionalism and accounting, including commercial divestiture in 1998, have put an increasing portion of revenues and expenditures on the books. The dearth of specific data disclosed by China's government leaves obtaining internal information by other means or inductive estimation as the only alternatives for determining the precise extent and nature of Chinese defense spending. Both these approaches require resources beyond what is available to individual civilian researchers working with open-source data.

The best evidence of the tremendous challenges in this regard is the paucity of published studies on China's defense spending, despite enormous global interest. Even research organizations with sufficient resources to assign multiple specialists to this task are unable to produce systematic, detailed, and authoritative inductive estimation. Western think tanks such as SIPRI (Stockholm International Peace Research Institute) and IISS have done excellent work, but their efforts yield only general estimates of defense spending.

A prime example of the barriers that even capable organizations face can be found in one of the most conceptually straightforward tasks: calculating the cost to China of producing a given platform or weapons system. Simply extrapolating from known prices of rough equivalents in other countries may not yield reliable results given China's very different, poorly understood, and possibly still-unsystematic input pricing. Then there is the question of whether, to what extent, and how to factor in purchasing power parity. As a result, truly intensive, systematic efforts may yield general costs estimates of some platforms with commercial analogues (e.g., simple surface ships) but not those with few commercial connections (e.g., missiles or stealth technology). Moreover, even achievement of a few rough estimates leaves vast areas uncovered and the task of estimation of China's aggregate spending unmanageable. Our discussions with specialists who have attempted such investigations suggest that one of the few reliable

conclusions of their herculean efforts was that China enjoys significant pricing advantages over other major military powers in some defense industrial areas (e.g., shipbuilding). Among nations capable of constructing relatively capable military vessels, for instance, none even approaches China in “bang for the buck” with respect to salaries for both engineers and laborers. Such advantages may allow China to afford very substantial armaments even at its announced budgetary levels, not to mention at somewhat higher spending levels.

What would new information concerning Chinese defense spending reveal to outside observers?

More specific information and evidence concerning categories of spending included in China’s official military budget would help outside observers more confidently determine what proportion of military-relevant spending is actually reflected in the budget. Budget breakdowns by service and within service would provide valuable indicators regarding PLA development priorities and capabilities.

On the whole, greater transparency about China’s defense spending would help reduce uncertainty significantly and mitigate concerns about whether Beijing is hiding a large proportion of its military spending. It would also help Chinese and foreign analysts evaluate the extent to which China’s capabilities and spending priorities are consistent with Beijing’s stated strategic intentions and interests.

Far from being limited to budgetary issues, greater military transparency overall would serve the interests of all states seeking to maintain regional and global peace and stability, including—and especially—China. Beijing has little to gain and potentially a great deal to lose by exacerbating extant uncertainty and widespread concerns about its current and future military trajectory.

The views expressed are those of the experts.

For further reference, see:

Adam P. Liff and Andrew S. Erickson, “Demystifying China’s Defense Spending: Less Mysterious in the Aggregate,” *China Quarterly* (forthcoming, 2013).

Andrew S. Erickson and Adam P. Liff, “China’s Military Development, Beyond the Numbers,” *Diplomat*, March 12, 2013.

Andrew S. Erickson and Adam P. Liff, “A Player, but No Superpower,” *Foreign Policy*, March 7, 2013.

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