



Executive Summary

EU-China relations are in 2020 almost as much a test of the EU's resilience as is its economic response to the coronavirus pandemic. There are good reasons for this.

2020 had not only been designated officially as an EU-China year, but it also coincided with Germany's semester presidency in the second half of the year. 2020 is also a year when several

European policy initiatives will have a significant impact on relations with China. In June 2020, the European Union looks increasingly likely to succeed in setting up **defensive economic policies**. Facing the failure so far of talks aiming at policy changes from China, it has just used a direct virtual meeting with Xi Jinping and Prime minister Li Keqiang to point out, it has put China on notice to translate its words into deeds.

The End of China's cherry-picking in Europe

The recent years have seen a clear progress in EU unity and coordination when it comes to defensive issues – trade, inward investment and critical technology. The European Commission has issued precise guidelines on critical security issues for the coming 5G networks, and the new investment screening regulation is scheduled to be operational in October 2020. In addition, due to the concern over the fire sale of company assets as a result of the pandemic, the European Union and some member states are creating new guidelines or temporary rules on financial **take-over** by non-EU actors. Recently, on June 17, the European Commission even adopted a White Paper “to address the distortions created by **foreign subsidies**” in the Single Market. Increasingly, cybersecurity threats and disinformation from China are also addressed.

Challenging China's preference for no change

A virtual EU-China summit was moved forward to June 22. There simply hasn't been enough contact over the months of Covid-19 confinement, and **no tangible sign of China's goodwill** has emerged, other than very vague proclamations. The Leipzig meeting of the 27 with China, which was an opportunity for the investment agreement with China, has been delayed *sine die* at the request of China. China is once more stalling *top-level* talks with Europe: it is likely waiting to see the result of the November US election.

This has caused **European leaders to move away from engagement** and what was for some independence or even equidistance between China and the US. They realize China is in no urgent need for a deal with the EU. In a bid to implement the promise of a “geopolitical Commission”, the EU leaders are now **airing publicly their disagreements with China** on a very broad range of issues: Hong Kong, human rights, cybersecurity, in addition to a level-playing field for a fair

and reciprocal access to the Chinese market. On WTO reform, climate change and debt forgiveness to countries hard-hit by Covid, they are also pointing out the need for action by China. Our note explains how the EU came around to these positions, while simultaneously reinforcing its defensive measures.

China's first stop in any important negotiation is Washington

Whatever Chinese analysts may say of an American decline, respect for Washington's capacity to make decisions has run stronger than any urge for concessions in order to “win over” Europe. This is due to the actual dependencies of China vis-à-vis the United States. **China's foreign policy is conducted on the of relative strength and risk**. Europe, with its balance **between cooperation and acknowledgement of systemic rivalry**, its taste for nuance and proportional responses, its institutional limitations, its internal divisions, a military focus on the immediate Eastern border or nearby regions in crisis, has appeared far less likely to inflict damage on China.

The European leaders in a quandary

Periodically, partners wishing to engage, or to re-engage China draw up a list of issues on which they expect China to converge on the basis of its own interests. In reality, the only area of agreement is a common but **vague commitment to multilateralism** and multilateral institutions. A convergence between China and Europe on the need to implement the 2015 Iran nuclear agreement has perhaps been the only positive item on a long list of issues. In March 2019, in the face of **undelivered promises**, the Commission's strategic document cited ten action points to be fulfilled within one year. The EU is going full steam ahead on action points which it can implement on its own, **regardless of China's move**.

However, **not all member states are ready to pay the price for a strong negotiating stand in front of China's** obstinacy and leverage. The hesitation also appears in declarations regarding China's recent aggressive moves. Sweden is the only member state which has advocated sanctions of any kind towards China in light of the announcement of the imposition of a transposed national security law into Hong Kong. To the EU's credit, the HR/VP had made a statement early on, regretting that the Chinese move did not conform to “its international commitments, nor with the Hong Kong basic law”. European hesitations also coincide with the **difficulty to achieve unity** over time for a strong policy, and a preference of EU institutions for mixed policies – cooperation, competition and systemic rivalry at the same time.

China is betting on a strong recovery to heal the social wounds

It is too early to predict how an exceptional year will run its course for the European and Chinese economies. China's seasonally adjusted GDP did plunge by 9.8% in the first quarter of 2020, against -3.3% for the Euro-27. Judging from China's foreign trade numbers, the

“**second shock**”, or a diminished demand from the outside world, isn’t happening all that much. Overall, there is a huge spike in medical exports related to the pandemic – a short term outcome of China’s “**mask diplomacy**” seizing the opportunity of the world’s dependence to secure a major source of trade profit. What also appears in a trade breakdown by category is that China – as other East Asian suppliers – has enjoyed a surge in **digital and telecom exports**.

This unexpected trend is currently coupled with what some describe as “an **extra-friendly attitude**” of national and local officials to foreign companies. China’s Ministry of Commerce is in the lead for many of these initiatives since April to guard against the risk of disruption in China’s supply chains, following the widespread talk of moving away from reliance on China. This would seem to be a dream program for any negotiation with the EU on a basis of **reciprocity**. It is not, because these are only unilateral, local and easily rescindable decisions.

The EU Quest for Strategic Autonomy and the Issue of Decoupling

The issue of *de facto* deglobalization or voluntary decoupling from China is of course seen as a paramount risk by the leadership. Europe sees a wave of arguments for either **diversification of suppliers**, or **relocalization**. The scarcity of medical supplies during the Covid-19 pandemic was of course a shock that echoed in public opinion. This has given a boost to the advocates of a national or European **industrial policy**. Reshoring, whether in Europe or on a national basis, is an extension of the defensive policies that Europe is putting in place. This can also serve as **a warning to China’s leaders** that policies seeking to indigenize China’s industrial production, and failure to grant reciprocal access, do result in decoupling initiatives by China’s partners, and not only by the United States.

In the **waiting game** that has again started, China has a clear advantage. Talk about European “**strategic autonomy**” may be interpreted by some, in Europe or in China, as signaling a shift from the United States. China’s wait for the American election outcome is a perfect answer to Europe’s quandary and weakness. **Europe cannot extract by itself a deal with China**, and it currently sees no joint path with the United States.

Policy Conclusions

Who can blame Chinese leaders for thinking the relationship with Europe is fine as it is? It is now up to Europeans to make their own interests and values China-proof. Should convergence and cooperation from Beijing come back on some issues, it would be welcome. But Europe should not rely on this hope. **The “frank and intense” talk** by Europeans at the June 22 virtual EU-China summit is a new start. Accepting this sober reality leads to the following **policy recommendations**:

► Abandon your illusions.

China is no longer coming from behind, economically weak and in conflict avoidance mode. It is strong today, and **systemic rivalry** is

how the CCP sees the world under Xi Jinping. China’s foreign policy is conducted on a basis of relative strength and with calculated risks increasingly being taken. Europe may think it is far away, but in an actual conflict, Europe is vulnerable because we depend on global integration, supply chains and rules.

► Ready for China’s undelivered promises in the short term.

Climate and environmental issues or current medical and vaccine concerns should bring us together in an ideal world. They do not. On climate, China still conducts a carbon-based energy policy with “clean” coal as the key. Our other objectives for cooperation - multilateralism, denuclearization, cybersecurity - remain entirely unfulfilled, with the exception of support for the 2015 Iran nuclear deal. China’s preference for a **long-term declaratory horizon** is based, once more, on **gaining time** and **avoiding legally binding commitments**. “No change” is the preferred option in Beijing.

► Diversify strategic supplies, assess the priorities and costs of reshoring at home.

In the long term, policies to diversify critical supply chains away from China make sense for Europe, as does reshoring for some manufacturing. Ensuring the security of critical supplies and technology has a cost – think, for example, of the price of drugs for health systems. We can perhaps **bear the expense in this critical sector**. But extending the scope of reshoring requires either large productivity gains, or a reduction in labor costs, or protectionism **at the expense of our standard of living**.

► Europe gains no traction with China if it speaks with a weak voice.

When China takes new risks, Europe’s mixed language and balanced statements simply fail to make the grade, and are very often misread, voluntarily or involuntarily, by China’s leaders. The language of cooperation is easily twisted to fulfill compliance with China’s goals and ideology.

► Move whenever possible towards binding rules for member states.

Investment screening, a halt to predatory take-overs, an EU instrument to sanction state subsidies to non-EU companies or using third country bases for dumping, a unified approach to telecom and digital network security are all commendable. But Europeans should accept that these policies must become **more binding** towards member states.

► Turn to democracies without aiming for identical views.

Europe needs to stop focusing on trying to convince China, and turn much more to democracies instead. **A league of democracies** is an idealist concept, given the differences in interests and values within their range. Yet claiming equidistance between them and China or other autocracies only serves to fragment and **accelerate the crisis of democracy**, and to help the advocates of authoritarianism. Calling out China is useful. Pure and perfect multilateralism does not work if one is its only practitioner.