Europe-China relations – from the 2020 Strategic Agenda to seeking de-risked engagement

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China Macro Group (CMG)
Agenda

1. Economic baseline – Europe-China economic cooperation
2. EU and European policy towards China
3. PRC policy towards EU/Europe
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Top-level economic baseline: rapid trade and investment integration, “muted” mutual portfolio investments

Trade: trade keeps growing, especially services ...

Goods: EU-China bilateral trade by exporting country

- In 2022, total annual trade in goods reached 856 € Bn, making China the EU's 3rd - and the EU China's 2nd - most important export destination.
- EU now records a 396 € Bn trade in goods deficit, while running a relatively small surplus for services of 20.2 € Bn.

Services: EU-China bilateral trade by exporting country

Investment: FDI stocks grow in both directions

- EU outbound FDI stock in China increased moderately (CAGR 2.7% 2012-2020), now accounting for 3.8% of total.
- Chinese outbound FDI stock in the EU increased quite rapidly (CAGR 14.2% 2012-2020), now accounting for 3.1% of total.

Portfolio investment: low integration

Outward portfolio investment (in % of total outward portfolio investment, June 2022)

- EU with positive investment balance with China, although Chinese outward portfolio to EU accounts for a relatively much larger share of Chinese total portfolio investment.
- US-EU far more financially integrated.

EU’s growing trade deficit vis-à-vis China contrasted by a trade in services surplus, as well as a positive investment balance.

Sources: Eurostat, BACI Database (2021), Institut der deutschen Wirtschaft, IMF.
Notes: FDI and portfolio investment data for China includes Hong Kong.
China a key trading partner for Europe, but varying highly in significance across countries – DE alone accounting for 48% of EU27’s China exports

Source: UN Comtrade (data for 2022)
Note: Swiss trade without gold and precious metals (for context: 2022 Swiss exports to China incl. gold 42bn CHF, excl. gold 15.9bn CHF). UK data for 2021

Lower direct importance of the Chinese export market in countries lacking high-tech manufacturing and international brands
EU view/investment: EU FDI in China rebounds in 2022, but concentrated in a few deals in narrower sectors

Strong rebound of EU investments into China in 2022 after decline

Annual FDI flows from the EU to China (excl. HK)

- FDI from EU countries dropped between 2018 and 2021 by 51%, despite overall FDI inflows to China reaching a historic high in 2021
  - This can be explained by a combination of reasons pertaining to Covid-induced investment holdbacks, regulatory uncertainty, declining growth expectations as well as growing geopolitical risks

- In recent years, European FDI to China has overall been driven by a small number of big ticket transactions from a few EU companies
  - From 2018-2022, the four German companies VW, BMW, Daimler and BASF alone accounted for >1/3 of all European investment to China
  - In 2021, just five sectors (automotive, biopharma, chemicals, consumer products manufacturing, and food processing) attracted around 70% of total FDI from Europe

Mid-term trend since 2018, indicating EU FDI in China driven mainly by a few big transactions – mainly from Germany

Source: PRC MOFCOM (data source for 2022 are preliminary); Caixin
PRC view: geopolitical dynamics show impact on Chinese FDI trends, while trade relations remain fully intact

EU remains key trade partner for China...

- Since 2012, EU remained a key trading partner for China, especially as exports to EU have risen more than China’s total export
- Declining share of China’s top 5 export and important partners show trade diversification

China’s goods exports by destination (in %)

<table>
<thead>
<tr>
<th>Year</th>
<th>EU</th>
<th>Other</th>
</tr>
</thead>
<tbody>
<tr>
<td>2012</td>
<td>17.2%</td>
<td>50.5%</td>
</tr>
<tr>
<td>2013</td>
<td>16.2%</td>
<td>50.5%</td>
</tr>
</tbody>
</table>

China’s goods imports by source (in %)

<table>
<thead>
<tr>
<th>Year</th>
<th>EU</th>
<th>Other</th>
</tr>
</thead>
<tbody>
<tr>
<td>2012</td>
<td>10.7%</td>
<td>63.5%</td>
</tr>
<tr>
<td>2013</td>
<td>10.5%</td>
<td>63.5%</td>
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</tbody>
</table>

...while its FDI flows to the EU have collapsed...

Chinese FDI flows to EU27 + UK (in € Bn)

<table>
<thead>
<tr>
<th>Year</th>
<th>M&amp;A</th>
<th>Greenfield investment</th>
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</thead>
<tbody>
<tr>
<td>2012</td>
<td>7.6</td>
<td>1.4</td>
</tr>
<tr>
<td>2013</td>
<td>1.9</td>
<td>1.5</td>
</tr>
<tr>
<td>2014</td>
<td>2.4</td>
<td>1.5</td>
</tr>
<tr>
<td>2015</td>
<td>4.5</td>
<td>1.5</td>
</tr>
<tr>
<td>2016</td>
<td>9.8</td>
<td>1.5</td>
</tr>
<tr>
<td>2017</td>
<td>19.7</td>
<td>1.5</td>
</tr>
<tr>
<td>2018</td>
<td>15.3</td>
<td>1.5</td>
</tr>
<tr>
<td>2019</td>
<td>7.9</td>
<td>1.5</td>
</tr>
<tr>
<td>2020</td>
<td>7.9</td>
<td>1.5</td>
</tr>
<tr>
<td>2021</td>
<td>7.9</td>
<td>1.5</td>
</tr>
</tbody>
</table>

...now concentrating on greenfield FDI in NEV

Largest 6 Chinese FDI announcements in Europe since 2021

- Envision AESC: Greenfield, Automotive, €0.45 Bn
- Holodyne Medical Solutions: M&A, Pharma, €0.54 Bn

China’s M&A activities in the EU negatively affected by increased scrutiny from EU FDI screening and outbound capital controls

Sources: UN Comtrade, Rhodium Group
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EU-China milestones: loosing enthusiasm within a decade, from joint strategic agenda to the EU’s de-risking...

EU-China relations over the last decade – navigating growing economic, geopolitical and normative complexities

- ‘2020 Strategic Agenda for Cooperation’ and Xi’s European tour
- ‘MIC25’, Chinese investments in Europe and MES “issue”
- ‘Strategic Outlook’, “geopolitical commission” and HK NSL
- EU’s Xinjiang-related sanctions and Chinese response
- Covid and Ukraine crisis further prompt EU to “de-risk”

2013/4

China and EU jointly launch a series of ambitious goals to be completed by 2020

- EU and China 2013 jointly publish goal-setting document to widen cooperation
- After the BRI launch in 2013, Xi makes a “charm offensive” trip in 2014 to Europe

2015-2017

Chinese acquisitions of European “crown jewels” fuel the reciprocity debate

- ‘Made in China 2025’ policy lays out China’s technology leadership ambitions
- Acquisition of Kuka by Midea as key moment in changing perception in Europe
- EU refuses to grant China Market Economy Status (MES)

2019

Clear shift in EU policy, now describing China as “partner, competitor and rival”

- Strategic Outlook holds that China’s geopolitical goals “present security issues for the EU”
- The BDI, German business federation, labels China a “systemic competitor”
- EU imposes sanctions on Chinese officials in view of alleged human rights abuses – China retaliates

2020/1

CAI formally put on ice by EP – EU launching more “autonomous” tools

- Ratification of the comprehensive Agreement on Investment (CAI) «put on ice» by EU parliament

2023

“De-risking” as an “adjusted” and “strong” EU approach distinct from “de-coupling”

- Adjustment of EU’s China Strategy, now focusing more on China as a “rival” and “competitor”
- De-risking approach fueled by Europe experiencing external dependencies during Covid and war in Ukraine

China’s industrial policy with ‘Made in China 2025’ as pivotal moment to shift perception in Europe about EU-China relations
... reflected in narrowing outcomes of EU-China summits, as disagreements – mostly voiced by EU – multiply

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<tr>
<td><strong>Multilateralism</strong></td>
<td>Memorandum of Understanding on BRI-EU Investment Fund signed</td>
<td>Joint support for multilateralism and opposition to protectionism</td>
<td>Continued shared commitment to multilateralism</td>
<td>Stressing difference in values, political systems and approach to multilateralism</td>
<td>N/A</td>
</tr>
<tr>
<td><strong>Economy</strong></td>
<td>Need to address overcapacity</td>
<td>Opposing EU anti-dumping measures</td>
<td>CAI negotiations go into new phase after market access offers</td>
<td>MoU signed on state-aid control dialogue and fair competition review</td>
<td>Differences over reciprocated sanctions / both sides calling for fair market access</td>
</tr>
<tr>
<td><strong>Security</strong></td>
<td>N/A</td>
<td>Joint support for Iran Nuclear Deal after US withdrawal</td>
<td>Reaffirmed joint support for Iran Nuclear Deal (JCPOA)</td>
<td>EU emphasizes China’s “special responsibility” in the Ukraine crisis</td>
<td>EU emphasizes China’s “special responsibility” in the Ukraine crisis</td>
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<tr>
<td><strong>Global challenges</strong></td>
<td>Shared support for Paris Agreement after US withdrawal</td>
<td>Joint statement on climate change and clean energy</td>
<td>Joint statement signed on clean energy transition and energy security</td>
<td>Shared support for cooperation on climate change</td>
<td>Cooperation on global biodiversity framework</td>
</tr>
<tr>
<td><strong>Formal outcome of summit</strong></td>
<td><strong>Failure to reach Joint Statement over China’s Market Economy Status</strong></td>
<td>Agreement on Joint Statement</td>
<td>Agreement on Joint Statement</td>
<td><strong>Failure to reach Joint Statement over disagreement on Hong Kong and Xinjiang</strong></td>
<td><strong>Failure to reach Joint Statement over disagreement on war in Ukraine</strong></td>
</tr>
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</table>

Summit dynamics evolve from economic to governance and security issues – new recent dynamic of Xi’s personal involvement
On the basis of direction on China policy set in March 2019, the EU Commission turns more assertive

EU shifts strategic posture towards China...

**EU 10-point “Action Plan”**

1. Cooperate on UN commitments
2. Call on China to peak emissions by 2030
3. Deepen engagement on regional security
4. Cooperate on principles for 3rd countries (EU-China Connectivity)
5. Rebalance economic relationship
6. Reciprocity in procurement
7. Ensure level-playing field of public procurement in EU
8. Address foreign market distortions
9. Protect critical digital infrastructure
10. FDI screening in EU-MS

... evolving to the Commission’s re-articulated ‘clear-eyed’ approach in March 2023

Von der Leyen draws **3 key conclusions** that demand a recalibrated EU posture

- **Domestic hardening**: China “moving into a new era of security and control”
- **Securitized trade**: The “imperative for security and control now trumps the logic of free markets and open trade”
- **International order**: The CCP’s “clear goal is a systemic change of the international order with China at its centre”

In response, the EU vows to adapt its approach towards China

**Diplomatic «de-risking»**

- “Strengthen the international system itself”
- “Ensure diplomatic stability and open communication with China”

**Economic «de-risking»**

- “Our relations are not black or white – and our response cannot be either. This is why we need to focus on de-risk – not de-couple.”
- “But our relationship is unbalanced and increasingly affected by distortions created by China’s state capitalist system.”

**New four-pronged approach**

- Competitive, resilient economy and industry
- Strengthened trade defense instruments
- Investment controls for sensitive technologies
- Cooperation with partners

While EU China policy remains anchored in ‘partner-competitor-rival’ triptych, it is recalibrated to the new geopolitical situation

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1 Including resolutions, initiatives, non-legislative enactments, consultation procedure; 2 Resolution for a new EU-China strategy – EU Parliament, September 2021
From a “special relationship” and “pioneer spirit”…

1950: early recognition of PRC

1980: first sino-foreign JV (Schindler)

2009: early granting of MES to China

2013: first continental European and comprehensive FTA

2016: «strategic innovative partnership»

2018: UBS as first foreign bank with majority ownership

... to altered context for Switzerland’s China policy...

• General damage to China’s reputation in the “West”, e.g. with Zero-Covid policy

• US-China strategic competition and the EU’s more confrontational China policy – rising costs for pragmatic China policy

• Swiss parliament and public more concerned about human rights situation and ESG topics

• Frustration over lack of materialized cooperation under Sino-Swiss BRI Memorandum of Understanding

• China’s alleged influencing operations in Switzerland

... to China strategy (March 2021) seeking calibration and coherence

Acknowledging new geopolitical realities

• Recognizes China as a new global power

• Points out non-convergence, and is explicit e.g. on increasing societal control, challenges for ethnic minorities and China’s intent to “change rules of international cooperation”

• Recognizes trade-offs in balancing values and interests

Relations today – broad, multi-layered and “constructive”

• Adherence to One China policy

• Divergences and unsatisfactory outcomes on human rights dialogue

Geopolitical positioning – pro engagement

• Continue independent, universal, neutral and “bloc-free” foreign policy

• Focus on strengthening multilateralism

• Pro engagement, no intent to change China – but structured relations with the EU and closer cooperation becoming more important

Key priorities

• Unapologetic on human rights (e.g. HR dialogue)

• Economic policy, esp. broadening market access and FTA update

Enablers

• China competence, but no budget associated

• “Whole-of Switzerland” approach and cross-ministerial working group (IDAG)

Domestic and international situation increasingly narrowing Switzerland’s space to fully continue past policy trajectory
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In “a complex international situation”, Beijing continues to see Europe as “comprehensive strategic partner”...

China continues to push for constructive relations with the EU...

“China has always regarded the EU as a strategic force in the international landscape, and has always regarded the development of China-EU relations as a priority for Chinese diplomacy. We will continue our good tradition with the European side, maintain close communication, enhance strategic mutual trust, focus on mutually beneficial and win-win cooperation, and work together to overcome disturbances and challenges, and achieve a high level of performance of China-EU relations.”

— Xi Jinping during visit of European Commission President Ursula von der Leyen in Beijing in April 2023

...driven primarily by geopolitical and economic considerations

<table>
<thead>
<tr>
<th>Strategic intent vis-à-vis the EU&lt;sup&gt;1,2&lt;/sup&gt;</th>
<th>Prioritized areas of cooperation with the EU&lt;sup&gt;3&lt;/sup&gt;</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Preserving constructive relations and a shared interest-focused engagement logic between the EU and China</td>
<td>• Shaping multilateralism: Pursuing shared interests of enhancing cooperation and coordination in the intl. system with the UN at its core and ensuring equality</td>
</tr>
<tr>
<td>• Advocating an independent EU approach to China under the EU’s “strategic autonomy” policy, without interference or influence from “third parties” (i.e. the US)</td>
<td>• Economic cooperation: Continuing to strengthen ties with the EU as China’s largest trading partner</td>
</tr>
<tr>
<td>• Ensuring access to EU markets and technology knowhow, while also attracting foreign investment from the EU</td>
<td>• Improving market access: Attracting EU investment to China, while also getting better access to EU markets</td>
</tr>
</tbody>
</table>

Source: <sup>1</sup> Xi’s speech during EC President VdL’s visit; <sup>2</sup> New Statesman interview with Chinese Ambassador to the EU, Fu Cong; <sup>3</sup> China’s 2018 EU White Paper

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**China’s EU strategy focusing foremost on economic (technology/development) and geopolitical (multipolarity) interests**
### Analysis of change vs. 2003 White Paper

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<tbody>
<tr>
<td><strong>External environment and China’s position</strong></td>
<td>• Multi-polarization and globalization continued, though with some difficulties</td>
<td>• China did not fundamentally change its view of the external environment</td>
<td>• China held that unilateralism, protectionism, and anti-globalization trends on the rise</td>
</tr>
<tr>
<td></td>
<td>• Peace and development as theme of times</td>
<td>• China claimed its comprehensive power increased, but China did not change its judgement about its global position</td>
<td>• China started aiming to build new type of international relations and a “community of shared future for mankind”</td>
</tr>
<tr>
<td></td>
<td>• China hoped to create a favorable international environment as it needed to build a “prosperous society”</td>
<td></td>
<td></td>
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<tr>
<td><strong>EU’s power and global role</strong></td>
<td>• EU integration process as irreversible, though facing many difficulties and challenges</td>
<td>• Though the EU was challenged by the international financial crisis, no change of China’s sentiment about EU’s power and global role</td>
<td>• Although EU affected by events such as Brexit, no change of China’s sentiment about EU’s power and global role</td>
</tr>
<tr>
<td></td>
<td>• EU would play an increasingly important role in regional and international affairs</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>EU-CN relationship and overarching objectives and principles</strong></td>
<td>• No fundamental conflict of interest between China and EU and not a threat to each other</td>
<td>• 4 new targets proposed:</td>
<td>• 4 new principles proposed:</td>
</tr>
<tr>
<td></td>
<td>• Shared interests “far outweigh divergences”</td>
<td>- Promote bilateral economic development</td>
<td>- Keep mutual respect and adhere to “One China Principle”</td>
</tr>
<tr>
<td></td>
<td>• Key objectives are:</td>
<td>- Share experience in reform, for example, global governance reform</td>
<td>- Complete global governance system together</td>
</tr>
<tr>
<td></td>
<td>- Deepen political relationship and maintain world peace</td>
<td>- Maintain world peace</td>
<td>- Maintain cultural exchanges</td>
</tr>
<tr>
<td></td>
<td>- Deepen economic and cultural exchange</td>
<td>- Enhance cultural connections</td>
<td>- Insist on openness and inclusiveness</td>
</tr>
<tr>
<td><strong>Key areas of cooperation</strong></td>
<td>• Politics, economy and culture as key cooperation sectors</td>
<td>• Military cooperation removed</td>
<td>• No relevant change</td>
</tr>
<tr>
<td></td>
<td>• Military cooperation also suggested</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>China’s aggregated stance towards EU</strong></td>
<td>EU seen as just another economic partner, no intention to partner on global affairs</td>
<td>China starts laying out ambition to work together on global governance reforms, and seeks to deepen economic cooperation</td>
<td>China asserting “conditions” for continued cooperation, wanting to partner with EU to reform global governance together</td>
</tr>
</tbody>
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Though importance of EU-CN relation unchanged to China, more friction expected with China adding more conditions.
As Russia's war in Europe continues, China with an increasingly difficult task not to push Poland closer to its US ally and distance itself from China.

Germany's potentially more assertive new China Strategy could lead China to reconsider its approach.

In June 2023, Premier Li Qiang will visit Chancellor Scholz in Berlin.

Maintaining strategic ties with Russia while dealing with key EU MS becomes more challenging.

Xi-Macron personal relationship is an important factor as annual head-of-state meetings are resumed.

In 2023 April, Taiwan set up Rep. Office in Milan.

As Russia's war in Europe continues, China with increasingly difficult task not to push Poland closer to its US ally and distance itself from China.

With strengthened Italy-Taiwan relations and Italy’s possible exit from the BRI, Sino-Italian relationship could be affected.

Prime Minister Giorgia Meloni announced to visit China in 2023.

### China vis-à-vis key EU MS: China’s foreign policy focus lies on maintaining constructive relations

<table>
<thead>
<tr>
<th>Key relations</th>
<th>China’s key strategic interests</th>
<th>Recent developments</th>
<th>Outlook</th>
</tr>
</thead>
</table>
| Sino-German relations | • Get access to Germany’s advanced manufacturing, technological expertise and the EU single market  
• Leverage Germany’s central position in the EU to shape EU policies on trade, investment, and technology | • China emphasizing common ground in the face of German ambivalence  
  ➢ Nov 2022: Xi received Chancellor Scholz as first G7 leader in 3 years, focus on business ties  
  ➢ Apr 2023: FM Baerbock’s assertive visit with main focus on Taiwan perceived as hypocritical | Germany's potentially more assertive new China Strategy could lead China to reconsider its approach  
• In June 2023, Premier Li Qiang will visit Chancellor Scholz in Berlin |
| Sino-French relations | • Build support against US-led containment via this important and less US-leaning EU member  
• Get access to France’s advanced research and technology in key areas such as aerospace, civil nuclear technology, and pharmaceuticals | • China backing France in its push for EU “strategic autonomy” and revitalizing business ties  
  ➢ Macron received lavish reception by Xi in April with several major Sino-French deals signed  
  ➢ Macron subsequently stressed need of own EU approach, not just being “followers of the US | Maintaining strategic ties with Russia while dealing with key EU MS becomes more challenging  
• Xi-Macron personal relationship is an important factor as annual head-of-state meetings are resumed |
| Sino-Polish relations | • Get access to the EU single market via infrastructure investments in Polish logistics hubs  
• Prevent atlanticist Poland from tipping the EU more towards the US | • China trying to convince Poland of the importance of a political settlement of the Ukraine crisis:  
  ➢ Special envoy Li Hui travels to Warsaw for talks, voicing China’s support for peace talks | As Russia’s war in Europe continues, China with increasingly difficult task not to push Poland closer to its US ally and distance itself from China |
| Sino-Italian relations | • Get strategic harbor ports for better access to Eastern Europe and Northern Europe  
• Impact EU's China policy via Italy and coordinate and cooperate with Italy in G20, who is also a G7 member | • In 2023 April, Taiwan set up Rep. Office in Milan  
• Italy is screening Chinese SOE’s (state-owned enterprise) new investment agreement in Pirelli  
• Italy claims that it has not decided about the extension of BRI but will not damage its relationship with China in any case | With strengthened Italy-Taiwan relations and Italy’s possible exit from the BRI, Sino-Italian relationship could be affected  
• Prime Minister Giorgia Meloni announced to visit China in 2023 |

China strives to engage key EU-MS for pragmatic collaboration, strategic goals such as strategic autonomy play subordinate role.
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