



## Transcript

# China–EU Relations: Moving Beyond Trade

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**Jonathan Fenby:**

Well thank you everybody for coming. My name's Jonathan Fenby, I'm chairing, moderating this group. Today we have a large and interesting subject ahead of us on China–EU relations and there are many, I think, different facets to this. First of all on the trade front, obviously what China–EU trade relations really consist of, the extent to which it is an EU to China relationship or the EU nations on their individual basis with China, and then whether beyond trade what relationships can be evolved, how they have been evolved, what's come out of the many dialogues that are going on between Europe and China over recent years, and of course that some of you may wish to look at in the context of the recent visits by the battling two British representatives, George Osborne and Boris Johnson, shortly to be followed, we understand, by David Cameron, and we have an extremely well-suited expert group here on the panel to speak about this.

Kerry Brown, who I referred to as Kerry but I must now refer to as Professor Brown, quite clearly, who's written a great deal on this subject, has been particularly involved in EU–China relations, was here at Chatham House, mainstay of the China programme for I can't remember how many years, it seemed quite a long time, and then went off to other climates in Australia where he is professor and dealing with China affairs but still very much with a hand on the EU–China relationship.

Guy de Jonquières, who I've known for more years probably than either of us would wish to remember, going back to being correspondents together in Paris in the 1960s or 1970s, I can't remember, was a mainstay of the *Financial Times* for many years as the expert on global trade and then as columnist on Asian affairs based in Hong Kong, and since then has maintained his interest in Chinese affairs, and indeed in China–EU affairs, as a senior fellow at an organization which I was about to mispronounce, but ECIPE (European Centre for International Political Economy).

Bernice Lee, research director for Energy, Environment and Resource Governance here at Chatham House, and was previously head, or she was head of the Energy, Environment and Development Programme and team leader for the EU–China Interdependencies on Energy and Climate Security project, and again has had much experience in this field with a particular expertise in your own sector.

So if I could start off with you Kerry, do we go beyond trade?

**Kerry Brown:**

Since I've been living in Sydney I have been overcome by an enormous optimism, so I'm afraid when you live in the world's most beautiful city that you see the world through intrinsically rose-tinted glasses. I know there are people on the panel who might not share some of the things that I'll say, but that would be good for a debate. So what I would say is that the EU and China – I mean every time in the last few years that I have been asked to talk about the EU and China there's always this moment before I open my mouth of existential crisis when I think what the hell do I say about this? I don't not only know about it but originally I didn't really care about it, but because of running a project for the European Union China Research and Advice Network, which is still running, I have picked up knowledge of the EU-China relations rather like one picks up a bug, but it's a pleasant bug and so that will be the basis of what I'll say, the sort of few comments.

So I think in fact the only conceptual way that you can look at the EU and China is as dynamic reforming entities. They are different of course, but they have to go through a big, big change in the next 10 years. China's changes are really about its internal balance, its urbanization, the extraordinary issues, it will have to find new sources of growth while the rest of the world really isn't delivering the things that China wants for that indigenous growth, and for the EU it's obviously, as a result of the eurozone crisis, got to find a different way of functioning. And I don't think that there's much choice in what they have to do, they either change or die, they either survive or go down, and so I think that that means that the policy choices are different, are reasonably restricted. If you look at the sort of evolution since 1975 when the EEC as it was then, the People's Republic, made their first diplomatic recognition – you think what China was like in 1975, I think in that year Zhang Chunqiao, one of the members of the Gang of Four, produced an important paper call on the dictatorship of the proletariat fighting against the bourgeoisie, and when you think of what happened in three years' time when the reform and opening up process started, of how radically different China is now to what it was in 1975, but also how radically different the European Union is now to the entity in 1975.

In fact if you plot the key moments over the last 40 years of change, in fact there's an odd kind of synergy between the changes that China underwent and pragmatic decisions it made about its relations in particular with the European Union or Europe and the things that changed in Europe. So if you think in 1985 – the legal basis of the relationship between the European Union to this day and the People's Republic of China is the agreement in the

1985, the EEC-China Trade and Economic Cooperation Agreement, which is basically a tariff agreement and it's all trade, it's not a political agreement, it is restricted to trade access, and when you think of why China and the EU and the European Economic Community would have made that agreement, well it was at the beginning or really at the very critical moment of China's liberalization of the 1980s and sort of really, really important moment in its reform and opening up, and also a moment when the European Economic Community was undergoing the first of several stages of enlargement, which resulted in 1992 in the Maastricht Treaty, kind of really making a much more significant political unity in creating the Union as we know it today. But also if you think in 1992, that was the year of Deng Chow Ping's sudden tour and therefore also a critical moment in the evolution and commitment of the People's Republic to marketization and change and engaging with the international trade environment.

If you think of 2001, I mean really the big sort of enlargement process from 2001 to 2005 of the EU when it changed, I think 15 members up to 27 members over that period. You also think in 2001 onwards the first five years really of China's implementation of the World Trade Organization, the kind of extraordinary impact that that has had on China's productivity, on its integration into the global economy and global supply chains. And then a critical document in 2006, the EU and China, produced by the European Commission that year, a sort of very prescient document, a document called Closer Partners Growing Responsibilities, which is a much more politically nuanced document but it sets out five key areas and those I think are the areas that we have to reflect on when we think of kind of strategic interest that the European Union has as it tries to, during its own era of reform and dynamic change, trying to engage in pragmatic ways with the opportunity that China offers.

Those five key areas are: supporting China's transition towards a more open and plural society. Number two: sustainable development, which I'm sure Bernice will talk about, and energy climate change, international development and sustainable economic growth. Number three: trade and economic relations, which is the traditional area of their most deep relationship, the most deeper kind of integration with each other. Number four: strengthening bilateral cooperation. Well I was in Brussels a couple of weeks ago and I said the only thing I really know about the EU and China is they have 56 strategic dialogues, but that's wrong, they have over 80 strategic dialogues. I mean there are an extraordinary number, an extraordinary amount of speaking in different kind of sectors, between different commissions and different parts of

the Chinese government system and that's an enormous amount of knowledge, obviously it needs to have some kind of consolidation and it's a really important kind of dialogue to have. And the final one is supporting and promoting international and regional cooperation.

Very finally, so I think we're talking today about pragmatic issues, about the things that we would say that EU and China need to do in the next 10 years of their distinctive reform paths as they try and map out a holistic vision of what they want and what they want from each other and how they can pragmatically help each other. So I would say we can talk to Europe, the European Union, about these things. Number one is that we need greater conceptual unity in Europe about our expectations over trade and investment with China. This is a very contentious thing, and Jonathan's just mentioned the two visits in Beijing this week, a lot of that has been about investment in, welcoming Chinese investment in nuclear energy in particular in the UK at the moment. I mean there's very different regimes across Europe, the 28 member states now, and trying to have some conceptual unity about where we see mutual benefit between member states and where we're fighting for bilateral interest. Because, according to the EU Chamber of Commerce audit of Chinese companies based in Beijing this year, they issued this saying the biggest problem for Chinese investors is barriers to entry because of the very different regimes across the member states, and so this is something that we obviously have to think about.

The second is a greater political vision over what Chinese growth means for us. I mean it's a huge market that we kind of have potential access to in China and it'd be a good market for us to have greater kind of entries into, and we need to be more unified about that. The third is service and finance. I mean these are really, really important areas for our economies in Europe and we need to have the right tools in order to be able to build financial and investment and service sector cooperation with China. This is something Li Keqiang has talked about as premier as the sort of basis for growth – service and finance are very important. The fourth is stronger vision for partnership in innovation, China's talked a lot about innovation, but we don't have a common understanding of what innovation is and how we can tie into the 15 year programme from 2007, I think it was, the sort of blueprint for innovation. And finally, I think we need to have some shared vision of modernity. We have an era of smart phones, smart devices, so therefore I think for the EU we need an era of smart policy. Thank you.

**Jonathan Fenby:**

Thank you very much. Well Guy, what smart policy would you advocate? I should just say for a moment that this is on the record, I should have mentioned that earlier.

**Guy de Jonquières:**

Thanks very much. Trade and investment, one arena in which the EU should really carry weight with China, the EU is the world's biggest trading block, it's China's biggest export market, trade and investment encompass almost all their bilateral economic relations and they're the only area of foreign relations where EU members are bound by treaty to act as one. Unfortunately, the EU is not only failing to punch its collective weight, it has repeatedly shot itself in the foot. That's particularly unfortunate at a time when many European companies are looking to a united and effective EU to challenge creeping protectionism and discrimination against them and other foreign businesses on the Chinese market. A united EU is not what they have got. China's rulers respect power above all else and, unlike Dr [Henry] Kissinger, they have a number to dial when they want to talk business with Europe. It starts with 4930, not 322. For China-EU central is not Brussels, it's Berlin, which it has cultivated acidulously in the last few years. Indeed, so low is Beijing's regard for Brussels that a couple of years ago it unilaterally cut off all contacts with the European Commission on trade issues for a period of months.

The EU and its member states have only themselves to blame for this. They have positively encouraged Beijing to play divide and rule by allowing themselves to be bought off one at a time with export orders, investments, development aid and market access concessions and other blandishments. As a result, their economic dealings with China increasingly bypass Brussels as well. Now all of this has been a source of growing concern in Brussels, particularly to Karel De Gucht, the EU trade commissioner. Last year he resolved to assert his authority by landing a sure-fire knockout blow that would make China sit up and take notice and bring the errant EU member governments into line. Against the advice of some of his more experienced officials, his chosen instrument was an anti-dumping investigation into Chinese solar panels, panel exports, which I imagine you have all heard.

In retrospect, he could hardly have picked a more ill-judged battleground. The case was flawed both economically and procedurally. Why threaten to raise the prices of products that Europe was subsidizing, in some cases quite

heavily, in order to hold their prices down? The case failed to cow Beijing which, far from seeking to expand solar panel output, was actually busy struggling to purge the industry of a ruinous excess capacity glut by closing much of it down, and the case backfired politically. Berlin equivocated even though the principal European industry complainant was a German company. In Brussels German officials indicated support, but on a visit to Beijing earlier this year Chancellor Merkel as good as told Commissioner De Gucht in public to drop the investigation. It would, of course, be excessively cynical to suggest that the lure of juicy Chinese orders for German exports and the approach of Federal elections had anything to do with that.

When the commission got around to proposing provision dumping duties on the solar panels earlier this year, most unusually, a majority of EU governments opposed them, though that was not a binding vote it was clearly not a signal of confidence in Commissioner De Gucht who then hastily settled for Chinese price undertakings rather than dumping duties. He is now visibly wavering over another planned investigation into alleged Chinese telecoms equipment subsidies after failing to get any European producers to support it. Indeed some, such as LM Ericsson of Sweden, have openly lobbied against it because they fear that it could lead to reprisals against their business in China, and the word that I hear is that under German pressure the investigation may now be quietly shelved.

So where next for EU–China economic relations? The immediate outlook I think is for a period of calm. Beijing craves external stability while it wrestles with the contentious economic reform plans and other big challenges on the agenda at home. It's fairly clear that Beijing considers Commissioner De Gucht, whose term in office ends next year, as a lame duck and it's counting on Berlin to stop him making trouble again. China has also given up pressing for the one really valuable prize that it wants from the European Commission, and it's in the commission's gift, which is market economy treatment in dumping cases which is economically very important to China, because Beijing knows that the EU must grant it automatically in 2016 under the terms of China's WTO's accession agreement.

The next major item on the agenda is planned negotiations on a bilateral investment treaty. The two sides' priorities here are somewhat different. The EU wants an agreement in order to improve access to China's market. China, on the other hand, is chiefly interested in protecting its investments in Europe. Those divergent positions could, however, narrow if Chinese economic modernizers see the EU as a useful ally in ratcheting up the pressure for domestic reforms, but if the EU is going to play that role effectively it will need

to stop acting like a pantomime horse and start behaving in ways that get China to take it seriously.

**Jonathan Fenby:**

Thank you very much, Guy, and I think the external/internal dynamic here, which I'm sure we'll come back to, is something that's going to be more and more important. Bernice.

**Bernice Lee:**

Well thank you very much and I'm delighted to be sharing the platform with so many old China hands, it's a real privilege in fact. What I would like to talk about today really focuses more on the dimension that I thought the two of you wouldn't cover, which is the prospect for the two sides' collaboration on global public goods like energy and climate security. About seven years ago now, or six years ago, we published a report here called *Changing Climates* and we, together with lots of Chinese and European institutions, argued for closer cooperation between the two sides. The argument at the time went as follows: that the two sides are already economically intertwined; that, as Guy pointed out, that EU was China's largest trading partner and the largest supplier of direct investment, technologies and also services; that the Chinese and the Europeans already have very similar policies on energy efficiency and on scaling up renewables, and the two sides also are very aware of the potential impact of climate change. The question then is whether or not the two sides could actually work together to become de facto low carbon engine for the transformation of the world economy.

Now, as we heard from both Guy and Kerry, obviously the bilateral relationships aren't all rosy all the time and that here have been many different disputes and problems, especially related to trade and investment. So where are we today after seven years? And there were lots of nice shiny things that we proposed; let's work on low carbon zones together, let's work on standards etc., etc., etc. Now where we are today is not as bad it sounds. In many respects the formal cooperation has been quite successful at the practical level – that our collaboration on developing carbon markets now in China that the EU strongly supports on urbanization projects, there are real changes that are being driven on the ground in China and possibly the EU because of this bilateral collaboration. But what is obvious is that despite the success at the practical level, at the political level or at the sort of the ground



admission level, the two sides are still very far apart and find it very difficult to find ways to turn this into something more practical in the global arena or in the international arena.

Now perhaps what is not helpful is economic crisis in the last couple of years, which, of course, made it even harder for the Europeans especially to basically derive political dividends out of this collaboration. In fact, they probably felt that its investment in China and in general in climate change had backfired including what happened in Copenhagen, and there's no question, as Guy intimated, that China doesn't really seem to be valuing EU-China relationship in the same way that it values the US-China relationship, and for whatever reasons, because it is actually quite substantive in terms of the discussions, it's not seen to be a political flagship from a foreign policy perspective. Now what I want to quickly talk about today is how despite the challenges and despite the fact that the two sides don't seem to see eye to eye when it comes to presenting themselves together as an alliance, there are many things or many justifications for the two sides to continue to work closely together on energy and climate change.

First of all, both are going to continue to be major consumers of energy and both will be importing a lot of it, and I think by our last count China will be importing and the EU will be importing some 80 per cent of its oil around the same time, and I should really check the numbers and I can't really see what I've written there. Secondly, as the two sides continue to face energy and climate changes both are turning to gas, and this is an area where obviously down the line it deserves some attention. EU's interest in natural gas has obviously grown partly because of carbon reasons, but also partly because of the shale gas revolution. On the Chinese side for the same reasons, partly because of air pollution moving closer and faster towards scares us also within the immediate horizon. So the question then becomes whether or not the two sides can actually come to some kind of understanding *vis-à-vis* gas in such a way that they can turn that into a competitive scenario and more towards an area where the two sides can work together to develop the next generation of technologies, partly because it is likely that within the immediate future, between 2020 to 2030, the two sides will likely scale up on this in addition to scaling up renewables.

And I think one thing I want to remind all of us is that despite all the talk of the trade problems, EU-Chinese trade relations have actually grown four times in the past decade and 50 per cent since 2008. And again, for all the talk of decoupling etcetera, etcetera, about I think 50 per cent, 40 per cent of exports from China is still destined for the EU and US and Japan, among others, and

therefore the collapse of demand from these economies had been incredibly problematic.

And the last thing I want to mention before I close the solar panel question: at the moment because of the politics of the trade side we forget that actually the low price of solar panels is the beauty in fact of interdependencies and collaboration, and I've talked about the story many times, but for those of you who don't know, the solar PV prices, the module prices have fallen 80 per cent since 2008 and 20 per cent since 2012, and this was absolutely made possible by a combination of European subsidies, Chinese manufacturing, European demand and now Chinese demand. In fact my good colleague had said recently, and I thought that's an interesting thought, that if indeed for the new energy generation the US contributed shale gas, in a very, very odd but actually meaningful way, the contribution from EU and China is cheap solar energy. It is the result of the two sides working together at the time when the climate was better in terms of trade.

So looking to the future, and since we have a EU-China summit coming up, I think what is important to remember is that this time round the Chinese actually have asked the EU to help commit to a 10-year programme on green growth. For the reason that I very briefly outlined, obviously we think that it makes sense for this to continue, but perhaps one thing to remember is that urbanization in China will attract or will need something like \$8 trillion of investment between now and 2020. This is the number – whenever we talk to businesses in the EU you can see them salivating, it's a huge number. No question there are market entry barriers, companies were telling us that they're often invited to do the planning for these big cities but they don't actually get the contracts to actually implement, all of this has to change. Now this is exactly where hopefully the EU-Chinese investment agreement that will begin negotiation in the fall will try and address.

And if I may close with one thought; obviously in Europe a lot of attention on trade has focussed on the bilateral relationship with the US and TTIP (Transatlantic Trade and Investment Partnership), but perhaps TTIP is indeed an opportunity too for Europe to think through what it could or could not achieve in a stronger EU-China trade and investment relationship. Why not put all the stuff that has been in discussion in the TTIP side, government procurement, fast tracking green goods, etc., onto a Chinese negotiation agenda? Why not actually use TTIP in some ways to potentially strengthen the negotiating hand when it comes to EU-China trade negotiation and I leave you with that thought.