*INSS Insight* No. 1427, January 14, 2021

# Europe and China: Surprising Conclusion to a Year of Problematic Relations

**Oded Eran**

**The European Union was careful not to identify with the United States in the struggle against China waged by President Trump on the economic front, against China's trade policy, and on the cognitive front in the demand to investigate and blame China for not preventing the COVID-19 pandemic. On the other hand, European Union leaders did not hide their concerns about Chinese aggression in the economic sphere, and even less so their criticism of China's policy on human rights and minority rights. The election of Joe Biden as President of the United States has increased the chances of a transatlantic front that will work to soften China's policy on these two issues. It is therefore surprising that the leaders of China and the European Union reached an agreement in the final hours of 2020 on a comprehensive investment deal. This occurred after years of long negotiations, and before the new US President enters the White House.**

The tension inherent in the relationship between China and Europe is related to values as well as interests. The two sides have a clear, partially shared interest in advancing their economies while exploiting their relative advantages in a fashion that is mutually acceptable, maintaining strategic industries, and protecting them. This tension is reflected in the definition of the relations with China ("EU-China – A Strategic Outlook," March 12, 2019), whereby China is a partner with which Europe shares similar goals; it is a negotiating partner with which the EU must find a balance of interests, it is an economic rival competing for technological leadership; and a system rival in advancing different forms of government. These require a flexible and comprehensive approach on the part of the European Union that enables protecting interests and values.

The tension between China and Europe has intensified of late, particularly in three arenas:

- China's policy regarding Hong Kong, individual liberties, and the rights of ethnic and religious minorities**:** The European Union criticizes China consistently for human rights violations. In December 2020 alone, five statements were issued criticizing China for the detention of journalists, including Zhang Zhan, who reported on the outbreak of the coronavirus in Wuhan. Josep Borrell, the High Representative of the Union for Foreign Affairs and Security Policy at the European

Commission, appearing before the European Parliament on December 17, 2020, criticized China's policy toward the Uyghur minority, the re-education camps established for them, and the suppression of the freedom of religious belief and worship in Xinjiang and Tibet. Borrell noted that in early December, the European Union adopted the Global Human Rights Sanction Regime, which allows the EU to impose sanctions on countries that violate human rights. In two summit meetings between the leaders of the European Union and China in 2020, the Europeans raised concerns about the human rights situation in China.

- China's policy toward foreign companies seeking to operate in China and the activity of Chinese companies in the advanced telecommunications, artificial intelligence and robotics, as well as strategic infrastructure: The European Commission's March 2019 document states that foreign investment in strategic sectors, the acquisition of critical assets, technologies, and infrastructure in the EU, and the supply of critical equipment could pose risks to EU security. In addition, the European Union established a "framework for screening of foreign direct investment," a non-binding framework for coordination. Only 15 members of the European Union have such a mechanism, but the lack of the mechanism does not reveal the approach of the member states to Chinese investment in sensitive areas, and the involvement of Chinese companies in the new communications infrastructure (5G) has become a central and problematic issue in the European Union's relations with China.

  In Sweden, for example, the government decided in October 2020, based on a recommendation by the security services, to bar Chinese companies Huawei and ZTE from bidding on tenders related to this technology. A Swedish court confirmed the legality of the decision on December 16, 2020. In contrast, in Hungary, where the mechanism exists, the government permitted Huawei's activity. Hungary is also active in the 17 + 1 Forum – a framework for cooperation between China and 17 countries in Eastern and Central Europe and countries bordering the Baltic Sea, which was established in Budapest in 2012 to support China's Belt and Road Initiative. In April 2020, China and Hungary signed an agreement for a Chinese lender to fund the railroad from Budapest to Belgrade, which will form part of the Budapest-Piraeus line. With the completion of the railroad, Hungary will be able to become the distribution center of Chinese exports to Europe, most of which arrive in the Port of Piraeus, which is controlled by the Chinese shipping company COSCO. In Greece itself, a mechanism for screening investments has not been established.

In Germany a developed screening mechanism is used in particular areas (energy, telecommunications, transportation, health, water, food supply, finance, and insurance). The obligation to report to the Ministry for Economic Affairs and Energy applies to every transaction in which an investor who is not within the European Union or the European Economic Area (which includes countries that are not members of the EU, such as Norway and Switzerland) intends to invest over 10 percent of the value of the asset or project. The German screening mechanism can also disqualify transactions that entail possible harm to public security and order in Germany and in another EU member. On December 16, 2020, the German government submitted a bill to the Bundestag, "Information Technology Security 2.0," whereby more powers would be granted to the government to screen suppliers to the government and to essential systems, and to inspect the designated equipment on two levels – the level of security risk and the reliability of the supplier. The final arbiter would be the Chancellery. Germany's omission of the names of specific companies and/or countries in the proposed law – unlike Sweden and the UK, which mentioned the names of Chinese companies – sparked a wave of analyses that Huawei would be able to compete in the German market despite the Trump administration's pressure on many governments to prevent this.

- World public opinion and China's struggle against the narrative heralded by President Trump, namely, that the Chinese government is responsible for the COVID-19 pandemic. China resisted this accusation aggressively, including vis-à-vis official and senior position-holders in Europe, and claimed that it acted with full transparency and shared knowledge and medical aid around the world. During the first half of 2020, official figures in China and Europe hurled accusations at one another of conducting a disinformation campaign. China's image in European public opinion was damaged, as indicated by public opinion polls. According to the Pew Research Center, between 2002 and 2020 the number of people holding negative opinions of China more than doubled in the ten polled countries in Europe. Over 70 percent of respondents expressed distrust in Chinese President Xi Jinping (although more respondents expressed distrust in President Trump.)

The comparison between the level of distrust in Europe toward the leaders of China and the United States, the world's two other economic blocs, is relevant to the discussion. Despite the rising concerns in Europe about China's increasing economic aggressiveness and the criticism against it expressed at the highest levels of government for its suppression of human rights and minorities, the leaders of Europe were careful not to identify with the struggle waged by the Trump administration against China – even though the same issues were in dispute between the European countries and China. The European reluctance toward comprehensive dialogue on central international issues was replaced by the

proposal (European Commission document from December 2, 2020) to the incoming Biden administration to engage in dialogue with the goal of global change. Among the main topics in the EU proposal was working together to tackle the strategic challenge that China poses to the EU and the United States.

Against this backdrop, the announcement by China and the European Union on December 30, 2020 that they had reached agreement in principle on a "Comprehensive Investment Agreement" was a surprise. The full text of the agreement has not yet been released, but the European Union publicized its main components, including China's waiving limitations on European investment in certain spheres and the need for a Chinese partner for a European venture. In the vehicle manufacturing industry, for example, China agreed to gradually waive European manufacturers' need for a Chinese partner, and it will provide free access to the market for vehicles powered by renewable energy. The cancellation of the need for a Chinese partner also applies to the establishment of private hospitals in five central Chinese cities, including Beijing and Shanghai; the establishment of real estate agencies; translation services; and environmental services (solid waste removal, sewage, and landscape and nature conservation). The agreement allows European investment in companies engaged in the transportation of sea cargo, container terminals, and freight transport agencies. European companies will be able to invest in aviation-related enterprises, such as ticketing and handling air freight. The agreement subjects governmental companies to a system of economic considerations in order to prevent discrimination during the acquisition of products and services, and requires that China provide information upon request regarding the actions of specific companies on these issues. The Chinese government, for its part, commits to transparency in the provision of subsidies in the service sector that could hurt European investors in China. The agreement sets clear rules for preventing the transfer of information collected by the authorities in the country in which the foreign investment takes place. In addition, it sets rules to prevent coercion to transfer technology by the investor.

The contents of the agreement were not surprising, mainly because they were made public after most of the rounds of negotiations, which took place over the course of more than seven years. What was surprising was the timing of its conclusion – three weeks before the inauguration of President Biden, with whom the European Union expressed desire to formulate a joint response to the Chinese challenge – as well as the European willingness to grant China a substantial achievement when it is under political-public relations pressure, that is, an agreement that does not include Chinese concessions related to issues fundamental to the survival of the regime – its control of the economy, policy, and defense.

European Union leaders could encounter domestic criticism regarding these aspects of the agreement. Chancellor Angela Merkel, for example, could face criticism due to her

willingness to sacrifice central European values in return for the interests of the German vehicle industry. The European Council's announcement on reaching the agreement mentioned the phone call held on December 30 between China's President and the Chancellor, the President of France, and the heads of the European Union. After a long description of the EU's achievements, a single sentence appears regarding Europe's concerns about the human rights situation in China. This sentence will not be enough to fend off criticism within Europe and from Washington.

It is difficult to assess whether the agreement will serve as a precedent for other countries too, including Israel. Canceling the requirement from foreign investors for a Chinese partner in certain industries and projects could lighten the process for Israeli investors and prevent the transfer of technology through coercion. However, transatlantic agreement on defining and demarcating the risks stemming from working with Chinese economic entities would reduce China's ability to maneuver vis-à-vis different countries and provide them with international umbrella protection. Conversely, the lack of transatlantic coordination on addressing the challenge posed by China would leave Israel and other countries caught between political pressure from Washington to reduce cooperation with China and a desire to enjoy the economic fruits of cooperation and political dialogue with it.