The Growth of Economic Relations between China and the European Union

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Over the last decade, trade between China and the European Union has grown by an annual average of 8 percent. Nonetheless, both sides feel they are far from exhausting the potential for economic cooperation. Recent economic crises, decelerated growth in China, and President Trump's sharp reversal of traditional US international policies are some of the factors impelling leaders on both sides to expand trade. At the same time, the forces urging cooperation face several difficulties, including issues of fair competition, intellectual property protection, and market access. An even greater fundamental obstacle is the EU's concern over Chinese political influence in the European continent, stemming from the dominance of government-owned Chinese companies as well as the scope of Chinese investments in the EU, especially ownership of critical infrastructures.

This paper examines the development of economic relations between China and EU states over the last ten years and asks what Israel can learn from this experience. It begins with a short survey of the political and economic changes over the past decade to the three largest economies in the world: the United States, China, and the EU. It then examines the development of economic relations between China and EU states and the difficulties facing all parties in maximizing the economic potential inherent in cooperation. The last part of the essay probes what Israel can learn from the economic cooperation between China and the EU states.

Background: Economic and Political Changes to the Large Global Economies

The last decade has seen political and economic changes that some thought would lead to a new world order. They include economic crises (the global

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financial crisis and the euro crisis), Brexit, Donald Trump's foreign policy, and China's ascent to economic dominance.

The economic crises damaged Europe's economy, sparked tensions and disagreements among EU member nations, and resulted in the need for money and investments, especially among states on the EU periphery. They also led to the oft-cited claim that the root cause of the growing economic inequality is globalization. The 2016 British decision to leave the EU heightened concern that other nations would follow suit and that the EU might disintegrate altogether. EU leaders are working extremely hard in preventing such a domino effect, in formulating an agreement between the parties, and in implementing reforms following Britain's exit.

In the United States, President Trump is spearheading a change in the US role in the global order. His foreign policy, even if not always translated into practice, is nationalist, anti-global, protectionist, and at times isolationist.[1] The President decided that the United States would withdraw from the JCPOA, the Trans-Pacific Partnership, and the Paris climate accord; he also decided to impose protective tariffs. These are but some of the decisions pointing to the changes in the world's largest economy that have led to a loss of much of the trust the United States enjoyed in the international arena. The United States is increasingly seen as an unreliable partner.

China, one of the world's three strongest economies, is experiencing economic and social changes that affect its power and status in the international array of forces. China's economy – even after the slowdown – is growing faster than the global average. This growth is based on an expanding wealthy middle class and an increase in local consumption of goods and services. Investments around the world – especially in Europe – are skyrocketing; in fact, by 2020, China is expected to be the biggest investor nation in the world. In 2016, its global investments totaled $200 billion, a 40 percent increase compared to 2015.[2] At the same time, China faces challenges in making the complicated transition to a new economic model that stresses market freedom, innovation, growth, and more.[3]

These transformations are part of an increasingly heated debate over the future of globalization. Some see the start of a retreat toward national economies and the beginning of challenges to international trade and investments. Has the change in the US position pushed the EU into China's arms, opening the door to stronger relationships on a range of issues? While the US signals its intention to act unilaterally and independently, the EU and China have a shared view on the importance of a multilateral regime calling for collective action. For example, in 2018, the Chinese ambassador to the EU called on the sides to take an anti-protectionist stance,[4] and in 2017, the EU's High Representative for Foreign Affairs and Security Policy noted that in times of increasing tensions and geopolitical uncertainty, EU-China cooperation had never been as important as it was now.[5]

The Development of Economic Relations between China and EU States

Trade Relations

Once diplomatic ties were established in 1975, China-EU relations developed rapidly. Especially after the signing in 2013 of the EU-China 2020 Strategic Agenda for Cooperation, cooperation in every possible sphere – trade, peace, climate, human rights – grew exponentially and made the EU and China highly interdependent.[6] The spheres of cooperation stress the EU's and China's expanding roles and responsibilities as global actors, as well as their willingness to continue to broaden their overall strategic cooperation, based primarily on trade and investments.

The EU is China's biggest trade partner, and China is the second largest of the EU's trade partners. Trade relations grew in particular after China joined the World Trade Organization, reaching 573 billion euros in 2017, compared to 306 billion euros in 2007. Similarly, the EU and China are one another's largest import source and second largest export destination. In 2017, China represented 20.2 percent of EU imports, and the EU represented 13.1 percent of Chinese imports. In terms of services, EU exports to China are equivalent to 22 percent of its export of goods, but this rate is only 8 percent of Chinese exports to the EU.[7]

According to a 2025 forecast, China's economy is expected to be 10 percent larger than the EU's (had Great Britain stayed in the EU, the EU's economy would have remained larger). Similarly, annual trade is expected to reach 678 billion euros, focused primarily on services and investments, and could improve as part of the One Belt One Road (OBOR) initiative.[8] Once OBOR is completed, the EU can expect to see a 6 percent increase in trade.[9]

China Buys Europe: Chinese Investment Trends of the Last Decade

Between 2008 and 2018, China acquired and invested some $370 billion in European assets. Since 2014, there has been a clear increase in the overall value of Chinese deals in Europe, peaking in 2016. Chinese investments in Europe in the last decade are 45 percent greater than Chinese investments in the United States. More than half the transactions were completed in Europe's five strongest economies; in Great Britain alone, China invested some $70 billion.

Since 2008, some 360 European companies have been sold to Chinese owners, including tire manufacturers, aircraft makers, wind farms, seaports, airports, hi-tech companies, soccer teams, and more. Some of the acquisitions are staunch symbols of EU member states, such as the Italian tire company Pirelli, the Inter Milan Football Club, and the Swedish vehicle manufacturer Volvo – sharp reminders of China's tremendous purchasing power. Moreover, some of China's buying spree includes infrastructure projects, such as an English nuclear power plant and interest in future transactions involving Romanian and Bulgarian nuclear reactors, the construction of a new Swedish seaport, the acquisition of an Irish gas and oil manufacturer, and more.[10]

Obstacles to EU-China Economic Relations

Along with the economic benefits, trade relations between the EU and China face various problems; these are intended to be resolved through the efforts of more than 60 working groups and joint dialogues. Of the gamut of topics hindering trade development between the sides and investment agreements, there are three principal issues: the lack of fair trade with the EU market; the lack of intellectual property protection; and the degree of access by Chinese companies to the EU market.

The EU complains of unfair competition because of the role played by the Chinese government. Many Chinese companies investing in Europe are either owned or largely financed by the Chinese government, and consequently have an advantage over their competitors in the EU with easy access to enormous amounts of cheap money with which they can aggressively acquire attractive assets all over Europe. The lack of competitive parity is compounded by the claim that Chinese manufacturing overruns are exported to the EU at prices far lower than what EU companies can compete with.[11]

Another problem concerns China's standards of intellectual property protection, which differ significantly from those of the EU. This is manifested in two ways. In EU exports of technology and intellectual property, EU companies charge that their intellectual property is insufficiently protected; they fear that their technologies will be replicated in local Chinese factories. This concern has become more acute since 2016, when Chinese acquisitions and investments in the EU included access to intellectual property.[12] In terms of importing Chinese technologies to the EU, EU data indicate that China is the leading nation to sell goods while violating intellectual property rights.[13]

At present, access to markets is the most trying strategic issue in terms of EU-China trade. While China claims that EU standards – e.g., on human rights, intellectual property, and technology – harm its ability to invest in and sell to the EU, thus in practice limiting its market access, the EU disagrees. The EU is troubled by the local market being overly open, manifested in the fact that China can do business as it pleases in all EU nations in a liberal market economy and under fair trade conditions, allowing China to acquire technological companies, chemical manufacturers, and national infrastructures.

The scope and nature of China's buying spree in Europe over the last ten years has finally sounded the alarm among EU leaders. The preoccupying theme is the potential for political influence that these acquisitions wield, a concern stemming both from the presence of Chinese government-owned companies in acquisitions all over the EU and from the acquisitions themselves – strategic national infrastructures.

In the last decade, of the 670 entities investing in Europe, 100 are owned by the Chinese government and are responsible for transactions whose total value is $162 billion, i.e., 63 percent of reported transactions. Furthermore, eight of the ten largest deals were carried out by state companies or companies financed by the state. These figures underscore that companies owned or financed by the Chinese government dominate the acquisitions and investments scene in the EU. It has been said that there is no such thing as a purely private company in China; in some way or another, all companies are connected to the government and the Communist Party.[14] EU leaders are troubled that some of these deals may be motivated by non-economic factors and represent political and/or security threats. For example, the Chinese company CEFC, which only in 2017-2018 invested more than a billion dollars in the Czech Republic, has close relations with the Chinese government. In exchange, the Czech president has become a huge supporter of China, pledging his support for China's claims against Taiwan.[15]

The concern about political and security influence grows more acute given the acquisition of infrastructures, especially in the context of OBOR.[16] The concern stems from the Chinese government's involvement, whether by outright acquisition of infrastructures or by the provision of financing, and from the fact that these are critical infrastructures that could serve China as leverage to increase its political influence in Europe and dictate the spirit of the Chinese regime. China has stated that it does not intend to use OBOR to further its political or military influence,[17] but given China's lack of transparency and the very nature of the initiative, world leaders are skeptical regarding China's goals vis-à-vis the various nations through the project.[18]

In the past decade, China has made countless investments in critical infrastructures. It has acquired many seaports in France, the Netherlands, Belgium, Spain, Romania, and Greece, so that Chinese government-owned companies now hold one tenth of the capacity of European ports. The massive acquisitions of ports raise the concern that China is gradually seizing control of Europe's naval portals, jeopardizing the continent's security.[19] Similarly, the transfer of the Greek port of Piraeus into Chinese hands is an example of China's political influence: Greece supported China, choosing not to join in the EU's censure of China for human rights violations. In addition to the acquisition of seaports, China is buying other critical infrastructures, such as gas and energy companies, roadworks companies, and more. Portugal, for example, approved the sale of its largest energy company to a company owned by the Chinese government. China established the 16+1 Global Partnership with central and eastern European nations to increase Chinese investments there, especially in infrastructures and technology. This too is cause for concern that these nations, starved for funds and investments, will change their positions on China and support its policies. The fact that China owns the national infrastructures of EU member states will yield it political influence in those nations.

The rate of China's expansion into critical sectors of Europe's economy has caused EU leaders to call for joint action. It seems that a united European front does not top the agenda of the EU's most vulnerable, investment-starved members. In Portugal and the Netherlands, for example, political leaders have announced that they fear losing Chinese investments and can therefore not support a selective investment mechanism.[20] By contrast, Germany, France, Italy, and Great Britain are calling for a way to screen foreign investments for all of Europe. By the end of this year, these nations will have decided on significant steps to protect critical assets against foreign investments.

In July 2018, Germany blocked two Chinese intended acquisitions: one of Germany's largest electricity operators, and a metals company contracting with the aerospace and nuclear industries. Denial of the acquisition of the metals company – the first such instance in Germany – was justified on security grounds. In addition, Germany has instituted foreign investments reforms and established that the government may undertake a security analysis if the foreign investor wants to acquire 25 percent or more of a company. The sectors included in this provision include critical infrastructures, energy, technology companies, transportation companies, and more. Recently, some have called for more stringent protections against Chinese investments and for reducing possible purchase by a foreign entity to 10 percent. These calls demonstrate a German consensus: fear of China's deep pockets and its industrial and political ambitions.[21]

France, Italy, and Great Britain likewise support a way to screen foreign investments more closely and expand the list of sectors subject to intervention to include technologies, artificial intelligence, aerospace, and the financial sector. President Macron temporarily nationalized the French technology company STX out of concern that technology would leak into Chinese hands. France is also working on shifting the authority to screen investments from the Finance Ministry to the presidency. Italy too is using newly legislated authority: it blocked the transfer of military technologies as part of the sale of Piaggio Aerospace to a Chinese government owned company. In Britain, several bills on national security and investments are currently being debated; these would cover security threats connected to intelligence activities and critical infrastructures.[22]

In tandem with legislative moves by individual EU member nations that support a European mechanism to screen investments, the European Commission is promoting an initiative to establish an investment mechanism that is supposed to be approved by the European Council before the end of the year. The plan includes an expansion of the sectors subject to screening, including ports and infrastructures, clearer definitions of critical infrastructures and technologies, attention to investments by foreign governments, and more. Similar developments are underway in Australia, Canada, Japan, and the United States.[23] Until such a mechanism is established, EU member nations will find it hard to reach a consensus on developing a united strategy on China; it might even lead to an EU split on policy toward China.

What Israel Can Learn from EU-China Trade Relations

In 2017, Israel-China trade was valued at $10 billion, a 6 percent increase over 2016.[24] While this does not come close to the scope of trade between China and the EU, there is a similar trend on the part of both Israel and

China to further trade relations. In recent years, China made some important acquisitions in Israel: it bought Tnuva Dairies, the electronics company Servotronix, and the cosmetics company Ahava. Chinese investors are looking to invest in Israeli innovation, especially technology. Alibaba, for example, has invested in several Israeli companies, and a consortium of Chinese companies acquired Playtika Ltd. for several billion dollars.[25] Also, as part of the OBOR initiative, China is moving into Israeli infrastructures, and is involved in roadworks, the light rail line, the Carmel tunnels, the Ashdod seaport, the operation of the Haifa seaport, and more. Nevertheless, the potential of Israel-China trade is far from maximized. In this context, some economists urge Israel to increase the number of Chinese investments in Israel; others warn against embarking on full-scale cooperation before having an orderly strategy in place.

By virtue of being a technological and innovation powerhouse (eleventh on the world innovation index, immediately after the ten most innovative nations in the world, eight of which are European),[26] Israel must be particularly vigilant about intellectual property protection and closely examine the types of investments and acquisitions by foreign companies, including Chinese. While the Foreign Trade Administration in the Ministry of Economy is aware of concerns about intellectual property rights violations and is working on this issue, mainly through trademark regulation, patent protection, posting a special attaché for regulatory matters (China is the only nation where Israel maintains a special regulatory affairs position), and more,[27] there is still not enough regulation to help protect Israeli intellectual property.

As evident from the EU's experience, the acquisition of critical infrastructures in Israel could also have political and security influence.[28] Chinese entrenchment in Israel through the acquisition of a railway line or seaports could enable China to hamstring Israel and limit its freedom of action in making political decisions with implications for its relations with China.[29] Thus, for example, transferring the management of the Haifa port to the Chinese casts a political shadow over Israel – China now controls a critical Israeli infrastructure, which could potentially be used to apply pressure to Israel should it damage Chinese interests. It also incurs a security issue, as an Israeli Navy base is located near the port, which gives the Chinese proximity to Israel's military activities.[30]

Israeli media recently reported that the government is looking to establish an investment screening mechanism to supervise foreign investments in Israel. Presumably Chinese investments would be the focus of such a mechanism.[31] Because such a mechanism is being formed in the EU and can be expected to enter into action before year's end, Israel can learn from this legislation and decide if and what to implement. In tandem, Israel can learn from the nations that are already implementing legislation to screen investments at the national level, including limiting the percentage of control a foreign company can have in a local one (as Germany did), expanding the list of sectors subject to an investment screening process so as to include technology and infrastructures (as did France, Great Britain, and Italy), and examining the source of the investment to discover if a foreign government is involved. These steps taken by European nations, based on their cumulative experience in cooperation with China, could help Israel learn from the European experience and support a decision making process on Chinese investments in Israel.

Notes

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