



# PAPER

## Working

### **Towards an EU-China Partnership**

**Dai Bingran**

Abstract: It only needs a common sense to arrive at the understanding that China, the largest developing economy, and EU, the largest developed economy, should commit each other closely in economic exchanges and cooperation. The common challenges and shared interests between them at the moment verify this need and possibility. And, in spite of some difficulties, there exist wide scopes for further cooperation upon the solid basis built up in the past few decades.

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## China-EU Economic Relations

**Dai Bingran**

It only needs a common sense to arrive at the understanding that China, the largest developing economy, and EU, the largest developed economy, should commit each other closely in economic exchanges and cooperation. The common challenges and shared interests between them at the moment verify this need and possibility. And, in spite of some difficulties, there exist wide scopes for further cooperation upon the solid basis built up in the past few decades.

### **1. Cases for closer economic ties: common challenges and shared interests**

One of their common challenges is the accelerated process of economic globalization. Whether you like it or not, economic globalization is a natural course and destiny, inevitable from the science and technology advancement and economic-social development. When in a flick of the minuet, huge amounts of capital can be transfer to the other end of the earth for transactions just concluded through computers, and when with outsourcing, a company does not need to build a workshop or factory any more to take the advantage of local resources and market, economic operations are truly running out of the national boundaries, and have to be planned and carried out against a global environment. In macroeconomic terms, the marked acceleration of factor movements brought about by globalization entails competition at international level, worldwide reallocation of resources, shortened business

cycles—just to mention some of them—which every economy has to reckon with seriously. Issues of international scopes and implications have to be dealt together by the major players, including China and EU. Globalization has also created new opportunities, which are likewise better exploited through common efforts.

Another challenge is a lesson that we all should drawn from the current financial crisis: Against the changes and developments in the past few decades, the existing international institutions are no longer capable of dealing with the new situations and problems, such as financial stability and security, food and energy supply, climate change, etc.. Reform of the old order has proven and shall prove to be as difficult as the setting-up of new ones, and as stakeholders China and EU have the strong case for cooperation.

Against this general background, China and EU also have had their specific interests to strengthen their mutual economic ties. China's transition and transformation is still far from accomplished. In spite of its recent fast and tremendous developments to become No. 2 in the world in terms of gross GDP and No. 1 in exports, it is still very much underdeveloped in many respects, for instance, in terms of GDP per capita, it ranks still well behind the 100<sup>th</sup>, that is, far behind the world average. More importantly, it is still faced with a series of problems and impediments, such as development and distribution disparities, unemployment and employment, environment deterioration, etc. which impose as serious bottlenecks for its future development. So the Chinese economy may still be termed as “a giant with clay feet”, imposing but in danger of sudden collapse. For its further development,

and more importantly for the transformation into a better development pattern, it depends heavily on a favourable external environment, of which EU remains a very important part. The EU and its member states have contributed greatly as its suppliers of goods, investment, technology and management experience. In its course to become “medium well-off” around the middle of the century, such contributions will be indispensable as well. So, to continue and strengthen its economic ties with the EU and its member states is to its vital interests.

To EU and its member states, continued economic partnership is likewise essential. In the last few decades, EU passed an important stage in deepening and widening its integration process. Meanwhile, its economy is also faced with the structural adjustment—the transformation from a manufacture-based economy developed during the post-war periods into a post-industrial one base on IT. If we look at the economic performance of the EU and its member states in the recent two decades, records well indicate that they mostly lag behind with the US in this transition. The main two symptoms are the sluggish growth<sup>1</sup> and high unemployment, but behind are the drop in labour productivity and the lag in economic competitiveness. To revitalize its economy, the EU has been pushing for the Lisbon Agenda in the last decade and the Europe 2020 for the next decade. To fulfill the modest objective “for smart, sustainable and inclusive growth” of the latter, the essential element would be an upgrade of its economic structure, towards an industrial composition favourable for growth and employment. It is just in this respect that China can contribute. As the largest and most

open developing economy, China has been attracting large-scaled foreign investment especially from the developed economies, and becoming, therefore, the production base of a large proportion of the labour-intensive manufactured goods. In this wave of industrial reallocation, the ‘made-in-China’s not only supply the developed economies with cheaper consumer goods, but also cheaper intermediate products to sustain growth and employment as well. More importantly, by moving into China and other developing economies those industries that could no longer produce competitively there, the developed economies are able to release resources for the development of the “industries of future”. In this spiral cycle of world economic development, China may not be the driving force, but is certainly an essential link.

To sum up, there is indeed a strong case for close economic ties between China and the EU: the interests and benefits are mutual and reciprocal, rather than one-sided.

## **2. Analyses of the current status and issues**

In the 35 years after China and the EU established diplomatic relations in 1975, and especially during the past 15 or so years, China-EU economic relations grew very rapidly and have reached a quite high level. The most conspicuous indicator is that the EU is now China’s NO.1 trade partner, accounting some 17.3% of its external trade in goods in 2009, and China is EU’s No.2 trade partner, accounting 12.9% of its trade in goods with the outside world in the same year. Besides, EU is now the NO.1 technology transferor to China and NO.4 investor<sup>2</sup>, and maybe also the largest provider of development aid. China-EU

<sup>1</sup> In most years its GDP growth rate is at least 1% less than the US’ during the period.

<sup>2</sup> NO.2 if not include Hong Kong and Taiwan

economic relations suffered from the financial crisis, but remained relatively stable as against their relations with other partners, and the first few months of 2010 registered a marked recovery<sup>3</sup>. It also should be noted that during the difficult time of the financial crisis, China's financial presence and involvement in Europe creased markedly, in terms of both investment and monetary cooperation. We do not need to cite more figures to understand that their economic relations have reached a quite high level of interdependence which neither could afford to neglect. To keep them up and push them further are to their mutual vital interests, and the only option.

It is true that during the past decade of rapid growths, disputes and conflicts increased as well. The top issue in their bilateral economic relations seems to be the trade imbalance, that is, the rising trade (in goods and services) surplus of China against the EU, which reached its peak in 2008 to 164.7 billion of Euro as against the total trade volume of 361.2 billion<sup>4</sup>. It is indeed an imbalance, which needs to be addressed. Protection measures to limit imports from China are certainly not the right way, as they will be at the expenses of the European consumers and industries alike. A better approach is for China to import more from Europe. Here the key issue is EU should export what China needs to import. The comparative advantage of Europe is in high-tech products; if the EU could be more open in this respect, with the higher added value of these products, the imbalance would be easily addressed.

Having suggested this, it might be still interesting to see how this imbalance comes

about and what is behind it.

Just as was mentioned before, China's opening-up in the late 1970's and especially its entry into the WTO around the century happened to fall in with the world-wide industrial transfers driven by the economic globalization, in which manufacture industries moved out of the developed economies and into the developing economies seeking for higher marginal profits. China became a preferred choice with the transnational world over, because of its political-economic-social stability, cheap labour costs, and huge market potentials; they came to settle down in China, and turned it into a huge "workshop", where they manufactured through importing a great part of the raw materials or semi-products, and exported as much as they could to the world markets—a greater part to the US and Europe, as most of such goods were no longer produced there, or rather could not be profitably produced there. As trade is often the function of investment, the Chinese trade surpluses should be looked together with the investment profits of the foreign firms that created a by far greater part of China's exports.

For a deeper analysis, there is the question of what China gained in this course? There are benefits in connection with employment and living of its huge surplus labour, tax revenue, technology and management improvements, development of the supporting industries and services, etc. These are essential for the recent development of China, which it could not get otherwise. On the other hand, being the No.1 producer, China has also become the No. 1 energy and raw material consumer, and consequently the No. 1 plaintiff for pollution and climate change. At the moment, with its some 7% of world's GDP, China contributes

<sup>3</sup> From Jan. to April, bilateral trade increased 34.6% as against the same period last year.

<sup>4</sup> EUROSTA statistics, but much less in Chinese statistics due to different calculations.

more than 16% of world growth. That does mean: China is not just producing for itself; the consumer has a share in pollution as well as the producer. And there are other charges. For instance Chinese exports are often blamed for the bankruptcy of European industries and unemployment of local workers. The plain fact is: were such industries not squeezed out of production by Chinese exports, they would be driven out of the markets by exports from other developing economies anyway; this is the working of the law of economics. On the other side, cheap Chinese exports, in addition to keep down the consumer and producer prices in Europe, might also help to cut energy and raw material consumption and to save resources for developing clean industries.

Of the trade disputes, China's main complaint is on EU's anti-dumping measures. Since the 1990's, China is by far the NO.1 sufferer of the EU's anti-dumping measures, and the main cause is that the EU has not given China the so-called market economy status (MES). Because of that, when determining whether there exists dumping, the exporting prices of the Chinese exports are not compared with their domestic prices, but with the prices of the similar goods of a country with established MES, which could, for instance, Norway, Canada, Japan and US. In this way, many of the Chinese dumpings are calculated rather than real.

According to the GATT rules, the solely criteria of the MES is whether the domestic prices of the country are determined by the market, and has nothing to do whether a country is a market economy in economic terms. With more than 95% of the domestic prices determined by the market, China is very much qualified for a MES, but the leading

developed economies including the EU still refuse to give China this status. It is OK, as China agreed to a no-change of it in 15 years when it joined the WTO in 2001. The question is while the EU refused a re-consideration to China's application in 2004, it gave Russia the status. China is not in the least against the EU giving Russia such status, but in so doing there is apparently double standard, and even discrimination. 2016 is not very far away when China will automatically enjoys that status, but the dark spot of the unreasonable refusal may remain longer in the Chinese people's hearts.

Another much talked issue is that of RMB's exchange rate. At the moment, the USD is still the most used international currency, so the pegging of RMB to USD is a Chinese choice when there are no better choices. The issue of RMB vis-à-vis Euro is, therefore, very much that between USD and Euro. And in these years, RMB has appreciated against USD more than 20%. China resists the pressure for a drastic appreciation, as it has the fragile domestic stability to consider. Both the East-Asian financial crisis in 1997 and the current international financial crisis have proven that such caution is not a wasted effort, and the disturbances in the Chinese economy will not be a gospel to others.

Other main issues on the agenda include: market access, intellectual property, investment treatment. China is often criticized for insufficient openness of its services markets. It might be true, and there are domestic outcries as well to make them more open, as it will introduce the competition needed for further reorganization of its financial sectors and markets. But in so far as China has creditably fulfilled its WTO obligations in this respect, further openness of its market is a matter for

bilateral and multilateral negotiations and compromises, rather than one for unilateral pressure.

Intellectual property right is also an issue frequently coming up in China-EU economic relations, and there are complaints that foreign firms have been reluctant to sell patents to China, for fear of being copied afterwards. In this respect, there is the international jurisdiction, which should be able to take care of serious violations and apparent copying and imitations. On the second thought, intellectual right is not to prohibit renovation and innovation, and the best protection is to upgrade the patent.

There are also complaints saying China is tightening its control over external investment. To those, the Chinese Premier made a denial himself recently, showing how seriously the matter is taken care of. On the other hand, it might be true that China is gradually moving towards the principle of equal treatment. For one thing, it is for fair competition, and for another, to pave the way for a more rational industrial policy.

Trade disputes mentioned above are but normal, oft related to the closeness of the relationship and the increase of the exchanges. The EU and the US are constantly at trade wars, but that does not affect, nor cause people to deny, their close alliance. The trade disputes between China and the EU are not insurmountable. The important thing is to treat them as such, and not to politicize the disputes. By sitting down in serious negotiations, solutions could usually be found through compromise.

### 3. For deeper and wider cooperation

In spite of the apparent difficulties and

disputes, the Chinese and European economies are more supplementary than competitive, as they are still at different stages of development. And for all the rapid growths these years, China EU economic exchanges and cooperation are far from exhausted, and there remain large scopes and potentials to be explored and developed. For instance:

--financial cooperation: In the financial sector, Europe is much stronger than China. The introduction of foreign competition is just what China needs for further reform of its financial services and markets. The current international financial crisis should provide some new impetus for China-EU dialogue and cooperation into the future.

--monetary cooperation: Many of the current international financial disturbances are rooted in the contradiction between Dollar's international usage and its sovereign issue. Cooperation between China and EU, between PBC and ECB and between RMB and Euro may still be a political issue at the moment, but its successful development will certainly be a stabilizing factor of great economic implications.

--energy cooperation: China is bound to be the world's NO.1 energy consumer sooner or later, and that has caused great concerns both at home and abroad, especially as it is linked to the issue of climate change and environment protection. Europe is much more advanced in energy saving, green energies, etc. Increased technological cooperation and assistance in this area will be beneficial for both and the world at large, and with great economic implications as well.

--transportation cooperation: This is another cooperation area of tremendous potentials, covering equipment production, technology

transfer, construction projects and management. And their cooperation might even give them an edge in the international markets.

--tourist and cultural cooperation: Both China and Europe are rich in natural, historical and cultural attractions, and this is an area where consumption potentials are always rising. To realize the potentials, both sides need to make the markets more open and to provide better information and better services.

--education cooperation: This has also an economic aspect, and education cooperation is an investment into the future. Europe enjoys here a big advantage in attracting the Chinese students, if only the language barrier could be lowered.

--government procurement: If China and EU could negotiate and reach an agreement in this area, the gradual opening of the markets

will yield tremendous economic benefits for both by bring forth their comparative advantages.

--cooperation between the small- and medium-sized firms: As both sides have large numbers of such firms, the creation at the government level of a joint mechanism, including a service agency and a fund, to facilitate and support such cooperation would open a new horizon in China-EU economic cooperation.

These are just a few areas where China and EU could work together to deepen and widen their ties, but it does show that there are between them more than just trade to think about.

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