EU-China Hub

Monthly Report

APRIL 2020

YOUR MONTHLY REVIEW
OF KEY EU-CHINA NEWS

About EU-CHINA HUB

We are a Brussels-based, private, non-profit initiative pushing forward dialogue on EU-China relations.

Given China's rapidly rising importance on the global stage, it is now more important than ever for EU-China relations to be better understood not only by an inner circle of professionals and enthusiasts, but also by politicians, business people, and the general public.

This is especially true as Europe struggles to embrace the complexity of its relationship with China as a partner, a competitor, and a rival.

We aim to break down this complexity in a digestible format by aggregating the key EU-China news stories and interviewing important players directly involved in EU-China relations.

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APRIL 2020

Welcome to the first Monthly EU-China Report!

In this format, paired with an audio version coming to "EU-China Podcast", we bring you a digest of the key trends of EU-China relations. This way, you can be sure that you can keep up with the key EU-China happenings of the month, even if you have to go on a few days of news and Twitter detox or miss any of our weekly EU-China Briefings.

April brought many tensions between the EU and China, all at a fragile time during the "corona crisis". Much of this is owing to China's deployment of a new, more aggressive "wolf warrior" diplomacy style paired with disinformation campaigns. And while the low-key diplomacy with a carefully defined single Party-line is not gone, it is telling that China made a significant shift in its communication strategy.

Confident Beijing doesn't need wolves, but the Party leadership has reasons to feel cornered. China's economic outlook is challenging, to say the least, given the contraction of the Chinese economy in the first quarter of the year - the first since comparable data have been recorded. It is hard to expect a smooth bounce back similar to that following the SARS pandemic of 2002-2004, with a global demand shock looming on the horizon. At the same time, Beijing can't just throw money at the problem, as it did after the Global Financial Crisis of 2008, since the country's debt is so high, particularly within shadow banking. On top of that come external challenges like the international controversy surrounding COVID-19 or the prospect of supply chains being at least partially diversified. This is not to say that Beijing is on the edge, but it surely isn't the best of times, and turning to nationalistic messaging and looking inwards shouldn't be surprising.

China's more aggressive communication style and disinformation campaigns encouraged many European leaders to push back against Beijing. Granted, they have done so in a toned down, non-confrontational way, which some wouldn't see as push back at all. But here we need to consider that the EU is trying to develop a framework for a multilateral response to the threat of COVID-19 under the circumstances of growing Sino-American rivalry and considering the EU's current dependence on imports of medical supplies from China, which the Party-State seems to be ready to weaponise in its foreign policy.

Still, the response went beyond rhetoric. We could see EU leaders beefing up mechanisms for protecting European companies against takeovers by non-EU actors, calls for diversification of supply chains, as well as for international investigation into the origins of COVID-19. While controversies were stirred up by the alleged watering-down of the EEAS's report on disinformation, it appears that the circumstances increase the pressure on Brussels to acknowledge that it has been "a little naive" about China. What we are seeing may be the groundwork being laid down for a wider "China rethink". Don't expect it to happen just yet, given the circumstances just outlined, but returning to "business as usual" may not be so likely after the pandemic.

Enjoy and stay safe!

Grzegorz Stec
Founder of EU-China Hub

EU-CHINA INTERVIEWS APRIL 2020

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News Curated by Grzegorz Stec and Flavian Berneagă

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THREAD 1

CHINA'S ECONOMY SHRANK - WHAT ABOUT RECOVERY?

KEY SUMMARY

HISTORICAL GDP CONTRACTION

China's economy contracted for the first time since comparable data have been recorded, by 6.8% in Q1, according to data presented by the Chinese government. Over 200 million people were left without work, the export sector is worse off than in 2008-09, industrial production dropped by 13.5%, and retail sales dropped by 20.5%. A recession is not out of question.

BUSINESS COMING BACK

Nonetheless, business has been making a slow comeback. In the beginning of April, Trivium China indicated a National Business Activity Index (NBAI) of 78.3%, with 95% of large manufacturers back to work and an official Purchasing Managers' Index (PMI) of 52.0. (The PMI is an index of economic trends in manufacturing - levels over 50.0 indicate optimism, those under 50.0 indicate pessimism about future trends.) By mid-April, the NBAI rose to 82.8%, while the PMI dropped to 50.8.

UNEMPLOYMENT HIGHER THAN STATS

By the end of Q1, unemployment stood at 5.9%, down from a high of 6.2% in February, meaning around 27.4 million people. Liu Chenjie, chief economist at fund manager Upright Asset, gives a darker estimate of over 205 million unemployed. Liu includes in the count a key category, migrant workers, who are usually excluded from government stats, even though they make up more than one third of urban workers in China (174 million out of 442 million). During the COVID-19 crisis, migrant workers could not travel, so they were left unemployed.

A DIFFERENT STIMULUS STORY

In 2008, China issued a 4 trillion RMB stimulus package (13% of its GDP at the time) to offset the economic downturn. Don't expect the same now. China's total debt to GDP stood at 300% in 2019, the highest in the world, much of it done through shadow banking and estimated at over $40 trillion. In March 2020, new bank lending skyrocketed to 2.85 trillion yuan ($405 billion). Post-COVID-19, China will not have the same stimulus flexibility as it did in 2008.

DOMESTIC SPENDING NEEDED

Domestic spending in China has been described as a major challenge in bringing the economy back to normal: 65% of consumers indicated plans to limit their spending habits, which is significant for an economy in which 58% of the GDP had been domestic spending. The central government has decreased bank loan rates, while more than 30 provinces and cities started issuing digital coupons via Alipay and WeChat Pay.

CHALLENGE OF EXPORTS

Exports represent another challenge. Europe and North America, the regions buying most of the Chinese exports, are themselves facing grim economic outlooks. In 2019, each of them bought one third of China's total exports, but in Q1 2020 the figure dropped, by 25% for the US and by 16% for the EU. The EU expects a recession of 'historic proportions" of 7.5% and the US economy is expected to drop by 5.9%, meaning "business as usual" will not resume right away for Chinese exporters. Chinese exports did witness a slight recovery (3.5%) in April, but the real demand shock is yet to come.

GAOKAO POSTPONED

An important sign of the gravity of the situation was that the competitive university entrance exam, the 'gaokao' (高考) was postponed until July 7-8 (a month later than planned). The last time the gaokao was postponed was during the Cultural Revolution. On the other hand, schools resumed classes, albeit with strict regulations of smaller class sizes, shorter days, and social distancing between students.

TWO SESSIONS SCHEDULED

The Two Sessions were scheduled for May 21-22. This refers to meetings of the National People's Congress (China's top legislature) and the Chinese People's Political Consultative Conference. Although they hold negligible legislative power, the Two Sessions serve as a rubber stamp parliament. The announcement of their dates is seen as a signal of returning to normal rhythm, a symbolic victory over COVID-19. Questions remain over the format of the plenary (which could be done over video) and the agenda, whose highlight is usually the annual announcement of new economic growth targets. Sources say that, due to the economic uncertainty of 2020, this year's Two Sessions may not include a numerical target for economic growth.

DIGITAL CURRENCY ON THE HORIZON

China announced the launching of an experimental central bank digital currency (CBDC), to be rolled out in Shenzhen, Suzhou, Chengdu, and Xiong'an. The end goal here is to fully replace paper money, a process that began in 2014, when QR codes gradually started substituting cash. Among other things, a digital currency would help control the budget better, trace shadow banking, and help avoid money laundering.

OUR COMMENTS

IN FOR A RIDE

Beijing has found itself in a very tough position amid the corona crisis. The first quarter of 2020 brought about the first contraction of the Chinese economy since comparable data have been recorded. With the demand shock expected in the markets of its key trade partners—the US and the EU—paired with calls for diversification of supply chains, it cannot hope for a smooth economic bounce back as it did after the SARS epidemic. At the same time, colossal debt prevents Beijing from deploying stimulus similar to that used after the Global Financial Crisis of 2008. While China's domestic consumption as a percentage of GDP has increased considerably since then, Beijing is still in a very hard position, particularly as the implied (sometimes contested) social contract between the Party-State and the populace has been based on an exchange of political liberties for continuous increase in living standards. This is not to say that China is on the edge, but the Party-State definitely is not at ease, as many past debts will resurface.

MISSING THE MARK

The contraction has definitely been a wake-up call for political leadership in Beijing, particularly given that it will make it impossible to achieve one of the century goals outlined by President Xi Jinping. Namely, by the hundredth anniversary of the establishment of the Chinese Communist Party, next year, China was supposed to double per capita GDP levels of 2010, thereby achieving a moderately prosperous society (小康社会). As of now it even remains unclear whether during the delayed Two Sessions Meeting Premier Li Keqiang will reveal the GDP target for the year. All this shows how the economic slowdown is a political problem.

BRAKES ON THE BRI TRAIN?

Still, amid all the uncertainties, it may be possible for China to continue its BRI lending—if it chooses to do so. According to a report by Rhodium Group, BRI loans make up a small proportion of China's lending portfolio. Peak BRI investment was reached in 2015/2016, at $50-60 billion. Compared with China's total bank lending of $2.6 trillion in 2019, it is a manageable amount even amid challenging economic circumstances. Particularly during the corona crisis, the influence bang for the lending buck may be much greater as China could present itself as a savior in contrast to Donald Trump's "America First". The challenge remains the need to renegotiate old loans, which may not rest well with the Chinese public, who have already been vocal in the past about the government's openness to pledge large-scale credit lines and support for the developing world instead of using the money for domestic development (as was the case at the FOCAC Summit in Beijing in 2018). In the past, though, Beijing has shown it is open to BRI debt renegotiations.

RELATED NEWS IN WEEKLY BRIEFINGS

- **China's Economic Recovery - Fact or Myth? [April 6]**
- **Chinese Economy Shrinks for the First Time since Data Have Been Recorded [April 20]**
- **From Digital Payments to Digital Currency [April 27]**

SELECTED READINGS

- COVID-19 crash: How China's economy may offer a glimpse of the future - World Economic Forum (Jenna Ross), Mar 31
- China GDP: Five things to watch after coronavirus - Financial Times (Tom Mitchell), Apr 15
- Coronavirus: China's unemployment crisis mounts, but nobody knows true number of jobless - SCMP (Frank Tang), Apr 3
- Booster or Brake? COVID and the Belt and Road Initiative - Rhodium Group (Agatha Kratz, Daniel Rosen, Matthew Mingey), Apr 15
- China aims to launch the world's first official digital currency - Economist, Apr 23

THREAD 2

WOLF FACE OF CHINA'S DIPLOMACY AMID COVID-19 PANDEMIC

KEY SUMMARY

WOLF WARRIORS, ASSEMBLE

Chinese diplomacy is on an upward trend towards an aggressive defence mode, with a brand new term for its wards: "Wolf Warrior" diplomats. The lack of official statements on this practice indicates there is "blessing from above" for it, but it may also be a way for rookie diplomats to snatch promotions, as has happened with Zhao Lijian and Lin Songtian. The diplomacy is largely directed towards the US but also at developing countries like Kazakhstan, India, Sri Lanka, and Thailand.

A WOLF AND A POODLE

Europe also got its share of it. In mid-April the Chinese embassy in France posted false information online, saying French nursing home workers stopped taking care of the elderly. After the censorship of the EU delegation's op-ed in China Daily, Chen Weihua, the Europe bureau chief at China Daily, called the EU the US's poodle and directly answered to Nicolas Chapuis on Twitter, saying he did nothing wrong.

DISINFORMATION DEFINED

The EEAS launched two reports on disinformation related to COVID-19. The reports described Russian and Chinese attempts to spread disinformation about the EU ('Chinese global projects are superior'), propagate incorrect health advice ('milk and vodka help against the virus'), promote conspiracy theories saying 5G internet spreads the virus, negate the virus's origin in Wuhan, and exaggerate Russian and Chinese aid.

BOT ATTACK

Much of the social media narrative is driven by fake accounts. A report by Alkemy for Formice looked at 47.821 tweets between March 11 and March 20, thanking Chinese intervention. It found that up to 46% of them were sent by bots and fake accounts. These bots were found to have spread propaganda, shared fake videos of Italians playing the Chinese anthem, and targeted EU inaction. Similarly, in Serbia, the Digital Forensic Center found that 71.9% of 30,000 tweets between March 9 and April 9 containing the words 'Kina' and 'Srbija' (China and Serbia) were posted by bots. The messages praised Chinese intervention, highlighted EU inaction, and praised Vučić.

MASK DIPLOMACY IN SERBIA

Medical supplies distributed by China in Serbia were instrumentalised by Serbian president Aleksandar Vučić to claim that "European solidarity does not exist" and to praise the "steel friendship" between Serbia and China. Billboards sprung up in Belgrade thanking "Brother Xi". Social media drew comparisons between Chinese aid and alleged European helplessness. In more extreme cases of disinformation, the EU was outright blamed for planning an invasion in the Western Balkans. The extent of Beijing's mask diplomacy success in Serbia may have more to do with Serbia's own foreign policy than with Beijing's persuasion skills. Context is important: Vučić's comments come at a time when Xi Jinping agreed with Vučić on a visit to Belgrade later this year.

MASK DIPLOMACY IN ITALY

We are starting to see early data on the results of Beijing's mask diplomacy. Another country that was strongly impacted by it is Italy. A poll by SWG, conducted between March and April, showed 52% of respondents perceived China as a friendly country, while 45% and 38% perceived Germany and France, respectively, as enemy countries. (The poll was taken, though, at an early stage and with a sample of only 800 respondents.)

TOYING WITH THE COVID-19 NUMBERS

Multiple reports point out that the number of cases and deaths in China is higher than initially reported by authorities. Reports from Wuhan suggest underreporting. For example, on April 17, the government revised data on the deaths in Wuhan, resulting in a figure 50% higher. Similarly, reports indicated the central leadership of CCP delayed disclosing the news about the outbreak to the public by 6 days (14-20 January), which was particularly crucial during the Chinese New Year.

POLITICAL LOGIC PREVAILS

Political logic seems to have played an important role, as shown by The Economist analysis of 15 instances where the number of cases jumped by at least 20% in one day. In two thirds of these cases, they were accompanied by important government decisions: Xi Jinping's speech, the sacking of a local leader, etc. This aside, the delay in response by the Party-State is likely linked to underreporting by local officials with ambitions of higher political office who did not want to send bad news to their superiors. A lot still remains uncertain, as shown by the increases in the number of deaths.

OUR COMMENTS

CHINA'S PUBLIC OPINION COUNTEROFFENSIVE

Beijing feels defensive, which shouldn't come as a surprise. Domestically, the Party-State faces unprecedented economic challenges that strike at the heart of its legitimacy. Internationally, the Party-State has become the subject of increased scrutiny over mismanaging the key period at the beginning of the COVID-19 outbreak, misreporting data related to the outbreak, and being unwilling to launch an international health investigation, blocking inquiries even from the WTO. Consequently, Beijing seems to have turned to outspoken "wolf warrior" diplomats and disinformation efforts to lead an offensive defence that can appeal to its domestic nationalistic public and can counter or obscure narratives unfavorable to Beijing. The embodiment of this change is MFA spokesman Zhao Lijian, whose highly controversial remarks, also shared on Twitter, and promotion of conspiracy theories related to origins of the coronavirus seem to be earning him support from the Party leadership. However, there appears to be no consensus in higher circles on whether this new style is productive and desirable, so China communicates now through a mixture of wolf-warrior and low-key diplomacy, as expressed by such veteran diplomats as Cui Tiankai or Zhang Ming.

But even putting these (in)famous wolf-warriors aside, there is a sense of the need for defence through offense, as interestingly captured in a strategy proposal to "increase ability to respond to external attacks on China" issued in the magazine of the Chinese Academy of Social Sciences, one of China's leading think tanks. Six proposed measures clearly argue for an active response and include studying foreign media to prepare for "attacks" from them, establishing a 24h monitoring and response system for narratives unfavorable to Beijing, diversifying channels of communication (including support to China-friendly experts publishing on foreign platforms), and improving the messaging to use narrative forms preferred by foreign audiences.

ADAPTING TO PROPAGANDA TRENDS

Part of this counteroffensive was the emergence of China's new style of propaganda—or, in this case, disinformation—campaigns. Traditionally, Chinese propaganda efforts have been characterised by consistent unified messaging through multiple sources. But it appears that amid the outbreak of COVID-19 China started to also adopt a style of deploying multiple, even contradictory, messages at once, which has been associated with Russian disinformation practices. One of the goals of this new messaging style has been to push back against the questioning of Chinese official figures, to question the origin location of the virus, or to create an impression that the Chinese, authoritarian system of governance is much better suited to tackling the challenge of COVID-19, by discrediting responses from democratic countries and overreporting China's success. This shift also further highlights the need for European decision makers to increase their "China literacy" and to diversify the Chinese sources they draw information from, to avoid falling victim to either pro-China or anti-China messaging.

COUNTERPRODUCTIVE COUNTEROFFENSIVE

But it is exactly this tougher rhetoric, disinformation, and limited transparency that pushed multiple international leaders that had not been prone to criticise China to express their dissatisfaction with the Party-State's activities. Once normality resumes, a tougher rhetoric on China's mishandling and underreporting is likely to affect various levels of EU-China cooperation, as EU governments are now being confronted with a radical and vivid example of dealing with a non-transparent partner. Also many European leaders, civil servants, and business people were personally affected by COVID-19 and China's limited commitment to international, transparent cooperation may not fare well with them. An extreme example would be that of the UK's PM Boris Johnson, who was allegedly furious at early stages of the outbreak in the UK over China's providing inaccurate data—and that was before he himself became infected with COVID-19. While such personal experiences are unlikely to lead to the adjustment of national strategies towards China, they can definitely affect personal sentiments and the overall atmosphere of diplomatic exchanges.

RELATED NEWS IN WEEKLY BRIEFINGS

- **COVID-19 Disinformation Targeting "EU Disintegration" Spreads to the Balkans [April 6]**
- **Toying with the Numbers? China's Data on COVID-19 Questioned [April 13]**
- **China Changes Charm Offensive to Offensive Charm [April 20]**
- **Pragmatic Discontent and EEAS Scandal - EU's Response to China's Disinformation [April 27]**

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- EEAS Special Report Update: Short Assessment of Narratives and Disinformation around the COVID-19 Pandemic - EEAS, Apr 1
- China's data reveal a puzzling link between covid-19 cases and political events - Economist, Apr 7
- What to Make of China's Coronavirus Figures - Foreign Policy (James Palmer), Apr 1
- China wants its diplomats to show more fighting spirit. It may not be intended to win over the rest of the world - SCMP (Shi Jiangtao), Apr 12
- A Bot Network Arrived in Serbia Along with the Coronavirus - DFC, Apr 13

THREAD 3

CHINESE INVESTMENTS TO EUROPE - TRENDS AND PROSPECTS

KEY SUMMARY

NEW DATA ON CHINESE FDI IN EUROPE

MERICS released its annual report on Chinese foreign investment in Europe for 2019. Some interesting trends are underway, most notably the continuous decline of FDI, its concentration in four sectors, and its concentration in Northern Europe.

COUNTINOUS FALL

Chinese FDI in Europe dropped to €11.7 billion, a low figure compared to 2017 (€29.2 billion) and 2016 (€37.3 billion). In fact, this number only slightly overtakes 2012 levels (€10.2 billion). The downward trend makes sense, in the context of Beijing adopting restrictions to curb “irrational” outflow of capital in 2017-2018. This made it more difficult for Chinese companies to raise funding and get approval to invest abroad. The decrease is also related to new EU regulation on investments.

DECREASING INFLOWS TO THE BIG THREE

Northern Europe overtook the ‘Big Three’ (France, Germany, UK) in attracting Chinese investment. The former received 53% of investments, while the latter dropped to 34%, down from 45% in 2018 and 71% in 2017. Finland and Sweden are the big ‘winners’ here. Finnish company Amer was bought by Anta for €4.6 billion, while China’s Evergrande invested €830 million in Swedish company NEVS. Southern Europe and the Benelux’s shares dropped, while Eastern Europe’s share of investment increased, but just barely, by 1%. However, most of the investment in Eastern Europe was in Romania’s Nuclearelectrica, a deal cancelled in late 2019, after the change in the Romanian government.

CONSUMERS, SERVICES, ICT

Chinese FDI in 2019 were also considerably concentrated, as 80% of it was spent in just four sectors. 40% of it was focused on consumer products and services, 20% was invested in ICT, 13% went to the automotive sector, and 8% went to transport, utilities, and infrastructure. The continuous investment in ICT shows that China maintained interest in European tech companies and their know-how.

PRIVATE POWER

Investment from Chinese state-owned enterprises (SOEs) dropped dramatically to 11%, down from 41% in 2018 and 72% in 2017. It is the lowest level of SOE investment over the past decade.

INVESTMENT APPETITE AND COUNTERMEASURES

The beginning of April saw increased interest from Chinese SOEs and private firms for investment proposals on targets in Europe. This comes amidst a 23% drop of the European index. Fears of takeovers in strategic sectors prompted EU Commissioner Margrethe Vestager to encourage member states to buy stakes in struggling companies, echoing calls by the Commission from March to beef up defensive measures. Italy, Spain, and Germany were the main countries moving to protect their industries, but Hungary may also take a different route as, with new powers acquired amid the COVID-19 crisis, the government of Viktor Orbán moved to classify details of the largely Chinese-funded Budapest-Belgrade railway project.

R&D CHALLENGE

Non-equity investments grew rapidly, especially in joint research and development (R&D) partnerships between Chinese and European companies, universities, and science hubs. The benefits are that cooperation may provide breakthroughs in technologies, know-how, products, and services. The potential disadvantage is that R&D partnerships may leave sensitive European technology exposed, meaning China may gain access to tech that could potentially have a dual-use. Human rights is another issue, in the unfortunate circumstance where the acquired tech could be used for surveillance or prosecution, such as in regions like Xinjiang.

OUR COMMENTS

REVERSING THE TREND?

Chinese FDI to Europe continued to fall in 2019, but there have been signs of interesting adjustments of destinations, sector focus, and limited participation of Chinese state owned enterprises in overall investments to Europe. However, the outbreak COVID-19 and the subsequent economic crisis may prove to be game-changers. After all, the last wave of rapid increase of Chinese FDI in Europe was linked to the Global Financial Crisis and the Eurozone crisis, and continued until it culminated in a flurry of M&As in 2016. Also, the current economic hardship may encourage many struggling companies to become more open to foreign investments and vulnerable to takeovers. Interest from Chinese actors is there: in April bankers noticed a spike in requests from Chinese firms and funds for proposals on European investment targets.

EU BEEFING UP DEFENCES

But the Europe of today is not the Europe of 2008. Already very early on in the crisis, in March, the Commission asked the member states to approach the issue of non-EU investments and takeovers amid the corona-crisis with great caution and make full use of available investment screening mechanisms. Such calls for caution continued in April, as the Commission, particularly Commissioner Vestager, urged increasing defensive measures against non-EU takeovers in strategic, vulnerable companies and even buying stakes in those companies to ensure their resistance. While many countries heeded the call, as described in the summary above, the Commission considers going even further by launching an investment mechanism as part of the next budget. InvestEU could include a €12 billion fund aimed at incentivising buying stakes, particularly in companies in poorer member states. But whether this is going to indeed limit the non-EU (Chinese) investments remains to be seen, given what we observe in Hungary or a buyout of a majority stake of a majority stake (increasing ownership from 30% to 57%) by China's CITIC Group in the Czech Republic's largest domestic media agency, Médea.

CHALLENGING NEGOTIATIONS

The negotiation process on the EU-China Comprehensive Agreement on Investments is bound to be affected by those dynamics, paired with still ongoing debates about Huawei's participation in rollout of 5G in EU member states and the postponement (or possible cancellation) of key political EU-China events, including the Leipzig Summit. After a coronavirus-induced break, the two sides proceeded with the 28th round of negotiations between April 20-24th via video conference, with the next round of negotiations scheduled between 25th and 29th of May. Still, many key questions—including the EU's calls for Chinese SOEs to behave commercially when engaging in commercial activities—remain unresolved. Given all the circumstances, rapid progress will not be easy.

RELATED NEWS IN WEEKLY BRIEFINGS

- **Chinese FDI in Europe is Dwindling, but COVID-19 Could Reverse That [April 13]**
- **EU Reassesses its Relationship with China [April 20]**
- **Repatriation or Diversification - How Much Globalisation Will the EU Give Up? [April 27]**

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- China's Corporates Are Gearing Up in Europe for M&A Bargains - Bloomberg, Apr 7
- Vestager urges stakebuilding to block Chinese takeovers - Financial Times (Javier Espinoza), Apr 12
- China moves to keep EU investment talks on track - SCMP (Stuart Lau), Apr 18
- Europe Is Taking a Harder Look at China After Virus Suspicions - Bloomberg (Patrick Donahue and Ania Nussbaum), Apr 17

THREAD 4

EU-CHINA SUPPLY CHAINS REVISITED

KEY SUMMARY

EU'S DEPENDENCE ON CHINESE PHARMA

COVID-19 highlighted Europe's dependency on medicine produced in China. China accounts for 70% of the ingredients in medicines and 80%-90% of global supplies of ingredients for antibiotics. The main reasons behind this are cheap production costs in China and strict EU patent law. In response, EU Health Commissioner Stella Kyriakides announced on April 23 that the EU will draft plans to repatriate medicine production, notably from China.

WIDER PICTURE

Dependency on medical supplies and problems with supply chains during the pandemic have prompted wider re-examination of the status quo. China certainly plays a critical role in global supply chains, amassing one third of global intermediate product manufacturing. In fact, an asymmetrical relationship has formed, where China exports high-value products (albeit, in many cases, as an assembling country) to the EU, but imports fewer goods in return.

DIVERSIFICATION IN THE MAKING

Commissioner for Internal Market Thierry Breton announced that the EU will seek to diversify its supply chains and remove risks of interruptions, while also boosting its domestic industrial capacity in other sectors, so as to decrease reliance on China. He argued the EU must reassess the viability of its supply chains, diversify its sources, and cut the risks of interruptions.

REALISTIC HOGAN

EU Trade Commissioner Phil Hogan is not on board with plans that would fully bring back manufacturing. He said the EU must acknowledge the "simple fact that we will not be able to manufacture everything locally", while maintaining an open trade policy at the global level. To further diversify its supply chains, Hogan suggested the EU should take advantage of its arsenal of bilateral treaties with developing countries.

OPPORTUNITY FOR CEE?

Another option may lie within the EU itself. Bulgarian Deputy PM Tomislav Donchev lobbied for Eastern European countries to replace China in manufacturing. Donchev pointed to the comparative advantages of having industries within the EU's territory and developing critical manufacturing that could help to alleviate differences between Eastern and Western Europe, while also ensuring lives, jobs, and wealth are safeguarded.

EU BUSINESS IN CHINA NOT KEEN

But Many European companies think China is still the future. European companies in China seem to be reluctant about the idea of moving their operations. Jörg Wuttke, the head of the EU Chamber of Commerce in China said manufacturers will not find moving out an easy or economically efficient task, due to the difficulty of moving high-tech elements.

OUR COMMENTS

SPUTNIK MOMENT OF MASK DIPLOMACY

Amid the pandemic, the EU's supply chain dependency on China's medical equipment production became all too apparent, particularly given that China seems to have tied access to exports of high-quality equipment to political relations, as shown by reports from Germany and the Dutch case. And China's willingness to politically weaponise such supply chains will definitely leave a mark on the European decision makers' approach to the matter. At the same time, such dynamics also limit how outspoken the EU member states decide to be towards China amid the pandemic.

STRATEGIC DIVERSIFICATION

But the reconsideration of the dependency doesn't stop with health equipment. Disruptions to the supply chains that European companies noted in the first quarter of this year span different sectors and made many calls for reconsideration of overdependence on China. This doesn't mean large-scale repatiarion plans. Such a solution would be costly and counterproductive given that many European companies eye the future market in China. Also, as the key proponent of free trade, the EU isn't in a position to support protectionist repatriations. That is why Brussels is opting to support strategic diversification, which is a welcomed realisation of the need for limiting dependency on one country-based supply chains. Consequently, this may be good news for the CEE and South-East Asia, which stand out as potential benefactors. Don't expect dramatic moves but, rather, a strategic correction.

RELATED NEWS IN WEEKLY BRIEFINGS

- **The Path Forward for Businesses in the EU and China [April 6]**
- **EU Reassesses its Relationship with China [April 20]**
- **Repatriation or Diversification - How Much Globalisation Will the EU Give Up? [April 27]**

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- Europe's dependence on medicine imports - Euractiv (Florence Schulz), Mar 16
- EU should 'not aim for self-sufficiency' after coronavirus, trade chief says - FT (Alan Beattie and Jim Brunsden), Apr 23
- Introductory Statement by Commissioner Phil Hogan at Informal Meeting of EU Trade Ministers - European Commission, Apr 16
- Bulgarian Deputy PM: Eastern Europe could replace China in sectors critical to the EU - Euractiv (Krassen Nikolov), Apr 17
- European Manufacturers Not Eager to Exit China, Head of EU Chamber Says - Caixin (Wang Liwei and Guo Yingzhe), Apr 15

THREAD 5

EU'S PRAGMATIC DISCONTENT TOWARDS CHINA

KEY SUMMARY

PRAGMATIC DISCONTENT

An important piece of criticism came from Emmanuel Macron, who cast doubt on April 16 about the number of reported cases and deaths in China. His statement came just one day after the Chinese ambassador was summoned for claiming that French nursing home workers had abandoned the elderly. In Britain, Foreign Secretary Dominic Raab stated that the relationship with China after the pandemic will not be “business as usual”, while a former head of the MI6 called for the UK to prevent Chinese takeovers in the tech industry. In Germany, a leaked document from April 12 indicated Chinese officials approached German MFA officials and invited them to speak positively about China’s response to the virus. On April 20, Angela Merkel said that “the more transparent China is about the origin of the virus, the better it is for everyone in the world in order to learn from it”. In the Czech Republic, an analysis commissioned by the Ministry of Foreign Affairs on April 21 accused China of withholding information about the virus and attempting to sabotage the West.

SIGNS OF PUSHBACK

The pushback goes beyond mere rhetoric. Sweden shut down its last Confucius Institute on April 21st, three days before Gothenburg cancelled its sister-city agreement with Shanghai. Soon after, the European Commission issued a “concept note” to member states, encouraging them to hire civilian spy-catchers in European universities, in order to prevent foreign interference in international research collaborations. Furthermore, the Commission launched a website dedicated to fighting disinformation, while the EEAS started to provide regular anti-disinformation reports. So far, three have been published, on March 19, April 1, April 24.

NEIGHBOURHOOD PUSHBACK

In response to “mask diplomacy” in the Western Balkans, the EU pledged €40 million on March 30 to a set of Western Balkan countries to fight disinformation. Another €140 million was offered to countries in the Eastern Partnership and a further €374 million in existing funding packages was reallocated for combatting the economic effects of the epidemic. On April 29, the EU pledged another €3 billion in favorable loans to its Neighbourhood to help with economic recovery after the pandemic (from which Serbia was excluded, after its China-friendly comments). In response, Serbian president Aleksandar Vučić stated Serbia was not in need of any loans.

TIED HANDS - MEDICAL RELIANCE

In spite of more confrontational rhetoric, many countries don't go very far in escalating their tensions with China. Partially to build framework for international cooperation amid COVID-19, many countries still depend on China for the provision of medical supplies, meaning criticism is unlikely to go beyond a certain level. Medical supplies appear to be approved on the basis of political agreements and direct calls, as happened when Angela Merkel called Xi Jinping directly, which allowed Germany direct access to Moheco, a Chinese SOE producing protective equipment, according to reporting from Süddeutsche Zeitung. Furthermore, when the Netherlands changed the name of its representative office in Taiwan on April 28 (from "The Netherlands Trade and Investment Office" to the "Netherlands Office Taipei"), PRC-sponsored newspaper Global Times suggested the possibility of suspending medical exports and boycotting Dutch products in response.

MEDIA POLITICS

Harsh criticism of China came from some of the European media. The Daily Telegraph announced it would remove its PRC-sponsored China Watch column, while German tabloid Bild posted a video in which its editor-in-chief argued vehemently that China should pay for the damages caused by COVID-19. His comments were rejected by some for having a xenophobic character. On the other hand, CITIC (a Chinese SOE) acquired a majority stake in one of the largest Czech media groups, Médea.

INTERNATIONAL INVESTIGATION IN THE MAKING

Towards the end of the month, multiple world leaders agreed to an independent investigation of the origin of the coronavirus. German Chancellor Angela Merkel (April 21) and Australian PM Scott Morrison (April 22) were the first ones to make a call for an international investigation team. Later, on April 30, Sweden announced, through Health Minister Lena Hallengren, that it will ask the European Commission to join the calls for an investigation. Finally, Commission President Ursula von der Leyen announced on May 1 that she backs the creation of a transparent, international body to trace the origin of the virus.

EEAS SCANDAL CHRONOLOGY

The EEAS came under fire after Politico reported about a disinformation report run by its EUvsDisinfo team. The report was allegedly delayed and then watered down, at the express request of Chinese officials, before being released to the public on April 24th. The two most important elements missing from the published report were references to China running a "global disinformation" campaign and the Chinese criticisms of France's reaction to the pandemic. The report was picked up by other news media, which created friction between journalists and EEAS spokesperson Peter Stano. The latter implied those who saw the alleged influence of Beijing in the report have a "hidden agenda".

BORRELL'S GRILLING

High Representative Josep Borrell was summoned on April 30 for a hearing at the European Parliament's AFET committee, where he was grilled over the alleged Chinese interference. Borrell acknowledged pressure from Beijing existed, but rejected claims that the EU yielded to said influence, viewing it as a typical case of diplomacy. He argued there were two reports, one internal and one for the public, which were slightly different. His explanations were mostly well-received, specifically by MEP's with previous experience in foreign affairs.

VARRYING EACTIONS

The grilling drew a variety of reactions. Commission President Ursula von der Leyen defended the EEAS while MEP Reinhard Bütikofer (Chair of the Delegation for relations with the PRC in the European Parliament) said the scandal inflicted damage on China's image in the EU. Politico's main EU correspondent, Florian Eder, highlighted that Borrell did not acknowledge any mishandling, while Borrell himself recognised two days after the hearing in an interview with Le Journal du Dimanche that Europe had been "a little naive" on China.

OUR COMMENTS

DISCONTENT AND CHINA RETHINK

The circumstances are pushing Brussels and other European capitals to reevaluate their approach towards China. The COVID-19 pandemic exposed their dependencies on supply chains, the underlying systemic rivalry between the EU and China, and the challenges of cooperating with a non-transparent partner who doesn't shy away from deploying disinformation tactics. Consequently, multiple European leaders have been voicing their discontent with Beijing. However, their way of communicating has been less confrontational and characterised by low-key diplomacy style. Let's be clear: growing discontent is not synonymous with confrontation. Europe is reliant on medical supplies from the PRC (and Beijing expressed its willingness to politically weaponise this reliance) and is trying to build an international framework for a multilateral response to the challenge of the COVID-19 and corona-crisis.

BETWEEN A ROCK AND A HARD PLACE

With this last task, the EU finds itself between a rock and a hard place. On the one hand, Washington wants Brussels to be more aggressive while trying to cover up mismanagement of the response to COVID-19 by its own administration and undermining efforts to build a multilateral response. On the other hand, Beijing behaves as if it did nothing wrong and deploys its offensive defence tactics, including wolf-warrior diplomacy and disinformation efforts. Amid the outbreak of COVID-19, the tensions between the United States and China have been growing alarmingly and these are stormy seas for the EU to navigate.

INTERNAL AUDIT NEEDED

However, acknowledgement that the EU has been "a little naive" about China and that the EU and China want different types of multilateralism, as mentioned by High Representative Borrell, is not enough. The EEAS disinformation report controversies and the closely following scandal, related to censorship of the message from the EU Delegation in China Daily, pose a question: What communication strategy will be most effective in dealing with a multifaceted relationship with China? Such actions show a willingness to move in confrontational and cooperative directions at the same time. Such a description naturally captures the complex nature of EU-China relations, but it requires a nuanced, thought-through response that will be acted upon. The EU-China Strategic Outlook of 2019 was painted as such a step but now, a year on, only one of ten action points from the document has been achieved. Clear-eyed acknowledgement of EU-China dynamics is only the first step towards a China rethink. An internal audit is needed.

RELATED NEWS IN WEEKLY BRIEFINGS

- **EU Reassesses its Relationship with China [April 20]**
- **Pragmatic Discontent and EEAS Scandal - EU's Response to China's Disinformation [April 27]**

SELECTED READINGS

- FT Interview: Emmanuel Macron says it is time to think the unthinkable - Financial Times (Victor Mallet and Roula Khalaf), Apr 16
- Beijing tried to make German officials praise China over coronavirus outbreak – report - Hong Kong Free Press (AFP), Apr 12
- Germany pushes China for answers to coronavirus origin - SCMP (Stuart Lau, Catherine Wong), Apr 21
- EEAS SPECIAL REPORT UPDATE: SHORT ASSESSMENT OF NARRATIVES AND DISINFORMATION AROUND THE COVID-19/CORONAVIRUS PANDEMIC (UPDATED 2 – 22 APRIL) - EUvsDisInfo, Apr 24
- Parliament hammers Borrell over China disinformation report - Politico (Laurens Cerulus, David M. Herszenhorn), Apr 30

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