EU-China Hub

Monthly Report

EU-China Hub

MAY 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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MAY 2020

Welcome to the Monthly EU-China Report!

In May, multiple developments highlighted the contradictions engraved in the multifaceted approach of the EU towards China, as outlined in the Strategic Outlook from March 2019, in which China is defined as a cooperation partner, negotiating partner, economic competitor, and systemic rival.

The EU's response to Beijing's move to impose a national security law in Hong Kong exposed the challenge of protecting both values and interests when dealing with a systemic rival. But the view of China as an economic competitor also is gaining momentum, as further economic securitisation on the EU's side is visible on the horizon. The postponement of the Leipzig Summit may also be a blow to the "cooperation partner" dynamic.

This further highlights the need for a wider reflection on the EU's policy towards China and development of a "robust strategy on China," in the words of High Representative Josep Borrell. Such a strategy would require a more unified approach from the EU, faithful to its own interests and values despite the pressure to take sides in escalating tensions between Beijing and Washington. We would hope that the upcoming German Presidency will provide a platform for developing this more united approach towards China among the member states, despite Leipzig being put on hold.

The level of the challenge ahead for the EU—to promote its interests and values in the reality of Sino-American rivalry—was well exemplified by the controversies surrounding the World Health Assembly and the plans to launch an international investigation into the origins of the virus. The EU cooperated with the WHO in launching the Coronavirus Global Response (including international pledging event) and compromised on the international investigation, likely to avoid fragmentation within the organisation. While President Trump withdrew from the WHO, President Xi pledged $2 billion to fighting COVID-19 but is likely to spend it via China's own health diplomacy channels rather than the current multilateral framework. These are not easy times for the EU's model of multilateral globalisation.

But May was also a month in which the EU and China both set economic agendas and response plans towards the corona-crisis. The message coming from Beijing and the Two Sessions is the mantra “stability over growth”, as the GDP growth target was dropped for the first time in almost three decades. Brussels offered some positive news, as the Franco-German proposal on the recovery fund paved the way for the European Commission’s proposal for the “Next Generation EU” fund (combining grants and loans) as well as for the next EU budget, for 2021-2027. Fortunately, the initial reactions from the member states have been positive and we are set for negotiations in a constructive tone under the German Presidency.

We hope that you will enjoy this report and encourage you to share it with your network.

Enjoy and stay safe!

Grzegorz Stec
Founder of EU-China Hub

EU-CHINA INTERVIEW

IVANA KARÁSKOVÁ

17+1 China-CEE Cooperation - Vehicle of Influence, Empty Shell, or Multifaceted Network?

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CONTENTS

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THREAD 1

HONG KONG NATIONAL SECURITY LAW AND ITS IMPLICATIONS

KEY SUMMARY

BEIJING PASSESS THE MOTION

On May 28, the proposed motion on Hong Kong's national security law was adopted by the National People's Congress, with a wide majority (2878 out of 2885) voting in favour. There was one vote against and six abstentions. The proposal is now moved to the Standing Committee of the NPC, which decides on the final details of the draft. Once the draft is finished, it will be promulgated in Hong Kong, bypassing the local legislature.

WHAT EXACTLY IS THE NATIONAL SECURITY LAW

The Chinese government stated that the law will tackle actions that "seriously endanger national security" and those that perpetrate "separatist, subversive, infiltrative, or destructive activities". A broad definition of these terms could mean crackdowns on activist groups and a drastic reduction in freedoms of speech and assembly. Beijing gave assurances, through NPC Chairman Li Zhanshu, that the law will "uphold and improve the One Country, Two Systems policy," but provisions that are under discussion in regard to the law undermine his statement. For example, the Mainland Ministry of Public Security could openly operate in Hong Kong, and Teresa Cheng, the city's justice minister, argued that the establishment of a special national security court is being discussed as an element of the national security law.

ONE COUNTRY, TWO SYSTEMS?

The main pushback against this law relates to it contradicting the principle of 'One Country, Two Systems' established as part of Hong Kong reverting back to China in 1997. Similarly, Beijing bypassing Hong Kong's legislative body in adopting this law is viewed as a legal breach of the Special Administrative Region's mini-constitution—the Basic Law—which grants it political, legal, and economic autonomy. More specifically, the NPC is seen as violating Article 23 of the Basic Law, which stipulates that the Hong Kong government "shall enact laws on its own to prohibit any act of treason, secession, sedition, subversion against the Central People's Government [...]." The issue for Beijing is that the Hong Kong government has been unable to enact a national security bill since 2003, as mass protests have made legislators shelve the bill. And according to analysis of the PRC's legal system by the NPC Observer, the NPC has the legal grounds to dictate that the law is whatever it wants. However, the Central Government is still bound by the obligations of the Sino-British Joint Declaration and its broader international human rights pledges, which makes international reactions even more important.

HONGKONGERS PUSH BACK

The Chief Executive of Hong Kong says she is committed to implementing the new national security law, but the law's announcement caused segments of the Hong Kong population to join demonstrations opposing the Central Government's decision. May 24 saw thousands of Hongkongers demonstrating and putting up roadblocks to protest the proposed legislation, but protests were quickly met by police firing tear gas and employing water canons. The protests were broken up and the police arrested over 180 people. More protests on May 27 resulted in another 360 arrests, with the general morale of the population turning pessimistic about the prospect of avoiding the implementation of the law. Hongkongers reportedly started looking for avenues for emigration, deleting their Telegram app, removing Facebook posts that were critical of the Central Government, and downloading VPN apps.

REACTION BY THE EU

The key response about Hong Kong coming from the EU was a joint statement issued after a virtual meeting of the EU foreign affairs ministers, hosted by High Representative Josep Borrell on May 29. The statement argued that the situation in Hong Kong makes the EU question whether China is willing to uphold other international commitments. This may affect the basis of the EU-China relationship - "the mutual respect and trust". Nonetheless, Borrell did not adopt a combative approach, specifying that recent developments will not have an impact on the CAI or the Leipzig Summit (now postponed) and that sanctions are not a viable way of guiding the relation with China. Other voices in the EU were less accommodating. Reinhard Bütikofer, the Chair of the European Parliament's Delegation for the relations with the PRC, asserted that upholding the strategic partnership is becoming harder to sustain. In addition, the EU Chamber of Commerce in China and the Federation of German Industries said the NPC's decision will impact Hong Kong's status as a business-friendly hub.

REACTION BY THE UK

The UK took steps to oppose the national security law, which was mirrored in multiple actions. The UK raised the issue in the UN Security Council and Chris Patten, the last British governor of Hong Kong, suggested doing the same at the G7 level. This was followed by a joint declaration alongside the US, Australia, and Canada, asking China to uphold the Sino-British Joint Declaration. The most important measure was announced by PM Boris Johnson in an op-ed in the South China Morning Post, where he stated regulation will be relaxed, so that around 3 million Hongkongers could enter the UK without a visa. He warned that, if the law is passed, the UK will give "further immigration rights, including the right to work, which could place them on a route to citizenship." Johnson's proposal was welcomed positively in the British Parliament, where it garnered cross-party, unanimous support.

REACTION BY THE US

The Chief Executive of Hong Kong says she is committed to implementing the new national security law, but the law's announcement caused segments of the Hong Kong population to join demonstrations opposing the Central Government's decision. May 24 saw thousands of Hongkongers demonstrating and putting up roadblocks to protest the proposed legislation, but protests were quickly met by police firing tear gas and employing water canons. The protests were broken up and the police arrested over 180 people. More protests on May 27 resulted in another 360 arrests, with the general morale of the population turning pessimistic about the prospect of avoiding the implementation of the law. Hongkongers reportedly started looking for avenues for emigration, deleting their Telegram app, removing Facebook posts that were critical of the Central Government, and downloading VPN apps.

OUR COMMENTS

CALCULATED RISK

It is now up to the NPC's Standing Committee to draft the exact content of the law. While the Standing Committee may want to consider the impact of Washington's review of Hong Kong's special status, don't expect it to back down. Beijing is trying to achieve a lot here.

The obvious intent is for the Party-State to assert greater control over Hong Kong and to broaden the toolbox to crack down on dissent. Beijing has wanted to accomplish this since at least 2003 but now, after a year of protests following the proposal of the controversial Extradition Bill, Beijing questions whether the Hong Kong administration can enact the national security legislation without the intervention of the Central Government. The timing is important for two reasons. First, the authorities might have hoped that the threat of the coronavirus would quell the number of protesters taking to the streets. Second, and perhaps more importantly, the move comes amid the corona-crisis and at a time of economic challenges, so the Party-State wants to emphasise stability and its ability to control the situation. Taking decisive action against the protests in Hong Kong is definitely a message that can resonate well with China's domestic, nationalistic audience. While this comes at the price of China's international image—which Beijing likely sees as the lowest since 1989 anyway—and may dismantle Hong Kong's status as an international financial hub, the Party-State has definitely taken a calculated risk. Also bear in mind that maintaining social stability is the paramount interest of the Party-State, as it is being threatened by the impact of the COVID-19 and the leadership may be inclined to pursue more moves boosting its nationalistic mandate.

CALCULATED REACTION

The EU's reaction to the situation in Hong Kong is one of the most striking examples of the block's struggle to reconcile the dynamics of China being both its negotiating partner and a systemic rival. While the statement and the subsequent press conference by High Representative Borrell included concerns about Beijing's actions, it refrained from naming any potential punitive actions, with the High Representative explicitly stating that there are no such measures considered "on the agenda".

Such a reaction may be a result of a pragmatic assessment that pressure such as sanctions won't make Beijing revise its course and may actually make it double down on its efforts to curb Hong Kong's autonomy. This and the likely political costs could undermine the progress on CAI, the most recent round of which—conveniently for Beijing—were taking place as events unfolded between the 25th and 29th of May. No matter the reasoning, it is hard to defend the EU's adherence to its values and international law in this situation. Referring to points made by Reinhard Bütikofer, as of now, disregarding international law does not come at any price for Beijing, as the EU has resorted only to expressing its concerns. But such experiences of systemic rivalry are further undermining strategic trust. As a result, Beijing's actions in Hong Kong may accelerate the EU's revision of its policy on China.

FUTURE OF HONG KONG

While the NPC's move to draft a national security law for Hong Kong clearly indicates Beijing's uneasiness with the protests happening throughout the past year, the path forward for Hong Kong is yet to be decided. Importantly, the decision lies with the Standing Committee of the NPC (where the national law is drafted) and in the White House (where its special status is re-assessed). Both the PRC and the US have plenty to lose if they apply too much pressure too quickly. For mainland China, Hong Kong's economy is not that important as it comprises only 3% of GDP. Its real significance is tied to Hong Kong's ability to attract international capital: 60% of FDI in China in 2018 came through Hong Kong. Similarly, Chinese firms interested in accessing overseas technologies found Hong Kong to be an excellent destination for private wealth management with potential for international exposure. This is thanks to Hong Kong's legal and financial systems, which grant liberties to businesses and individuals that are otherwise lacking in the mainland, even in a city as international as Shanghai. For the United States, Hong Kong is not negligible either. The US boasted a $33 billion trade surplus with Hong Kong in 2018 and 735 US companies have their regional headquarters and offices in Hong Kong. Moreover, the Hong Kong dollar is pegged to the US dollar, making financial transactions much more facile.

As of now, we are not (yet) seeing US companies inclined to flee Hong Kong , as there has not been a sudden outflow of bank deposits. The president of the American Chamber of Commerce in Hong Kong did indicate, however, that the period ahead will be one of "sustained re-evaluation" for many US businesses, which must decide whether staying in Hong Kong is a sound financial decision. The fate of Hong Kong is tied to whether foreign businesses still trust it as a place where the West can meet China halfway. If Washington decides to come down hard on Beijing and completely remove Hong Kong's ability to move US dollars freely, that will severely impact its status as a global financial hub. Similarly, if mainland intervention leads to financial institutions losing their glamour to foreign investors, this will, in turn, lead to a gradual deterioration of Hong Kong's special status. In the midst of all of this uncertainty stand many ordinary Hongkongers, who fear this is the end of Hong Kong as they have known it and are increasingly seeking avenues to emigrate.

RELATED NEWS IN WEEKLY BRIEFINGS

- **Two Sessions 2020 - Breaking One Country, Two Systems, and Changing Rhetoric on Taiwan [May 25]**
- **Reactions to Hong Kong National Security Law [June 1]**

SELECTED READINGS

- 2020 NPC Session: NPC's Decision on National Security in Hong Kong Explained - NPC Observer, May 28
- Declaration of the High Representative on behalf of the European Union on Hong Kong - European Council, May 29
- Press conference following the video conference of foreign affairs ministers - European Council of the European Union (Video), May 29
- Donald Trump's announcement on measures targeting China - BBC (Video), May 29

THREAD 2

TWO SESSIONS - CHINA'S ECONOMIC PLAN AMID THE PANDEMIC

KEY SUMMARY

TWO SESSIONS EXPLAINED

The 'Two Sessions' (两会) refers to the annual gathering of two separate political entities in Beijing: the National People's Congress (NPC), which is China's top legislature, and the Chinese People's Political Consultative Conference (CPPCC). They add up to 5000 lawmakers and political advisors congregating in Beijing, usually every March, for about two weeks. Because of the pandemic, 2020 saw the start of the Two Sessions delayed until May 21 and shortened to only one week. The Two Sessions are portrayed as the main power body in China but amount, in reality, to a rubber stamp set of institutions. They hold symbolic value because, historically, they are the venue where yearly GDP targets are announced, which makes this year's Two Sessions even more salient.

NATIONAL PEOPLE'S CONGRESS

The National People's Congress is formed of 2987 deputies and is nominally the formal parliament of China and the highest organ of state power in the PRC. It passes laws, amends the Constitution, passes the central budget, and fills key state posts. In reality, these decisions are taken within the State Council and the NPC simply approves them, without debate.

CHINESE PEOPLE'S POLITICAL CONSULTATIVE CONFERENCE

The CPPCC is the advisory body of the NPC and is meant to represent civil society. It comprises 2200 representatives who are typically influential business people, United Front representatives, ethnic groups, and prominent thinkers. The Conference does not have any decision-making powers, it only provides consultation to the NPC. It is supposed to be an example of political pluralism in China but it is not an organ of the state and has no constitutional status.

SPECIAL YEAR

Typically, the Two Sessions happen in March, but due to the outbreak of COVID-19, they were re-scheduled to start on May 21st. The announcement was made in late April, and it came in a dire economic context, in which the Chinese economy had contracted by 6.8% in Q1 2020, the first contraction in over 40 years. The Two Sessions were thus seen as an important show of stability, as they highlighted China's embryonic recovery.

NO GDP TARGET

Nonetheless, Premier Li Keqiang did not identify a new GDP target for 2020, which broke with this particular, thirty-year tradition of the NPC. This is important in China where, under the logic of the self-proclaimed socialist market economy, performance by officials is evaluated on the basis of their compliance with growth plans. As official figures are questionable, the World Bank's estimation comes in handy. It suggests that China's GDP will grow by only 2.3% in 2020.

STABILITY OVER GROWTH

Targets were set, nonetheless, during the NPC, but they pertain to stability, not growth. The Chinese government vowed to provide the "Six Stabilities: employment, finance, foreign trade, foreign investment, investment, and expectations". In turn, Li Keqiang also promised to offer the "Six Protections": job stability, people's livelihood, businesses, food and energy security, stable industrial and supply chains, and the functioning of the lower levels of the Chinese government's five-level hierarchy.

CHINA'S CORONA STIMULUS

During the NPC, Li Keqiang also announced a $506 billion (CNY 3.6 trillion) fiscal stimulus recovery plan. An important aspect here is the increase in fiscal deficit (from 2.8% of GDP last year to 3.6%). This is the first time the deficit will rise above the 3% mark. The government also pledged to issue 1 trillion CNY of treasury bonds and to provide business cuts worth 500 billion CNY. Nonetheless, the stimulus package is well below those of the EU and the US, and China is expected to announce new packages once the economy stabilizes.

CONSTRAINED BY DEBT

One important reason the stimulus package is so low is debt. China accumulated significant debt after 2008, when a 4 trillion CNY stimulus package was injected into government-sponsored projects, such as high speed rail lines, train stations, metro systems, and airports. China's ratio of corporate debt to GDP is the highest in the world (156.7%), while its official government debt, remains low (54%). However, according to data of IIF for Q1 last year, China's total corporate, household, and government debt may, in reality, be much higher: over 300% of GDP. Overall, this would bring China's total debt to over $40 trillion.

OUR COMMENTS

MEANING OF NO GDP TARGET

This is a year of extraordinary events in Chinese economic history. Not only did the country's GDP contract by 6.8% in Q1 of 2020, marking the first contraction in at least 28 years (comparable quarterly data have only been recorded since 1992), but also no yearly GDP target was set, breaking an almost 30 year long streak. The decision to scrap the GDP target that would have been far-fetched or very low seems like the optimal choice for the Party-State, which is now focusing on stability over growth. After all, economic stability is a fundamental component of the key objective of the Party, namely social stability.

But the decision to scrap GDP target will likely have a significant impact on the overall performance of the Party-State's apparatus.The Organization Department of the Communist Party of China has long used GDP targets as an adamant part of an otherwise evolving benchmark to evaluate performance of the Party-State officials. Such a change can limit overreporting or pursuing unnecessary infrastructure projects that boost the numbers but don't necessarily result in real growth. That is why making officials focus on employment and paychecks rather than further buildup of physical assets can help the Chinese economy become more balanced. But first, there is a crisis to tackle.

UNEMPLOYMENT SECRET

A figure that is perhaps sparking even more controversy in China than the GDP figure is the unemployment rate. The government data released on May 15 reported the Chinese unemployment rate at the end of Q1 of 2020 as 6%. However, the official statistics are subject to scrutiny, as out of around 442 million urban workers, 174 million (so more than one-third), are migrants and therefore not counted as unemployed. On top of that comes the fact that, given the limited social benefits and social stigma, many people that could be counted in the statistics decide not to register as unemployed. Consequently, it is impossible to accurately assess the level of unemployment in China. (In)famously a report by Zhongtai Securities from Shandong estimated the rate at over 20% before getting censored. According to the Economist Intelligence Unit and Société Générale, the unemployment rate in 2020 is likely to hit 10% as additional 22 million urban citizens are likely to lose their jobs.

Such levels of unemployment provide a massive challenge to the legitimacy of the Party, which has long based its mandate on improving life standards and the prosperity of the Chinese population. In this context, it is important not to forget about the 8.7 million graduates that are set to leave Chinese universities this year who will be frustrated by the job market situation. This is why stability is and will remain the king for the Party-State in the foreseeable future; the uneasiness among the leadership caused by this situation may lead to a further increase of nationalistic rhetoric.

CHINA'S DEBT - WIDER PICTURE

For the last twenty years, the implicit global understanding was that Chinese savings would push forward international consumption, a position that relied on the rising wages of Chinese consumers since the reform and opening up. Chinese savings amount to 50% of income on average, which is the highest figure in the world, but these savings are essential to pay back colossal debt accumulated after 2008. Most of this debt is not visible, as it resides within local government administrations and SOEs. Nonetheless, an estimation of China's total debt (including government, corporate, and household debt) amounts to 300% of its GDP (which would be half of global GDP). The lack of transparency and illiquid, underdeveloped markets make Chinese financial markets unreliable in pinning down hard data (something that China may try to tackle through the introduction of digital currency). The problem with this post-2008 debt is that the financial stimulus that was injected into the economy at the time went towards infrastructure and construction projects, which created jobs but omitted the creation of a welfare state. On top of that, the real estate market boomed in just one decade, so purchasing a home has become extremely difficult. As a result, the high household saving rate is not destined for consumption, which means in turn, reduced demand at the global level.

This is bad news for post-COVID19 economic recovery. Over the past decade, consumer spending stopped being the main driver of GDP growth in China and was replaced by business investment. In other words, a boom in massive middle class consumption in China failed to materialize. This shortage in consumption was exacerbated by the increasingly expensive home mortgages. These high debt levels will prevent the Chinese economy from pursuing a similar role to the one it played in 2008. Back then, its debt was manageable, mortgages were cheaper, and consumer demand was still more important than business investment. In the current situation, the world should not expect China's consumers to spearhead economic recovery.

RELATED NEWS IN WEEKLY BRIEFINGS

- **Two Sessions 2020 - China's Economic Way Forward [May 25]**

SELECTED READINGS

- The Chinese Communist Party and its State - Xi Jinping's Conservative Turn - OSW (Michał Bogusz, Jakub Jakóbowski), Apr 2020
- China, Faced With Challenges, Mounts Show of Strength at Congress Session - New York Times (Keith Bradsher and Chris Buckley), May 21
- "Suspiciously stable": How China's unemployment rate is calculated - Quartz (Mary Hui), May 21

THREAD 3

THE TALES OF COVID-19 AND THE WHO

KEY SUMMARY

INVESTIGATION CALLS BUILDING UP

In the build-up to the World Health Assembly (WHA) on 18-19 May, multiple calls were made for an investigation to be started into the origins of the virus. Ursula von der Leyen stated on May 1 that she backs the creation of a transparent, international body to track the virus' origin, and dismissed arguments saying this would worsen relations with Beijing. Her statement came one day after Swedish Health Minister Lena Hallengren made known her plans to ask the Commission to launch an investigation on the virus. Other similar calls were made by Chris Patten, the last British governor of Hong Kong, Australian PM Scott Morrisson (whose country has been the most vocal on the matter), the WHO, and Angela Merkel (who has backed this idea since April 21). China retorted very clearly that it opposes any international inquiry that presumes its guilt. Despite this, on the eve of the WHA, 120 countries showed support for an international investigation.

TAIWAN CAN HELP

One other pre-WHA point of contention was Taiwan's potential right to participate as an observer, given its efficient handling of the virus (440 cases and 7 deaths to date out of a population of 24 million, plus donations of 17 million masks abroad between April 1 and May 5). Its observer status was removed in 2016, when President Tsai Ing-wen's anti-unification stance drew Beijing's ire. Taiwan managed to get support for rejoining of WHA from important countries such as the US, Canada, Australia, and Japan. In Europe, among others,France, Germany, and Lithuania lobbied for Taiwan's participation. Nonetheless, Taipei announced just one day before the WHA that it would postpone its bid, citing "allies and like-minded nations" who suggested delaying the process so that the WHA could focus on combating the coronavirus.

TWO MOTIONS EXPLAINED

The initial motion calling for an investigation, drafted by the EU and Australia, proposed an "impartial, independent and comprehensive evaluation" of "the WHO-coordinated international health response to COVID-19". Despite not mentioning Wuhan as ground zero for the virus, this initial motion did not make it to the negotiating table. Instead, the EU drafted a new, diluted motion which did not seek to investigate the origins of the virus but called for an independent and comprehensive evaluation of "experience gained and lessons learned from the WHO-coordinated international health response to COVID-19". The new motion was adopted with 110 countries in favor, including China.

TRUMP'S WHA OUTLASH

While accusing the WHO of being a “puppet of China”, US President Donald Trump lashed out at WHO Director General Tedros Ghebreyesus in a letter that accused the international body of missteps that “have been extremely costly for the world.” Among others, he criticized the WHO for praising China’s alleged transparency and for telling the world that the spread of the virus abroad was “minimal and slow”. The letter ended with a threat that the US will permanently freeze US funding and reconsider WHO membership unless it commits to “major substantive improvements” in the following 30 days. He did not end up waiting that long; on May 29 he officially announced the US will withdraw from the WHO, which generated criticism from health experts for not helping the effort to combat the virus and prompted a joint statement by High Representative Borrell and President von der Leyen, urging the American administration to reconsider departing from the WHO.

XI’S COUNTEROFFENSIVE

While Trump took repeated jabs at the WHO and its Director General, Xi Jinping scored multiple diplomatic wins for China at the WHA. He managed to avoid contested debates over both Taiwan’s membership and the independent investigation, which will now only happen after the virus is under control. Secondly, he pledged $2 billion to fight COVID-19 over the next two years, with the money destined for other countries, particularly developing ones. Importantly, he also promised that any vaccine developed in China will be made a public good.

FOLLOW-UP

Several important reactions came after the WHA. Internal Market Commissioner Thierry Breton claimed Europe could have faced the virus much better had it known in a timely manner from Beijing about its real health risks. More importantly, China decided to halt beef imports from four large Australian abattoirs, followed five days later by a decision to tax barley coming from Australia with an 80% tariff. Although lacking an official acknowledgement from Beijing, these actions were quite clearly linked to Canberra’s push for an international investigation. Belgium and Japan also met opposing discourse, after senior policy-makers in both countries stated the virus had originated in Wuhan. Chinese responses called these claims attempts to stigmatize China and politicize what would allegedly be an otherwise purely health-related issue. In addition, the virology lab in Wuhan announced that none of the viral strains in bats it was researching matched the strain of COVID-19.

OUR COMMENTS

POWER VACUUM

The dynamic surrounding the WHO is today's international politics in a nutshell. Donald Trump's United States is pursuing a unilateralist agenda, resorting to a high-pressure approach. Such moves, while effective in diverting the attention from domestic controversies surrounding the government's response to the COVID-19 pandemic, significantly undermine the multilateral international system just when a global response is needed. Trump's decision to leave the WHO is a case in point. With the multilateral order consequently eroding, China is well positioned to fill the power vacuum left by the US and pursue its own agenda of remolding the international order. An example can be found in the unilateral financial pledge made by President Xi Jinping, which will likely be channeled to support China's international projects.

In this context, it is important to take note of the EU Commission's Coronavirus Global Response, which is aimed at fostering multilateral response to the challenges of the pandemic. During the pledging event on May 4 that raised €7.4 billion, including through contributions of non-European partners such as Canada, Israel, Japan or Saudi Arabia. Despite many international leaders joining the event, China has only been represented by its EU Ambassador and made no financial pledge, while the US has not sent any representative at all. As of June 5, China decided to make a pledge of slightly over €45 million instead focusing on own global health diplomacy and domestic development of the vaccine. China's pledge is barely more than half of that of Poland, while the total amount pledged has reached €9.8 billion. This shows the challenge of the EU's attempts to pursue a constructive, multilateral agenda, amid the US-China rivalry, in which each of the two powers has an international agenda contradicting the EU's vision of the multilateral globalisation model.

This pledging effort will continue until June 27, when it will culminate in a Global Pledging Summit. If you want to donate funds for the Coronavirus Global Response, you can do so here, as explained on the Commission's website.

HOW WHO WORKED WITH CHINA

The WHO has been extensively criticised by President Trump (who himself praised China 15 times between January 22nd and February 29th) and many others over its alleged collusion with China and mismanagement of the early stages of the pandemic. Amid all that, it is important to remember that the WHO is not an executive organisation and it relies on messages from its members (including China). This reliance seems to have been the key to the organisation's dovish approach to Beijing as well as delays in addressing the threat of COVID-19.

As uncovered by great investigative reporting from the AP, China has delayed sharing vital information—such as genome sequence of the virus, detailed data on patients and cases—with the WHO, to the great frustration of the organisation's staff. Consequently, in order to encourage the Chinese government to share more data, the WHO began to portray China in the best light, something the Director General arguably took too far, which drew international attention. The fear was that if pushed too hard, China would simply restrict access to information altogether, which would have been even more destructive than the delays.

This new information paints a picture of the WHO being stuck between the US and China, trying to do the best it could with limited data, no enforcement powers, and no ability to launch an independent investigation into the epidemic. The report by AFP is highly worth a read, as it follows the exact chronology of the story. You can find it in the selected readings section.

HEALTH SILK ROAD RISES?

The COVID-19 pandemic drew international attention to China's health diplomacy, one part of it sometimes dubbed the Health Silk Road. Medical aid was offered, from Malaysia to Moldova and some countries, such as Sri Lanka, were granted concessionary loans to support their economies during the pandemic. China's health leadership has also been boosted in core forums, including ASEAN, the G20, or the Shanghai Cooperation Organization. But the Health Silk Road has definitely not been born out of the corona crisis. WHO Director Tedros Ghebreyesus praised it officially as early as August 2017, when he called it "visionary" and argued that securing the health of billions of people means to "seize the opportunities the Belt and Road Initiative provides". Now that COVID-19 has ravaged one healthcare system after another, the Health Silk Road appears salient again, especially because it could generate increased good will and demand for BRI projects that were undermined by the virus' spread. The BRI is not one coherent policy; it is made up of a plethora of projects here and there that relate to the wider BRI campaign. This flexibility is good news for Beijing because it allows it to rebrand past BRI projects as part of the Health Silk Road (and maybe even merge it with the Digital Silk Road, under the pretext of health monitoring).

As shown by Xi's $2 billion pledge of support during the WHA, the Health Silk Road is likely to expand into developing countries, many of them in Africa. However, at the current point, Beijing has prioritized bilateral, rather than multilateral, relations on health matters with African countries, which makes it perhaps more difficult to coordinate with the African Union as a whole. On top of that, Africans' view of China appears complex. On the one hand, the handling of the virus and its coverup—as well as racial incidents and the infamous mistreatment of Africans in Guangzhou—stirs critical approaches. On the other hand, any health policy will come with an economic component, which would be very important in a developing world hit by the corona crisis. Africa is highly dependent on medicine and other strategic imports from China, meaning that its leaders may also come to the conclusion that greater diversification is needed.

That being said, debt relief and economic support will be essential to keep Africa's economy from plunging, so China is bound to have a role in the recovery of the African continent. And there is also a lot of good that China can do to support Africans in their reponse to COVID-19.

RELATED NEWS IN WEEKLY BRIEFINGS

- **Investigating COVID-19 - International Consensus, International Divide [May 4]**
- **World Health Assembly - From China's Worst Nightmare, to a Dream Come True [May 25]**

SELECTED READINGS

- China delayed releasing coronavirus info, frustrating WHO - AP, Jun 3
- China outplayed the world on the day it was meant to face a reckoning over its coronavirus response - Business Insider (Alexandra Ma), May 19
- Coronavirus: Why is Donald Trump so critical of the WHO and China? - DW (Alex Matthews), May 19
- Historic health assembly ends with global commitment to COVID-19 response - WHO, May 19

THREAD 4

EUROPE RETHINKING CHINA POLICY

KEY SUMMARY

STRATEGIC VIEW

On May 25, when addressing the Annual German Ambassadors' Conference, High Representative Josep Borrell provided an overview of Brussels' evolving perspective on China and the geopolitical landscape. Naming COVID-19 as a "history accelerator" Borrell said that the EU now has to operate in a "leaderless world" seeing "the end of an American-led system and the arrival of an Asian century", where amid Sino-American rivalry threatens both the EU's globalisation model and political model. The HR urged that it is time to think boldly and make the EU "a real common strategic culture" and "follow our own interests and values and avoid being instrumentalised by one or the other." In this context, he advocated for developing a more robust strategy on China that would be based on "trust, transparency, and reciprocity", which echoed his blog post from May 15.

CHALLENGES OF CHANGE

While many agree with the need for a China rethink, questions remain. First, as shown by Rasmussen Global's audit of goals set as part of the 2019 EU-China Strategic Outlook, bold plans are only good if they get implemented. According to the audit, only one out of ten targets set out to be achieved within the first year was accomplished: releasing an EU 5G toolbox. Five other targets were only partially achieved and four were designated as failures. Second, political developments, such as the case of Hong Kong, further raised the question of the extent to which the EU is actually able to balance the complexities of its multifaceted relationship with China, particularly in regard to systemic rivalry. As expressed by Reinhard Bütikofer, the Chair of the European Parliament's Delegation for Relations with the PRC, in the context of Hong Kong situation that "it would be folly to assume that you can be systemic rivals on Monday and then go back to partnering for the rest of the week as if you were not."

HOPES AHEAD FOR GERMAN PRESIDENCY

This push for revisiting and redefining EU's China policy comes ahead of the German presidency of the Council of the European Union, which is set to start on July 1. Led by the motto "Gemeinsam. Europa wieder stark machen" (which translates as "Together for Europe's Recovery"), the presidency is set to guide the EU's economic recovery, negotiating the new EU budget, the 'Next Generation' recovery fund, and the details of Brexit. And, as indicated by

Chancellor Merkel—who faces some criticism in Germany for her allegedly soft approach to China—"relations with China will be a foreign policy priority of the Council Presidency." This is supposed to entail concluding negotiations on the CAI and further engaging China on commitments to curb CO_2 emissions per the thresholds of the Paris Climate Accord. The big event in this regard was meant to be the anticipated Leipzig Summit (also dubbed by some as 27+1), uniting 27 EU leaders, top EU officials, and President Xi Jinping. However, on June 3 the Summit was postponed by the German side, citing COVID-19 concerns. Still, hopefully the German Presidency will work towards creating a more cohesive approach towards China within the EU.

UPDATES ON CAI AND THE EU-CHINA SUMMIT

Negotiations on CAI have restarted after a pandemic-induced break. Following a round carried out in late April, the two sides negotiated the 29th round between May 25 and 29, with some progress reported. Importantly in this context, the European Commission is reportedly working on a white paper (expected to come out on June 17th) aimed at dealing with state-owned and state-aided foreign companies operating within the EU market. According to the reports, the Commission considers a two-track system, which would, on the one hand, enable the EU and its member states to impose measures to rectify market distortions caused by such state-aided actors and, on the other hand, develop an acquisition review system implemented by compulsory notifications. Such a move—clearly intended as a safety measure against a potential increase in Chinese acquisitions amid the pandemic—has the potential to shake up the CAI negotiations and the upcoming EU-China summit, which is expected to take place by the end of the month as a video conference.

NEIGHBOURS ALREADY RENOVATING

On the other side of La Manche, the UK government intensified its revision of China policy. Already at the end of April, a group of conservative MPs had formed the China Research Group aimed at stirring up debates on UK-China relations and providing some fresh thinking. Following this pattern, Prime Minister Boris Johnson ordered preparations for the so-called "Project Defend", which entails developing a plan to diversify supply chains of essential non-food products as well as plans to eliminate Huawei from the UK's telecommunication infrastructure by 2023. On top of that came the UK's call to establish a club of democracies, made of the G7 + Australia, South Korea, and India that would work on creating alternative 5G supply chains as well as decisions regarding Hong Kong, as discussed. Still, it remains to be seen whether those moves are really harbingers of a long-term, post-Brexit China strategy for the UK.

HUAWEI RETHINK

Also Huawei's already uncertain position within the EU's 5G rollout may be due for an adjustment. On May 19, the US Commerce Department instituted new export rules on semiconductor chips used by Huawei in its phones and 5G infrastructure. The rules would effectively bar Huawei from accessing vital components for their equipment. Although the company has already stockpiled an estimated two years worth of supplies, this does not constitute a long-term solution for them, particularly as a new generation of chips is already under development in the US. In the words of Huawei's rotating chairman, Guo Ping, "Survival is the keyword for us now." This also means that Huawei may not be able to rate as a reliable supplier of 5G tech for the EU simply because its supply chain is insecure. Already the company has been a subject of scrutiny within the EU, with the EU 5G toolbox, a non-binding framework advising the member states to diversify equipment suppliers and limit, albeit not ban, usage of state-backed suppliers (read: Huawei). With many auctions of the 5G spectrum across the block delayed amid the pandemic and amid diverse approaches towards tackling the Huawei question, the company's future in the European market remains uncertain. This is a big deal as, in 2019, activity of Huawei on the European market amounted to 24% of the company's revenues and roughly half of Huawei's 5G contracts were signed with European entities. But, blocking Huawei would likely come at a price for EU-China relations.

OUR COMMENTS

NEED FOR CHANGE

Josep Borrell's speech to German Ambassadors was clearly focused on the future, which remains uncertain. The shifts in the geopolitical landscape highlight how problematic the multifaceted dynamic defined in the 2019 Strategic Outlook is. Frustrated with limited reciprocity from China, the EU has been securitising its economic relations with Beijing since 2016 through a line of actions, such as development of the investment screening mechanism, the 5G toolbox, and recently discussed diversification of the strategic supply chains. But the tension between systemic rivalry and other aspects of the EU-China relations has been an underlying theme of the relationship: a status quo in itself. With both the EU's globalisation and political models being simultaneously threatened, Europe needs to give its strategic thinking a broader look.

In the context of China, this means going beyond simply further economic securitisation of its relation with China, which is seeking to prolong as much as possible the cooperation-focused approach that is becoming increasingly hard to keep in the spotlight. But maintaining the status quo of contradictions and complexities engraved in the Strategic Outlook is not sustainable. The EU needs to come up with a plan for redefining its relation with China and its role in a leaderless world.

IT'S NOT YOU, IT'S ME

The key challenge of EU-China relations is arguably not about China, but about the EU itself. In order to address such issues as asymmetrical market conditions or systemic rivalry, the EU needs to deal with the fragmentation of its decision making process, and not just in regard to China. Simply put, the EU needs more integration to protect its interests and values in relations with China. Treating this issue outside the context of the overall integration of the EU's foreign policy is likely to undermine a “real common strategic culture”, in Borrell’s words.

This is a huge undertaking and naturally one that will not be achieved easily. But hopefully this is the direction that we will see emerging through the new budget and the “Next Generation EU” recovery fund, as well as during the German Presidency. In this last regard, with the Leipzig Summit postponed, the German presidency would be wise to still use its term to host debates and pan-EU reflection on a united strategy on China. Uneasy questions should be asked not only about such issues as the 17+1 (as we discussed in our podcast with Ivana Karásková), but perhaps, even more importantly, about economic constraints on the EU’s policy on China, created by the reliance of German automotive industry on Chinese market. (As of now this reliance translates domestically to over 830,000 jobs and 2 million adjacent jobs.) One thing is certain: a new China policy has to start with introspection.

BUMPS AHEAD?

Further securitisation of the EU's economy towards China is on the horizon, as shown by the white paper targeting the state-aided actors, which is being prepared by the Commission. The Commission seeks to address the issue by allowing the EU and its member states to impose measures to rectify market distortions and to develop a compulsory notification system to review acquisitions of European companies. We are looking forward to reading the released paper, reportedly to be released on June 17, ahead of the virtual EU-China Summit. Also remember that the FDI screening mechanism, which was adopted in March 2019, will come into force this October, potentially causing more investment tensions between the EU and China. On top of that comes the potential limitation to usage of Huawei in the 5G rollout in EU markets, because of the unstable supply chain of semiconductors to the company, which makes it a far less reliable provider (with Party-State involvement considerations still remaining in place).

All this sums up to very challenging circumstances for the CAI negotiations. And the decision to postpone Leipzig until an unspecified date exemplifies a struggle to bring concrete results and progress in EU-China relations in 2020, which was supposed to be the year of intensified engagement.

RELATED NEWS IN WEEKLY BRIEFINGS

- **Updates on EU-China Summit and CAI Negotiations with China Re-think in the Background [May 18]**
- **EU's Neighbour Rethinks its Post-Brexit China Policy [May 25]**
- **Geopolitical Perspectives from Beijing and Brussels - Important Speeches by Top Diplomats Analysed [Jun 1]**
- **Priorities of the Upcoming German Presidency of the Council Revisited [Jun 1]**

SELECTED READINGS

- Annual German Ambassadors' Conference 2020: Opening remarks by High Representative/ Vice President Josep Borrell - European External Action Service, May 25
- "You Can't Be Systemic Rivals on Monday and Then Go Back to Partnering for the Rest of the Week" - The American Interest, May 28
- Europe Reaches a Tipping Point Over China's Hong Kong Gamble - Bloomberg (Alan Crawford, Ania Nussbaum, Arne Delfs), May 29

THREAD 5

EU RECOVERY PLAN - WHAT LIES AHEAD?

KEY SUMMARY

NEXT GENERATION EU

On May 27, European Commission President Ursula von der Leyen announced a proposal for an economic recovery fund, called "Next Generation EU", worth €750 billion: €500 billion in grants and €250 billion in loans. The money would be raised through loans from financial markets and it would be repaid jointly with money from the EU budget, between 2028 and 2058. The contribution to the budget per member state would be increased to 2% of GNI (upward from 1%). The money is to be allocated to help member states' investment and reform, aid private investments, and improve the EU's crisis preparedness. The countries getting the most funds would be, respectively: Italy, Spain, and Poland.

MFF 2021-2027

A second part of the recovery plan is tied to the EU's 7-year budget: the Multiannual Financial Framework (MFF). The Commission suggested allocating €1.1 trillion to the EU budget over the period between 2021-2027. A set of new taxes were proposed to alleviate the financial burden and align the MFF with the EU Green Deal and digital transformation. In exchange, budget cuts were proposed in areas of cohesion, defense, research, and administration. The Commission hopes to finalize negotiations on the draft of the MFF by the end of 2020.

THE FRANCO-GERMAN KICK START

The €500 billion in grants suggested by Ursula von der Leyen is the exact sum that Emmanuel Macron and Angela Merkel announced in their joint proposal on May 18. Merkel previously held a rigid opinion against grants, but was swayed by a ruling of the German constitutional court in Karlsruhe against the bond-buying powers of the European Central Bank. Merkel identified the ruling as jeopardizing for the future of the Union.

THE SOFTENING OF THE FRUGAL FOUR

Ever since the debate on corona bonds, Austria, the Netherlands, Sweden, and Denmark emerged as the "Frugal Four", a group that lobbied against mutualized debt and an increased EU fiscal space. Their stances have gradually changed. In March, they rejected anything over the €540 billion emergency package of the Commission. Now, they have adjusted their lobbying to claiming that the recovery should be made of loans (not grants), and that repayment should not be mutualized, but paid by the countries receiving the cash. In an example of further convergence, the Commission's proposal was not rejected by usually fiscally conservative voices, such as Austrian Chancellor Sebastian Kurz, Dutch Prime Minister Mark Rutte, or Swedish Finance Minister Magdalena Andersson. This gives hope that a slightly changed final draft will make the Frugal Four get on board with the recovery fund.

THE MONEY IS TIED TO REFORMS

Since the Merkel-Macron proposal was announced, it has been clear that the distribution of such a large sum will be conditioned on member states implementing "sound economic policies and an ambitious reform agenda". Commission VP Valdis Dombrovskis explained member states will need to agree on common recovery strategies and present reform proposals, implementation of which will be supervised by the Commission. Multiple member states expressed their support for across-the-board reforms, which is likely to become the condition of creating the fund.

MEMBER STATE REACTIONS

'Next Generation EU' received a diversity of responses. It was welcomed enthusiastically in France, Germany, Italy, Spain, and Portugal, and met minimal opposition in Finland, Denmark, and the Czech Republic. Central and Eastern Europe approved it in majority, and the only countries remaining to come on board are Sweden (the toughest in the Frugal Four) and Hungary. Viktor Orbán has called the proposal "Soros debt bondage" and stated it is "absurd and perverse", because it would be directed to wealthier member states. Nonetheless, the fund is important for Germany and for Merkel, so it is expected that the leverage of German companies in Hungary (which account for 300,000 jobs) will make Hungary change its mind.

OUR COMMENTS

WINNERS AND LOSERS

As far as policy areas go, the MFF for 2021-2027 comes with winners and losers. Naturally, the most obvious winner would be health policy, where the EU could very likely receive increased authority to prepare for crises and procure essential medicine and equipment. Another big winner would be digital policy, namely because the EU will try to structure recovery in a manner that is both green and digital. This is becoming somewhat of a self-enforcing cycle, because the pandemic has given new meaning to working from home and services provided online, so businesses that will strive will need to be more present on the www and in app stores. Proposed instruments are the Strategic Investment Facility and the Digital Europe Programme, which will also attempt to facilitate the transition to more 5G, AI, and the internet of things. Similarly, the EEAS would be granted an extra €16.5 billion for a total budget of €118.2 billion, which falls in line with the Commission's wish to have a geopolitical nature. (But, as we argued in a past weekly takeaway, this is still not enough for Borrell's EEAS to have a strong position in foreign affairs matters).

If we focus on what policy arenas are expected to lose, defence spending is set to take a hit. The European Defence Fund (EDF) will receive €8 billion, consistently lower than the €11.5 billion suggested in the Commission's 2018 proposal for the MFF (yet higher than some other sums advanced, such as Finland's €6 billion). Another feature that would see cuts is military mobility, which would decline from €5.7 billion to €1.5 billion. These cuts are in line with some (mostly CEE) member states, who don't want to sacrifice their current NATO status in exchange for an uncertain defence project within the EU. Nonetheless, France is adamant about the European defence (recall Macron calling NATO 'braindead') and will put up a fight for defence position in the budget to remain afloat.

THE ROAD TO CONVERGENCE

France and Germany initiated, the Commission proposed, now it is up to member states (acting in the Council of the EU and in the European Council) to decide what the final recovery plan and budget will look like. One defined group that has consistently taken a stance against grants are the Frugal Four, headed by Austria but with increasing presence lately by Sweden. As we argued above, the Frugal Four are gradually converging with the rest of the bloc. No reports from Vienna, Stockholm, or Amsterdam contest the plan, which means that solid negotiations are likely underway between Berlaymont and the Justus Lipsius, as well as between member state capitals. Given the proposals from Macron-Merkel and from the Commission, the final sum of Next Generation EU is likely to fall somewhere between €600-700 billion.

Otherwise, the EU seems to be moving in the three phases that former Finnish Prime Minister Alexander Stubb indicated: first, the crisis; then, the chaos; finally, the suboptimal solution. Let's be clear, Next Generation and the MFF are not 'suboptimal' in the absolute sense of the term. In fact, they manage to strike enough chords (fighting climate change, digital transformation, showing EU solidarity, providing both grants and loans) to achieve consensus. They are truly the best outcome after intense months of back and forths in Brussels and are a potential starting point for a revamp of the European economy.

RELATED NEWS IN WEEKLY BRIEFINGS

- **France and Germany Propose a Recovery Fund [May 25]**
- **EU's Recovery Plan and New Budget - Roadmap Explained [Jun 1]**

SELECTED READINGS

- EU long-term budget 2021-2027: Commission Proposal May 2020 - European Commission, May 2020
- Europe's moment: Repair and prepare for the next generation - European Commission, May 27
- Ursula von der Leyen's big gamble with borrowed money - Politico (David M. Herszenhorn, Lili Bayer), May 27

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