

GEOPOLITICAL VIEWS AND GEO-ECONOMIC CONSIDERATIONS ON THE GERMAN STRATEGY AND EU WIDER FRAMEWORK RELATIONS WITH CHINA

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Abstract

On July 13, 2023, the German Government has released the first national strategy related to approaching China in international relations, including from a geo-economic perspective. The text of the German strategy is of significant importance for other EU member states and the EU authorities, as it encloses aspects pertaining to the industrial policy and cyber-security, serving nonetheless as a use-case and / or a model for developing a coherent approach to China, including the perspective of economic diplomacy in the larger context of policy dialogues with China. From a diplomatic stance, China has anchored international relations in the countries of Central and Eastern Europe, some of which being EU members - in 2012, China forged partnerships via the "16+1" Cooperation, later extended after the Dubrovnik Summit to "17+1" by the adhesion of Greece. China looks to consolidate bilateral relations in Europe via a multi-level approach and sectorial-specific coordination (to include trade, energy, financial technologies, forestry, maritime services, etc) and the German strategy complements the projected EU-China comprehensive strategic partnership, rather than to be an alternative to it. In this context, the paper explores the implications of the German strategy towards China from the European viewpoint and analyses its value-added potential to supporting the wider angle of EU international relations towards China. The research

hypothesis is that in the current international geopolitical context related to China, the German strategy enhances at the national level the guiding principles of EU approach to managing the relations with China and adds value to EU economic diplomacy instead of duplicating it. The research methodology is focused on a qualitative analysis of documented authentic scientific public resources and synthesis of key aspects from a geopolitical and geo-economical wide angle of Sino-European relations. The conclusions draw on the fact that China acts as an international challenger, on a path to consolidate its international role and the EU and the German strategies towards China support the mitigation of exposures to economic dependencies by de-risking linkages rather than economic de-coupling from “a partner, a competitor and a systemic rival” at the same time, as designated by EU.

Keywords

17+1 Cooperation; Belt and Road Initiative; China Overseas Lending; Comprehensive Agreement on Investments; Derisking Strategy; Decoupling Strategy; EU-China Relations; German strategy to China.

“By 2049 China would become a global leader in terms of composite national strength and international influence”

Xi Jinping

19th Congress of the Communist Party of China (2017)

1. INTRODUCTION - CHINA IN THE INTERNATIONAL GEOPOLITICAL ENVIRONMENT

China has recorded an upswing on the international stage, due to the remarkable progress and fast and robust economic growth, dubbed by a considerable social prosperity in the recent decades, evidenced by an impressive reduction of the poverty in the country. After the year 2000 when China joined the World Trade Organization as full-rights member, China and

Europe benefited greatly from the increased political, economic and social exchanges.

More recently, in 2021 and 2022, these positive developments in China are countered by regressions of civil and political rights in the Chinese society (US Department of State, 2023), and China's economic policy aims to be less dependent on foreign countries in terms of investments and technology while trying to increase the dependence of the advanced economies on Chinese imports of strategic goods, especially regarding the European Union (Grieger 2020), through the implementation of the "dual circulation strategy" – a key concept of the fourteenth Five Year Plan for 2021-2025 (United Nations Development Programme 2021). Through this strategy, China aims to expand domestic demand, focus on the domestic market, improve the country's innovative capacity, reduce dependence on foreign markets, and at the same time, maintain openness to the global economy through investment and global value chains (Garcia-Herrero 2021).

Although in 2008 China supported the global growth through expansionary economic policies, today China seems to have no longer the same robustness, to ensure the continuation of the same growth rate of the economy as before the coronavirus pandemic, in the context of the challenges related to its recovery approach and structural changes (a shift to technology and services, while the real estate market seems frailer).

China still seems dependent on economic growth supported by infrastructure development and more specifically on the real estate sector, while the state-owned enterprises are subsidized, with an increasing amount of debts in the balance sheets and the regulatory environment is further reinforced to limit risks in the public sector as lender (Lam et al. 2023).

At the same time, there is a shift in views towards China, as geopolitical tensions are more evident than a decade ago. Some specific measures, that have recently been adopted, have proven to be insufficient, as financial risks, overindebtedness – as China should mitigate risks and ease the burden of around USD 9.000 billion local government debt that is recorded off balance-sheet, without resorting to major bailouts (Bloomberg 2023) and a tighter access to finance for the property sector seem to narrow and constrain growth (Reuters 2023). China is steering

towards a new growth model, focused on value-added manufacturing and green energy – on the occasion of the 76th General Assembly of the United Nations, the Chinese president announced the objectives for the Chinese economy to reach net-zero carbon emissions by 2060, before reaching the maximum level of carbon emissions before 2030 (United Nations 2020), in a long term, yet slow, process.

Regarding the foreign policy, China manifests an active approach stance and it is looking to reposition its role in the current rules-based international order (Pascu et al. 2020), having implications for the European and global security. China's ascension on the global stage started with the strategic economic policy of open doors, presented by Deng Xiaoping in December 1978 within the Third Plenary Session of the 11th Central Committee of the Chinese Communist Party. The two decades of opening up paved the way later on, for China's adhesion to the World Trade Organization in 2001.

As a WTO member, China has adopted a development model oriented towards attracting capital and technology on the one hand, and production for export on the other. This orientation allowed for prolonged economic growth and a growth strategy based on investments in infrastructure, which allowed China to emerge as a benchmark model of development for other economies (Ferchen 2020). Thus, China acquired the ability to engage internationally, seeking to challenge a revision regarding the "international economic order" – a concept enshrined in the United Nations Declaration in 1974, amid attempts to correct imbalances between advanced and developing economies at that time (United Nations 1974).

In the framework of the Bretton Woods monetary system, the US and the International Monetary Fund routinely played the role of lenders of last resort for states in situations of macroeconomic imbalances and fiscal instability. Sometimes, such sovereign financial distress determined the need to restructure the sovereign debts of distressed states or even enter into situations of default or insolvency, when it was not possible to reach a global agreement negotiated with the creditors under the framework of the Bretton Woods.

As a member of the International Monetary Fund, China aims to hold a significant global lending position by strengthening its role as a major

international financier. Each IMF member country has a "quota", based on its position in the World Economy, which determines its contributions to the fund as well as its voting weight within the institution and the access to emergency financing. At present, China's quota of 6 per cent is less than Japan's, despite its larger share of global gross domestic product (Smith 2023). As the IMF's largest shareholder, the US exerts 16.5 per cent of the votes, giving it veto power over quota decisions (International Monetary Fund 2023a), which require 85 per cent support. The IMF's board of governors conducts quota reviews at least every five years. The last time it agreed changes was in 2010. Since then, China's economy has grown considerably. The changes took effect in 2016 (International Monetary Fund 2023b).

A recent multi-researcher joint analysis under the aegis of AidData, World Bank, Harvard Kennedy School, Kiel Institute for the World Economy highlights China's endeavours to strengthen its role as a key lender to emerging economies, as an alternative to multilateral development bank financing and financial support of the Bretton-Woods institutions in situations of balance of payments difficulties. The report highlights that between 2000 and 2021, China undertook 128 default-rescue operations for the sovereign debt of 22 countries in public financial distress, totaling US\$240 billion, most of this cumulative sum under the form of refinancing support (Horn et al. 2023).

The Belt and Road Initiative is a core element of China's foreign policy strategy and in 2017, was included in the Constitution of the Communist Party of China. Two years later, in 2019, China organized the Second Forum for International Cooperation for the Belt and Road Initiative. The event has been chaired by the Chinese President Xi Jinping, which brought together leaders from 40 countries and international organizations. Internationally, the event was perceived as a way for China to demonstrate some opening up to the reform of the Belt and Road Initiative (Belt and Road Forum Communiqué, Point 30 2019), subsequent to international criticism to be a way increase in the dependency of the beneficiary states of Chinese investments. Through the main financing vehicles, China Development Bank (OECD 2018) and Export-Import Bank of China (Reuters 2019), the beneficiary states ended up holding an unsustainable long-term debt to China, repaying for projects with questionable transparency. Thus,

the Belt and Road Initiative may be seen as a geopolitical tool to consolidate China's international position (Ruwitch 2019).

2. RESEARCH METHODOLOGY

The research methodology, to approach the geopolitical and geo-economic relations between Germany and EU on one side with China on the other side, pertains to the cause-effect analysis and the dynamics of changes over time and to the synthesis of documented authentic public resources, giving substance to the main findings.

The paper is developed using the following methods / techniques of investigation and analysis: (i) qualitative research, to explore in a regressive manner / in a backward looking approach, how facts and strategies might explain the outcome, (ii) descriptive research and observations to investigate the causes of geopolitical tensions and geo-economic pressures, (iii) analytical research interpreting the consequences of the root-cause factors impacting the bilateral relations of EU-China and Germany-China, and (iv) applied research, on taking stock on the key analyses and scientific literature on the topics of China and its geopolitical policies related to EU.

3. THE STRATEGIC APPROACH OF GERMANY OF MANAGING RELATIONS WITH CHINA

On July 13, 2023, the German Government published the first strategy on economic relations with China (Federal Government of Germany 2023a). The text is of particular importance, as it also includes aspects of industrial policy and cyber security, being able to serve as a model of approach in economic diplomacy relations with China for other states in the European Union, and it also has relevance in the wider context of the EU's China strategy. On the same

day, the German Foreign Minister said that Germany is addressing these challenges of industrial policy and cyber security related to China while continuing to strengthen the economic exchanges and cooperation with China (Federal Government of Germany 2023b).

China remains an indispensable partner for the European states in all the international forums (G20, G7, Bretton-Woods institutional system, UN, etc.), at least in what concerns the combating of climate change, solving the debt crises of states with a high risk of insolvency, while ensuring security food supply and thus, the global stability. At the same time, China is a partner, a competitor and a systemic rival for the member states of the European Union. The strategy of the German federal government in the relationship with China takes into account and develops the national strategy, in line with these dimensions.

The new German strategy could lead to one of the most profound transformations in German foreign policy and economics as it is a reconsideration of the guideline of the European Union's relations with China which addresses "the change of China's policies towards the EU through trade", a concept that has also guided the German-Chinese relations. The year 2022 was the seventh consecutive year when China stood as Germany's first strategic trading partner, with a trade volume of EUR 298.9 billion in goods (DeStatis 2023).

The strategy presents the German federal government's vision of the current status and outlook on the relations with China and enables Germany to capitalize on the opportunities arisen in the current global environment. The German strategy encompasses ways and tools to continue the cooperation with China while facing systemic competition and rivalry, without undermining democracy, sovereignty, prosperity, partnerships or the overall security. The strategy lays the foundation for the operational framework in which individual ministries can coherently formulate policies towards China under the German federal and European coordination at the same time.

From this stance, Germany has a close approach to the current 2019 EU strategy from a derisking perspective (European Commission 2019), rather than the US approach of decoupling from China (Glaz et al. 2023). Derisking measures focus on diminishing the German dependency on China regarding the technology and

the electronics domain, as well as the rare earths and the materials needed in the energy transition pathway, by diversification of the global value chains. Still, the largest German companies have investments in China and continue to consolidate the business, i.e. in the vehicles manufacturing sector, the chemical sector and the green energy sector.

The German federal government strategy has been well received by the German industry, however opinions range between derisking and decoupling. For instance, the Federation of German Wholesale, Foreign Trade and Services considers that renewing the viewpoint on China was long overdue and appreciates the rethinking of the current supply chains system (BGA 2023). The Federation of German Industries supports the strategy as well and its balanced approach of not decoupling with China (BDI 2023). However, the German Economic Institute raised some concern on the lack of details given on the derisking process and the sectors involved (Matthes 2023).

China, on the contrary, was critical of the paper. The Chinese Embassy in Berlin defined the strategy as “ideological” and advocated for more pragmatic and “rational” relations. China views the derisking policy as counter-productive and to have the potential for intensifying risks artificially (Chazan et al. 2023). Equally, the Chinese Foreign Ministry denounced how “drawing a line according to values and ideologies and advocating so-called competition of systems” undermine the China-Germany cooperative partnership. It also described the derisking concept as a form of protectionism (Government of China 2023).

4. EU - CHINA GEOPOLITICAL RELATIONS FROM THE ECONOMIC DIPLOMACY VIEWPOINT

The EU standpoint has been emphasized on June 30, 2023 (European Council 2023) announcing the newest coordinates on the EU-China relation. China is nominated as a partner, but also a competitor and a strategic rival. Under such a dualistic approach, the EU constructively seeks to frame and develop relations

in a regulatory environment, founded on mutually respected agreements, and on compatible and aligned positions regarding some important global challenges such as climatic changes or granting humanitarian aid. However, to my views, the regulatory environment may be of a "state-driven" model (more to the Chinese approach to regulation), of a rights and obligations model (closer to the European Union approach to regulation) or of a market-driven model (a more pragmatic US-style approach to regulation). Fine-tuning the regulatory approach of the European Union to China is an ongoing process where the economic diplomacy and the common grounds of geostrategic interests of both parties might play a larger role, should bridging the gaps of divergent positions be fostered by a successful political dialogue between the European Union and China. Still, China is seeking a stronghold with the economies in the Central and Eastern Europe, as gateway to the European Union (Colibasanu 2020).

EU is pursuing the deployment of the "open strategic autonomy" concept, all while reaffirming its global role and strengthening the balancing act of realigning the economic ties with China. EU noted that "EU-China bilateral relations have deteriorated, notably related to a growing number of irritants (i.e., China's counter-measures to EU sanctions on human rights, economic coercion and trade measures against the single market, and China's positioning on the war in Ukraine) ... At the same time, the EU has remained committed to engagement and cooperation given China's crucial role in addressing global and regional challenges" (European External Action Service 2022).

The European Union and China continue to be important trade and economic partners. The European Union aims to ensure a level playing field in the bilateral relations, so that the trade and the economic relations be more balanced, reciprocal and mutually beneficial. The European Union is committed to reducing critical dependencies and vulnerabilities from China, including in aspects related to the supply chains, including the reduction of risks and diversification of strategic partnerships, through the EU's vision of achieving the open strategic autonomy. The Comprehensive Agreement on Investments (European Commission 2020a), whose negotiations "ad principia" ended on December 30, 2020 aims to give European investors improved access to the

Chinese market (European Commission 2020b). At the same time, other geopolitical considerations have been raised by EU in relation to China.

The EU-China dialogue should be continued to enhance the human rights abidance and safeguarding in China. European concerns are related to usage of forced labor, the mistreatment of workers, respecting the minority rights and the established autonomy of some provinces, such as Hong Kong. Such topics continue be included in the EU agenda of ongoing discussions with China. For instance, the European Union "strongly condemned" the Chinese government-led system of forced labour and the rights breaking of minorities in autonomous provinces. (European Parliament 2021).

In the wider context of the increasingly pronounced orientation of the EU member states economies towards greening and a neutral footprint of carbon emissions on the environment through the EU Green Deal strategy, China seems to acquire a geopolitically strategic position of influence over the European economies, especially through an increasingly pronounced control of the distributional value chains for critical minerals that are most needed in the processes of new technologies, such as electric vehicles, solar panels, etc., as well as market-influence on European industries that depend on these raw materials. This EU relationship with China can strengthen and expand the European dependency on Chinese companies that are producing and exporting these critical raw materials and minerals, augmenting the strategic upstream position of Chinese companies in the international market for rare metals and resources - essential to new technologies. The Center for European Policy Studies estimates that China currently has a market share of about 60 percent for the extraction of rare earths, 91 percent for the processing of these special metals, and 94 percent for the production of industrial magnets (Rizos et al. 2022).

China shifted the focus to produce more electric vehicles and batteries by first developing and acquiring new lithium projects and then, securing the supply chains for the manufacturing sector. China's outbound mining mergers and acquisitions activity has risen significantly over the past 10 years, slightly exceeding USD 7 billion in 2019. Interest in cobalt and lithium as options for battery metals has risen in recent years, while gold and copper (China is the

third largest global producer) have remained important targets for the Chinese authorities (Holden et al. 2022).

The latest challenge to globalization is China's stance on Russia and Ukraine, a geopolitical challenge with strategic implications for the international fora. In line with the Versailles Agenda (EU Council 2022) where the EU strongly condemned the aggression, the EU member states continue to appeal to China in order to assume a supportive role to mediate the diplomatic dialogue to cease the conflict, including on the occasion of the G7 Leaders' Summit in May 2023 (G7 2023). On the other hand, China manifests strategic territorial interests South-East China Sea pledged by the policy of "One China" (Mission of the People's Republic of China to the EU 2022), with consequences to prosperity and to the regional and global security.

5. VIEWS OF GEOPOLITICAL RESEARCH THINK-TANKS ON SINO-GERMAN RELATIONS

An analysis conducted by the Ifo Institute, which evaluated the value-added linkages among supply chains, pointed out the "important, but not primordial" dominant role of the German economy in relation to China. Germany has a role as supplier of capital for China and, at the same time, a role of receiver market for technologically intensive industrial goods made in China and key raw materials that are imported from China (Baur et al. 2022). However, in a subsequent survey by the Ifo Institute, 46 percent of German firms in the manufacturing sector said they currently depend on important intermediate factors of production in China. Among these companies, almost half of the firms plan to reduce imports from China in the future. The most commonly cited reasons for the reduction in imports from China were the management's desire to reduce dependencies and to increase diversification, the rising transportation costs and the disruptions in international transportation chains, as well as the uncertainty regarding the Chinese policies.

In implementing its new strategy, the German government will likely face difficulties in striking the right balance between the different sets of risks that China presents (Colibasanu 2023), the dynamics of which are a challenge for possible projections and econometric scenarios.

A wide range of experts believe that this strategy can be seen as a new "Zeitenwende" (on February 27, 2022, the German government announced a radical change in security and foreign policy following Russia's invasion of Ukraine, called this way by Chancellor Olaf Scholz. Although the official government translation for this term is "change of times", the original term has a more nuanced meaning, meaning "a geopolitical shift"). Although evolutionary, as a result of tripartite negotiations in the German government, the German Strategy towards China is not seen as revolutionary enough to really produce the effects intended by Germany, to change China's policies and bilateral relations. To their opinion, China is positioned within the document in a too balanced manner, in the frame of "partner - competitor - systemic rival triangle" (Atlantic Council 2023).

The European Council on Foreign Relations believes that the German strategy will have special significance for China (Oertel 2023), from an industrial perspective (Botschaft der Volksrepublik China in der Bundesrepublik Deutschland 2023), from the perspective of German investment in the Chinese economy (Generalkonsulat der Volksrepublik China in Frankfurt am Main 2023), and from the perspective of the dissemination of German technological advances in China (Erling 2015). In my view, given the fact that the German economy is the largest in the European Union and the fourth economy globally, the way in which the German strategy regarding relations with China fits into the global context of interest-based affiliations, such as "friendshoring" / "nearshoring" will guide the prosperity of the German economy and shape the ability of the European Union to maintain its position as a global economic power and benchmark or reference authority in regulatory matters.

In a context where China actively takes part in the international institutional frame under the aegis of G-20, including under a very pressing aspect of public debt and sustainability (*Debt Service Suspension Initiative*) next to IMF and the World Bank (Savage 2023), as well as to discussions regarding the restructuring

of these debts under the *Common Framework for Debt Restructuring* (Butler et al. 2022), in March 2021, AidData together with Georgetown University Law Center, Peterson Institute for International Economics, the Center for Global Development and Kiel Institute for International Economics issued a joint report entitled „*How China Lends: A Rare Look into 100 Debt Contracts with Foreign Governments*” (Gelpern et al. 2021).

The report presents a significant importance from a geopolitical and economic perspective, as it compares a set of Chinese lending contracts underwritten mostly by the Export-Import Bank of China (China Eximbank) and China Development Bank (CDB), commercial banks acting as special purpose vehicles of state policies and contributing to the core Belt and Road Initiative as key foreign policy economic tool for the Chinese authorities. Usually, China is lending bilaterally and is also open to lending multilaterally on occasions. The report describes the differences on how China lends by comparison to classic multilateral development banks and the IMF / World Bank, as well as international private creditors (The Paris Club). These differences in Chinese lending can be ascribed to four main aspects:

- Most credit agreements with China contain unusual confidentiality clauses for public debt loan contracts, which have been introduced since the inception of the Belt and Road Initiative. According to the report, confidentiality clauses would give rise to the problem of "secret debts" / "hidden debts" to debtor countries with emerging economies and it would make it difficult to calculate the debt sustainability of these countries for any multi-stakeholder debt-restructuring initiative.
- The contracts offered by China's official lenders expressly oblige borrowers to exclude Chinese-financed debt from the sovereign debt restructuring initiatives under the international framework of the Paris Club or any other multilateral restructuring initiative involving transparency.
- Chinese contracts contain clauses that tend to give China a relational geopolitical power over debtor countries and a stronger influence over the domestic and foreign policies of these states.

- Chinese lending to foreign countries requires the maintenance of special accounts for risk management purposes, pressuring the developing countries' foreign exchange reserves and affecting the accuracy of international creditors' analysis of these countries' ability to service their debts further into the future.

6. CONCLUSIONS SUBSEQUENT TO THE CHINA-RELATED GERMAN STRATEGY DEPLOYMENT

The German strategy was published at a time when trade relations with China cause structural current account deficits for the balance of payments for most states that import from China, and public debt and the financing of current account deficits are key geopolitical issues, alongside other issues critical to the global economy related to trade, technology and industrial policy.

Beyond any German or European strategy paper, there are still fundamental differences of opinion on Chinese policies, particularly on human rights, individual liberties and a number of issues regarding the application of international law, respect for international order and the interpretation of multilateralism.

Germany continues to have a major interest in the Chinese state continuing to open its internal market to European companies and homegrown products, establishing rule of law structures and fair social systems, allowing greater political and economic participation at the social level, resolve minority issues peacefully and with respect for human rights, making commitments at the level of international institutions and in support of a resilient rules-based global system. Germany's China Strategy is a good national instrument that complements, deepens and supports the European Union's relations with China. The German strategy aims to significantly reduce dependencies on Chinese value chains, maintain industrial competitiveness despite supply imbalances of rare metals and essential raw materials in the process of greening the economy for a carbon neutral footprint by 2050 (according to the framework European Fit

for 55 and EU Green Deal), improve digitalisation and take a clearer stance towards China's assertive actions.

This strategy should enable Germany to reduce geo-economic risks, especially in energy sector, in line with the European Union stance (European Commission 2022a, 2022b) and strengthen Germany's position in economic diplomacy with China, without risking a decoupling of economic growth and long-term development. Ultimately, any European strategy in relation to China should achieve the goals of a relation that is fairer, more sustainable and more reciprocal.

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