



ORDER from **CHAOS**
Foreign Policy in a Troubled World

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China's Global Rise

Can the EU and U.S. Pursue a
Coordinated Strategy?

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ABOUT THE ORDER FROM CHAOS PROJECT

In the two decades following the end of the Cold War, the world experienced an era characterized by declining war and rising prosperity. The absence of serious geopolitical competition created opportunities for increased interdependence and global cooperation. In recent years, however, several and possibly fundamental challenges to that new order have arisen—the collapse of order and the descent into violence in the Middle East; the Russian challenge to the European security order; and increasing geopolitical tensions in Asia being among the foremost of these. At this pivotal juncture, U.S. leadership is critical, and the task ahead is urgent and complex. The next U.S. president will need to adapt and protect the liberal international order as a means of continuing to provide stability and prosperity; develop a strategy that encourages cooperation not competition among willing powers; and, if necessary, contain or constrain actors seeking to undermine those goals.

In response to these changing global dynamics, the Foreign Policy Program at Brookings has established the Order from Chaos Project. With incisive analysis, new strategies, and innovative policies, the Foreign Policy Program and its scholars have embarked on a two-year project with three core purposes:

- To analyze the dynamics in the international system that are creating stresses, challenges, and a breakdown of order.
- To define U.S. interests in this new era and develop specific strategies for promoting a revitalized rules-based, liberal international order.
- To provide policy recommendations on how to develop the necessary tools of statecraft (military, economic, diplomatic, and social) and how to redesign the architecture of the international order.

The Order from Chaos Project strives to engage and influence the policy debate as the United States moves toward the 2016 election and as the next president takes office.

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Introduction

China's emergence as a global economic power and its fuller integration in the international order are among the principal policy challenges facing Europe and the United States in the early 21st century. At the time of Beijing's entry into the World Trade Organization (WTO) in 2001, China (though already growing rapidly) was in global terms an economic actor of limited consequence. A decade and a half later, China's transformation is without parallel in economic history. Over the past 15 years, China has experienced an eightfold increase in GDP, enabling it to serve as the primary engine of global economic growth in the early 21st century. It has leapfrogged from sixth to second place among the world's economies, trailing only the United States in absolute economic size. In addition, China has become the world's leading trading state and is now the second largest source of outward foreign direct investment.

Change of this magnitude has enhanced China's political power and economic leverage. It has also stimulated China's internal economic evolution, simultaneously expanding the power of state-owned enterprises (SOEs) while also contributing to major growth in the private sector. China has also begun to think bigger, devoting increased attention to the rules of global economic governance. Although Beijing insists it has no intention of supplanting the existing international order, China contends that changing power realities will require modification of global rules.

China's heightened ambitions are occurring amidst a wrenching transition in the Chinese economy. At earlier stages of the country's economic

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reforms, China's lower labor costs conferred ample advantage to Chinese producers of consumer goods. As economic growth has slowed, Chinese policymakers increasingly call for innovation and new product development to facilitate advancement to higher levels of development. These goals presume greatly increased investment and technology acquisition in the world's more advanced economies. But slowing Chinese growth threatens to limit investment opportunities within China for the EU and the United States. China's economic practices and priorities thus pose the issue of compatibility with the policy expectations of the advanced industrial economies. Reconciling these expectations have therefore become defining issues in both Europe and the United States.

Increased Chinese expectations were apparent in the September 2016 annual meeting of the G-20, hosted by China in Hangzhou. China's President Xi Jinping outlined an agenda for renewed global growth and the transformation of the G-20 into “an effective global governance mechanism,” declaring that China would assume a much more prominent leadership role. In his keynote address to the Business 20 summit prior to the opening of the G-20, Xi described China's future development tasks in global terms. Declaring that “China [is] moving toward the world and the world [is] moving toward China,” Xi stated the country's continued economic advances would focus on “the building of a more just and reasonable international order.” What might these aspirational declarations imply for the global economy, and for the United States and Europe in particular?

A successful transition to a new economic order that more fully reflects China's increased economic weight while remaining mindful of existing international practices will require far greater policy coordination between the EU and the United States. But the dynamics have changed profoundly from the earlier stages of the reform process. In the past, China emphasized purchase of treasury bonds, but its increasing focus is on asset purchases and mergers and acquisitions abroad. Though still devoting major efforts in manufacturing, its economic horizons extend increasingly to finance and monetary policy, and to the acquisition of high technologies that will ultimately enable China to become a global economic competitor.

Trade and investment with China thus seem almost certain to accelerate in future years. In light of these possibilities, the EU and the United States

are deeply engaged with China in various governmental and corporate dialogues across a wide array of economic policies and practices. These policy exchanges reflect the combined economic strength of Europe and the United States; their central role in innovation and product development; and their deep commitment to open, market-based economic principles. According to World Bank data for 2015, the EU and the United States account for 46.1 percent of global GDP.¹ These two power centers also retain major advantages in a wide array of advanced products and industrial technologies in which China displays growing interest. Can the United States and the European Union (even following the United Kingdom's withdrawal from the EU) develop and pursue shared policy approaches to the China challenge, and what are the implications if they cannot?

The United States and the EU have both wrestled with China's economic rise, but seldom in highly coordinated fashion. Though officials on both sides of the Atlantic with responsibilities for trade and finance interact regularly, these relationships do not extend to all policy realms. To an extent, these highlight differences between U.S. and EU policy concerns, as well as competing corporate interests across the Atlantic and within the EU. Ten years ago, the efforts of France and Germany to lift the 1989 arms embargo against China were aborted in the face of strong opposition by the George W. Bush administration. This placed additional strain on an already tense trans-Atlantic relationship in the aftermath of the 2003 Iraq war and the diplomatic fallout between Washington and various European capitals.

These policy differences highlight the absence of a European equivalent to the military-strategic competition between the United States and China. Some European countries (in particular, France and Germany) have developed bilateral exchanges with China on politico-strategic matters, including piracy, cybersecurity, and terrorism. But the mechanisms within various EU member states on possible sale or transfer of defense-related technologies (with the exception of France²) are not nearly as developed in Europe as in the United States. At the same time, the EU's institutional practices are distinct from those of the United States, especially the need to craft a poli-

¹ "The EU in the world - economy and finance," Eurostat, http://ec.europa.eu/eurostat/statistics-explained/index.php/The_EU_in_the_world_-_economy_and_finance.

² Since 1949, an Interdepartmental Commission on the Export of Armaments and Technology Transfers (CIEEMG), under the French Prime Minister's Office, has advised the government on these issues.

cy consensus among all member-states. The importance of bridging these potential divides can only grow, especially as the United States and various European states approach transitions in political leadership.

The stakes for Europe in China's economic transformation seem especially significant. Beijing's efforts to expand its economic and infrastructural involvement across continental and maritime Asia (to be discussed later in this paper) presume the establishment of increased connectivity between China and the economies of Europe, which serves as the terminus of Xi Jinping's "One Belt, One Road" initiative. As recently noted by former U.S. Treasury Secretary Henry Paulson, over the past decade "Europe has consistently outpaced the United States as a major recipient of Chinese money." In 2012 alone, he observes, "Chinese investments in Europe...were 50 percent higher than in the United States."³ This trend could readily accelerate in future years.

In addition, Chinese strategists have for many years characterized Europe as an emergent pole in a multipolar international system. For Beijing, multi-polarity reduces the singularity of America's global power and influence, without directly challenging U.S. leadership. Europe envisions multi-polarity as a means to achieve a more balanced yet closely connected relationship with the United States. But fully enmeshing China in the region's future poses risks as well as opportunities, especially for Europe's major economies. The EU faces dilemmas and complexities in developing a comprehensive approach to China policy, as distinct from country-specific strategies. This challenge will be even greater with the U.K.'s withdrawal from the EU, diminishing the possibilities of a unified European voice.

It seems very doubtful that China believes that it can detach Europe from its enduring economic, political, and security bonds with the United States, though it has an interest in eroding them. Leaders in Beijing recognize important differences between China's relations with the EU and its larger geopolitical competition with the United States. In Chinese strategic thinking, Europe does not represent a rival power center comparable to the United States. As a union with a current membership of 28 states (many of

³ Henry M. Paulson, Jr., *Demystifying Chinese Investment in the United States*, Paulson Papers on Investment, September 2016, p. 6.

whom face very difficult economic circumstances), the challenges of policy coordination are substantial. At the same time, there is no overt security rivalry between the EU and China, a factor that Chinese leaders believe can work to their advantage. But the deep commitment of European states to a rule-based international order raises the issue of how China seeks to accommodate to EU norms and practices.

China's increasing economic and financial weight touches upon all major issues in the global economy. The advanced industrial states therefore need to fully assess China's economic policies and practices and how they could affect the future order. These issues range from the rules governing trade, investment, and finance; addressing major imbalances in trade relations; cybersecurity; maritime security; climate change; terrorism; environmental degradation; global poverty alleviation; the role of nongovernmental organizations; the evolution of civil society; and intellectual property rights, to name some of the more important areas. Moreover, these issues concern the future of governance within China as much as governance between China and the outside world.

In this paper, we explore how Europe and the United States might move toward more complementary conceptions of their respective relationships with China. Though there are areas of commonality between Europe and the United States, their separate identities and interests also reveal significant differences, if not outright divergence. EU-wide and country-specific engagement with China have accelerated dramatically over the past decade, underscoring the challenge of coordinating EU and U.S. policy approaches.

Sustainment of the global economic order in the absence of China's full commitment to existing practices and norms would prove very difficult, especially if China is intent on developing alternative concepts of global governance. The United States and Europe thus face a common strategic task. Both must ensure that China's increasing power does not undermine the principles and policies that have enabled unparalleled economic prosperity across multiple decades. They must reaffirm a shared commitment to this institutional framework, while enabling China to emerge a full-fledged participant in the global economy.

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The draft version of a new EU China strategy, released in June 2016, sought to address many of these challenges.⁴ The document reaffirmed and extended the logic of comprehensive engagement with China. But it did not explicate the potential contradiction between the desire to elicit China's "more active participation in global governance, security, and defense," while also voicing concern about China's "increased assertiveness." Though there is clear overlap with U.S. policy concerns, the EU document is less hedged than comparable U.S. policy statements. It offers numerous "shoulds" to guide EU policies that seem largely unobjectionable (for example, advancing goals in Chinese economic reform, enhancing reciprocity and fairness in economic competition, increasing attention to the rule of law, heightening transparency and connectivity, and pursuing a shared commitment to global public goods and the protection of human rights). But it does not pose the equivalent "what ifs": What if the expectations underlying EU strategy are not met? It also does not specify how the EU should measure progress toward various policy goals, and how (if at all) the EU should respond if China does not meet EU expectations.

The United States and Europe have grappled with trade issues involving China for decades. The protracted negotiations between Washington and Beijing over normal trade relations date from the Clinton administration, culminating in a final agreement in 1999. Yet in 2004, when 12 new member-states joined the EU, China still considered Europe a partner of much lesser consequence. But trade and investment levels between Europe and China already approach or in some areas exceed the U.S.-China economic relationship. China has possibly concluded that Europe has advantages as a long-term partner greater than the possibilities with the United States. But the trans-Atlantic allies do not yet seem wholly mindful of the need to more closely examine their respective China strategies, and to determine how they can be more effectively coordinated.

There is also a clear need to better grasp how China views its policy strategies toward Europe and the United States, and the relative importance that China places on long-term relations with both power centers. China deals very extensively with companies and governments at the state and city level in the United States. But the executive branch and the U.S. Congress play the dominant role in U.S. policymaking toward China. By contrast, China's

⁴ "Joint Communication to the European Parliament and the Council – Elements for a new EU strategy on China," European Commission High Representative of the Union for Foreign Affairs and Security Policy, June 22, 2016, http://eeas.europa.eu/china/docs/joint_communication_to_the_european_parliament_and_the_council_-_elements_for_a_new_eu_strategy_on_china.pdf.

EU policies reflect the wide diversity of countries, regions, and institutions across the European continent, with China especially mindful of how these differences can work to its advantage. Europe's diminished economic growth has also enabled China to capitalize on its growing financial and economic weight. But this underscores Europe's increased need to ensure that the EU's equities are protected at a time of economic vulnerability in much of Europe, even acknowledging the differing interests of various states and firms.

China's expanding economic profile

In the late 1990s, China first began to explore the possibilities of a “Going Out” strategy (走出去), much of it designed to heighten the profile and activities of leading state-owned enterprises (SOEs). The explicit purpose was to acquire energy and raw materials needed for China's domestic development, with China increasingly in an ownership role. First begun under President Jiang Zemin, the program accelerated rapidly under his successor Hu Jintao, following China's entry into the WTO. It resulted in a two-track strategy: extensive purchases and investments in lesser-developed but resource-rich regions, and an extraordinary expansion in the export of Chinese consumer goods, especially to the developed world.

Fueled by its membership in the WTO, China's economic transformation in quantitative terms has been staggering. The country's GDP increased from \$1.33 trillion to \$10.86 trillion between 2001 and 2015. According to WTO data, China is now:

- the world's second largest economy in GDP terms;
- the largest merchandise exporter;
- the third largest merchandise importer (the EU is second);
- the fourth largest commercial services exporter;
- the third largest commercial services importer;
- the first destination for inward Foreign Direct Investment (FDI) among developing countries (fourth in the world after the EU, the United States, and Hong Kong); and
- the largest source for outward FDI among developing countries

Under the terms of WTO accession, China pledged to extend non-discriminatory treatment to all WTO members within a 15-year transition period prior to being granted full market economy status (MES). By December 2016, foreign individuals and enterprises (including those not invested or registered in China) were to be accorded treatment no less favorable than that accorded enterprises in China with respect to the right to trade.

China's WTO Accession Protocol of 2001 (approved by all WTO members including the United States and the EU), presumed—according to the Chinese side—that designation of full market economy status would occur no later than December 11, 2016. But this stipulation has embroiled China and its EU partners in major disputes over China's fulfillment of its obligations. These issues pertain directly to the role of China's SOEs, which retain highly protected status within China.

Following China's WTO accession, there was a major expansion in Chinese exports of machinery and industrial products (including consumer electronics) to developed economies and to the less developed world. Leading American and European firms also greatly expanded their corporate presence in China and deepened in-country business and technical cooperation in numerous sectors. But as the Chinese economy continued to grow, there was a parallel expectation among Western firms of enhanced access into long-protected sectors of the Chinese economy, including areas where the EU and United States enjoyed comparative advantage. Despite repeated Chinese pledges of increased receptivity to external investment, these pledges have frequently failed to meet expectations, leading both American and European trade organizations to voice increasing doubts about longer-term business prospects in China.⁵

Moreover, slowing economic growth within China has triggered intensive internal debate on the sustainability of the economic model that propelled China to the front ranks of global exporters. The country's revised economic strategy presumes movement away from export-led growth and toward longer-term industrial innovation and product development. But the after-effects of years of double-digit growth persist. Breakneck industrial

⁵ "European Business in China Position Paper 2016/2017," European Union Chamber of Commerce, <http://www.europeanchamber.com.cn/en/publications-position-paper>; "2016 American Business in China White Paper," American Chamber of Commerce in China, <http://www.amchamchina.org/policy-advocacy/white-paper>.

expansion resulted in overcapacity in steel, cement, and other commodities, with Chinese SOEs increasingly looking to external markets to offload excess production.

This prospect has created growing unease in the major European economies. To be sure, there is a long history (in Europe more than in the United States) in protecting domestic producers in important industries such as steel. This has assumed increased salience in view of the economic slowdowns across Europe. Some foresee the prospect of China unloading surplus products in Europe without honoring various anti-dumping provisions, and without equivalent opportunities for investment in China. As one EU official remarked in an interview during this research, some European economic experts envision Chinese trains arriving in Europe loaded with surplus goods, with the trains then returning empty to China.

As Europe confronts the prospect of continued sluggish growth and high unemployment, this pessimistic assessment cannot be lightly dismissed. According to one European Commission senior official interviewed for this research, full market economy status could result in the loss of 200,000 jobs across Europe. As the December 2016 deadline approaches, there are differing interpretations in the United States and Europe of the WTO protocol governing determination of market economy status. While U.S. officials have broached anti-dumping provisions in exchanges with Chinese counterparts, EU institutions have been discussing market economy status in greater detail. After some initial equivocation, the EU adopted a clearer policy stance. The European Commission declared that the five criteria for market economy status (MES) according to EU standards have not been met.⁶ In a non-binding vote in May, the European Parliament overwhelmingly rejected granting MES to China.⁷ Heated discussions followed in Brussels and in European capitals over the summer.

In July 2016, the European Commission shifted the focus from the possible recognition of MES for Beijing to the development of a new European

⁶ "Commission Staff Working Document on Progress by the People's Republic of China Toward Graduation to Market Economy Status in Trade Defence Investigations," Commission of the European Communities, September 19, 2008, http://trade.ec.europa.eu/doclib/docs/2009/june/tradoc_143599.pdf

⁷ Gary Clyde Hufbauer and Cathleen Cimino-Isaacs, "The Outlook for market economy status for China," Petersen Institute for International Economics, April 11, 2016. <https://piee.com/blogs/trade-investment-policy-watch/outlook-market-economy-status-china>.

trade defense system that should be applied to any non-EU state, regardless of its political-economic regime and structure. EU Trade Commissioner Cecilia Malmström said there would be no distinction between market and non-market economies in future EU trade policy decisions. Her colleague, Commission Vice President Jyrki Katainen, also underlined that the EU will have to adjust its system to that of the United States, which has tougher trade defenses against dumped and subsidized goods, and rely on international prices as a benchmark to determine whether a country dumps its products.

The centrality of economics, but what kind of economics?

European states—including Germany, France, and the United Kingdom—all have highly developed political and institutional relationships with the People's Republic of China (PRC). Over the past several decades, all 28 members of the current European Union established diplomatic relations with Beijing. China also began to pay increased attention to EU counterpart institutions. But the scope and character of these relationships has changed significantly in recent years.

The two-way traffic flow in government, business, and private institutional channels between China and the EU is now very extensive. Chinese officials and business delegations visit Brussels and other European capitals in large numbers, and there are parallel visits of counterpart European groups to China. According to a 2015 report, there are no less than 60 annual China-EU sectoral dialogues.⁸ After some years of hesitation, Chinese leaders now attach growing importance to EU institutions, including the European Commission and the European Parliament. Virtually every Chinese state or high-level visit includes important Chinese CEOs and business leaders. In 2014, President Xi Jinping paid the first-ever visit by a top Chinese leader to EU institutions in Brussels. Both China and the EU increasingly use the term “partnership” to define their relationship: In 2015, they celebrated four decades of diplomatic relations by announcing an “EU-China Comprehensive Strategic Partnership.”⁹

⁸ “From Strength to Strength: E.U.-China Trade Relations,” *Eurobiz*, May 2015, <http://www.eurobiz.com.cn/from-strength-to-strength-40-years-of-eu-china-trade-relations/>.

⁹ “The E.U.-China Comprehensive Strategic Partnership,” June 22, 2016, www.eeas.europa.eu/factsheets/docs/eu-china_factsheet_en.pdf.

The European External Action Service (the EU's equivalent of a foreign ministry) has also enhanced its presence in Beijing, emerging as an information hub on numerous policy matters.¹⁰ However, as observed by European scholar Frauke Austermann, “portraying ‘one European voice’ abroad (and especially in China) depends heavily on the local context to which a new EU institution must adapt and can hardly change.” The EU's foreign policy is primarily the sum of diplomatic goals and actions of individual member states, but there is ample differentiation and (at times) overt competition among key member states.

These trends are evident in the scale and significance of EU-China economic relations. The European Union is now China's second largest commercial partner after the United States. Two-way trade reached 467 billion euros in 2014, with a trade deficit of 137 billion euros in favor of China. However, the situation varies greatly from country to country. Nearly all EU member-states run a trade imbalance with China, now including Germany, which had previously maintained a trade surplus. Poland, for example, has a tenfold trade deficit with China. In the nearly 40 years of China's “opening to the outside world,” European countries with world-class multinationals have developed a long-term presence and deep relations with Chinese counterparts. But with Chinese foreign direct investment (FDI) in Europe moving to center stage in the China-EU policy agenda, reciprocal economic opportunity becomes an even more important policy concern.

The reasons for increased Chinese interest in FDI are readily apparent. Unlike trade and tourism, investment involves long-term commitment, and Chinese companies are looking for a stable, legally secure environment, including for private investors in sectors such as real estate. Acquisition of advanced industrial technologies from European firms has emerged as an increasingly important priority for China. As a result, there has been a major Chinese investment surge over the past half-decade. According to a report published by MERICS (Germany's leading think tank on Chinese affairs), and the Rhodium Group, China's cumulative investments in Europe

¹⁰ Frauke Austermann, *Representing the EU in China: European Bilateral Diplomacy in a Competitive Diplomatic Environment*, European External Action Service (Palgrave, 2015), http://link.springer.com/chapter/10.1057%2F9781137383037_16

reached \$23 billion in 2015.¹¹ (This represents approximately 4 percent of total FDI in Europe, but 29 percent of the total Chinese FDI worldwide.)

The United States remains by far the main holder of inward FDI in the EU (39 percent, or \$1.68 trillion). But many see China's deepening involvement as the leading edge of future trends, without agreed upon rules to govern these possibilities. The current wave of Chinese investment in Europe first accelerated in the aftermath of the 2008 global economic crisis, which ravaged numerous countries, including Greece, Portugal, Ireland, Spain, and Cyprus; and buffeted the United Kingdom, Germany, and France, the EU's three largest economies. Many European firms and state-owned entities were looking for cash and new sources of investment, and China responded vigorously. The rapid increases in Chinese investment and potential manipulations of various holdings through a web of intersecting relationships among Chinese stakeholders have raised increased concern in European political and corporate circles. Much of this concern has focused on collusive but insufficiently understood relationships between the Chinese state and powerful industrial entities.¹²

In some cases, it is doubtful whether some cash-strapped European countries have viable alternatives to Chinese investment. Deals have been consummated all across Europe, with Chinese SOEs putting cash on the table for projects that many European policymakers considered infeasible only a few years ago. Serbian Prime Minister Aleksandar Vučić, for example, has publicly expressed gratitude to China for helping to finance and build a high-speed railway between Belgrade and the Hungarian capital of Budapest.¹³

This trend has become even more pronounced since China launched its "One Belt, One Road" (OBOR) initiative, first proposed by President Xi Jinping on a 2013 visit to Kazakhstan. China showed a strong interest in building or rebuilding portions of the European infrastructure, with particular attention to energy plants, utilities, airports, ports, rail lines, and

¹¹ "Chinese investment into Europe hits record high in 2014," Baker & McKenzie, <http://www.bakermckenzie.com/news/Chinese-investment-into-Europe-hits-record-high-in-2014-02-11-2015/>. Chinese investments in Europe include those in greenfield and mergers and acquisitions (M&A) transactions.

¹² Paul Mozur and Jack Ewing, "Rush of Chinese Investment in Europe's High-Tech Companies Is Raising Eyebrows," *New York Times*, September 17, 2016, <http://www.nytimes.com/2016/09/17/business/dealbook/china-germany-takeover-merger-technology.html>.

¹³ Remarks at Brookings symposium, September 16, 2015. (Serbia is not a member of the EU.)

highways. If OBOR proves successful, it would transform Eurasia's economic and political landscape. But OBOR is also making a virtue out of necessity, as China seeks to manage the transition from a lower wage, export-oriented economy to middle income status. Though Chinese officials cloak these possibilities in the language of "win-win" cooperation, they undoubtedly grasp the geopolitical consequences, as well. China has therefore taken ownership (both literally and figuratively) of this strategy, which will be a central component of Xi Jinping's political legacy.

Not surprisingly, there is widespread European interest in the potential for much enhanced economic collaboration with China. Hungary and the Czech Republic have offered to welcome OBOR projects. European harbors in Rotterdam and Antwerp have also established OBOR taskforces. A press release from the Port Authority in Antwerp has highlighted the city's role as a major trading hub, declaring that the city can play a potentially very important role in the land-based Silk Road Economic Belt and the ocean-going maritime Silk Road.¹⁴ In 2015, China also signaled its willingness to take part in the European Commission's investment plan (the "Juncker plan," named after the current president of the European Commission), raising expectations of a potential incorporation of OBOR's European destinations within a broader Chinese investment strategy.

OBOR is therefore intended simultaneously to expand China's presence and influence among the needier, less developed areas of inner Asia while also taking advantage of the current weakness of various European economies, especially in Central and Eastern Europe. It will also provide opportunities for Chinese companies facing domestic slowdowns to extend their international footprint. Hence there are questions being asked in Berlin and elsewhere: What is China seeking in Europe? Is there a larger design with regard to the strategic dimensions of some investments?¹⁵ Or do assumptions of strategic intent obscure China's own liabilities, including burgeoning debt burdens (especially among China's SOEs), acute environmental degradation, pervasive corruption, income inequality, and industrial overcapacity?

¹⁴ "Port of Antwerp sets up 'One Belt One Road' taskforce," Port of Antwerp, September 23, 2015, <http://www.portofantwerp.com/en/news/port-antwerp-sets-%E2%80%9Cone-belt-one-road%E2%80%9D-taskforce>.

¹⁵ Interview with Philippe Le Corre, "China's Offensive in Europe: is there a master plan in Beijing?" *Wall Street Journal*, June 22, 2016, <http://blogs.wsj.com/chinarealtime/2016/06/22/chinas-offensive-in-europe-is-there-a-master-plan-in-beijing/>.

Some European countries have begun to engage in extensive debate about the implications of increased Chinese investment, and in several instances halted or deferred some privatization programs. But in almost all instances the ultimate results have reaffirmed prior decisions. For example, the Syriza-led left wing Greek government elected in January 2015 decided to freeze the Piraeus Harbor's privatization in order to reopen the bidding process to other competitors. It took a year before Athens (in the absence of credible competitors) granted a 67 percent share of the harbor to COSCO, a powerful Chinese SOE focused on maritime transit.

The new Lisbon government, elected in September 2015, has also expressed concerns about China's stakes in Portugal's national grid. In 2011, the previous Conservative government had sold 21.3 percent of Energias de Portugal to China's Three Gorges Corporation (TGC) for 2.7 billion euros. No competitor had offered to join the race at the time, opening the way to TGC, followed by more Chinese investors in sectors such as grid distribution, insurance, and real estate.

Debate is extending to German business elites, with growing attention to Chinese inroads into high technology sectors. The acquisition of Kuka, a German robotics firm, by China's Midea, a large appliance manufacturer, provides a relevant example. Approval of the transaction was slowed in the spring of 2016 following opposition by a number of German politicians, including Günther Oettinger, the EU's digital affairs commissioner, who called for non-Chinese bidders to step forward. In the end, no challenger came forward and Midea acquired 94 percent of Kuka. A key supplier of technology brands, Germany is already the main European destination for Chinese FDI, with a total amount of \$10.8 billion in the first half of 2016. Concerns include the risks to sensitive German industrial and corporate data if acquired by Chinese conglomerates. German officials have recently adopted a tougher line. Berlin's Ambassador to China Michael Clauss said that it was "more or less impossible" for a German firm to invest in China through acquisition, while Germany has yet to refuse a single Chinese investment such as Kuka.¹⁶

¹⁶ Wendy Wu and Laura Zhou, "German firms are having a hard time in China: ambassador points to rising protectionism ahead of Hangzhou G20 summit" *South China Morning Post*, August 29, 2016, <http://www.scmp.com/news/china/diplomacy-defence/article/2010599/german-firms-are-having-hard-time-china-ambassador>.

Although neither the EU nor any of the individual member states have developed the equivalent of the Committee on Foreign Investment in the United States (CFIUS), there are moves in that direction, and it seems likely that these efforts will draw on U.S. practice. Over the past decade or more, CFIUS has identified potential national security risks of FDI applications in the United States, including the proposed 2005 acquisition of Unocal by CNOOC, one of China's major energy SOEs.¹⁷ Although another SOE, ChemChina, was given a green light by CFIUS in August 2016 to acquire the Switzerland-based agribusiness firm Syngenta, there have been at least two rejections of pending cases. Philips' attempt to sell its lighting business to a Chinese consortium in early 2016 was blocked, and Tsinghua Uni-group withdrew from a \$3.8 billion investment in Western Digital after the deal was flagged during an investigation by CFIUS. In Europe, the absence of a CFIUS-like mechanism has prevented full scrutiny of high-profile cases. By and large, countries have handled critical projects on an individual (and fairly confidential) basis. These highlight shortcomings in governmental oversight of Chinese business practices that need to be rectified.

In post-Brexit U.K., Prime Minister Theresa May stunned China by deferring approval of the 18-billion-pound Hinkley Point C nuclear deal, to be financed by China General Nuclear Power Company and China National Nuclear Corporation, with the backing of Chinese sovereign wealth funds. The U.K. already has a major Chinese telecommunication company (Huawei) supplying key parts of its telecommunications infrastructure to its various mobile operators.¹⁸ But no other major country has ever invited Chinese involvement in a key nuclear energy project.¹⁹ Despite such unease, the May government in September 2016 reaffirmed the original agreement negotiated by her predecessor, Prime Minister David Cameron.

In October 2015, President Xi Jinping received an ostentatious welcome on his state visit to the United Kingdom, declaring that the U.K. "could play a more positive and constructive role in promoting in-depth development

¹⁷ Ziad Haider, "China Inc. and the CFIUS National Security Review," *The Diplomat*, December 3, 2013 <http://thediplomat.com/2013/12/china-inc-and-the-cfius-national-security-review/>.

¹⁸ Unlike the United States, where Huawei has almost no presence in the infrastructure field.

¹⁹ Carrie Gracie, "Hinkley Point: Theresa May's China calculus," *BBC*, July 31, 2016, <http://www.bbc.com/news/uk-36935342>; "Not so gung-ho," *The Economist*, August 6, 2016, <http://www.economist.com/news/britain/21703401-relations-may-cool-flow-yuan-britain-unlikely-dry-up-not-so-gung-ho>.

of China-EU relations.”²⁰ But the June 2016 decision by the majority of British voters to withdraw from the EU resulted in the resignation of Prime Minister David Cameron and Finance Minister George Osborne, the two leading advocates in the U.K. calling for much closer relations with China. Notwithstanding the reaffirmation of the Hinkley Point nuclear project, it remains to be seen whether the Sino-British “golden era” advocated by the former prime minister and the former finance minister will continue, or even whether it was more a political slogan than a genuine national strategy. At the same time, Brexit has undoubtedly compromised London’s ability to influence the EU’s decisions on China policy in the areas of trade, investment, and market economy status.

The expansion of China-EU economic ties also increased calls for a free trade agreement. When these efforts appeared to stall in the fall of 2013, China and the EU opted for negotiations on an investment treaty. Currently, 26 European countries have signed individual investment accords with China. Pursuit of a multilateral agreement reflects the rising difficulties of European firms in gaining access to the Chinese market. The EU has indicated it will not consider entering Free Trade Agreement talks with China until completion of an investment treaty. (The United States confronts comparable problems in moving toward a Bilateral Investment Treaty with China. Though some of the differences have been narrowed, it appears unlikely that an agreed-upon text will be finalized before the Obama administration leaves office.) A June 2016 EU-China joint communication drafted by the European side explicitly includes a Comprehensive Agreement on Investment (CAI) as an objective. EU officials assume it will be a slow process, but China has at least acknowledged the need for a long-term arrangement.

Summit diplomacy

The EU and the United States have both made major political commitments to annual diplomacy with China. The latest EU-China summit, held in Beijing in July 2016, was the 18th such meeting. The U.S. equivalent (known in the Obama administration as the Strategic and Economic Dialogue) does not have as extensive a policy lineage, but it serves a compa-

²⁰ “Xi Jinping and Prime Minister David Cameron of UK Hold Meeting Again,” Chinese Ministry of Foreign Affairs, October 27, 2015 <http://www.mfa.gov.cn/ce/cesg/eng/jrzg/t1309372.htm>.

rable purpose: a shared readiness to address a wide spectrum of economic and foreign policy issues, with participation by the responsible policy officials on both sides. On the U.S. side, this process now includes approximately two dozen cabinet-level officials and agency heads. The EU-China summits include the presidents of the European Council and the European Commission and numerous other senior officials. Both sets of meetings are replete with long recitations of “policy outcomes” that presumably attest to the substantive import of the discussions. Even acknowledging the forcing function such meetings provide relevant policy bureaucracies, major policy breakthroughs are exceedingly rare. But the political investment in these mechanisms very likely ensures that they will persist in future years.

The EU-China summit has also tried to address new areas of concern, including enhanced security cooperation. But the most recent EU-China meeting took place in Beijing following the International Arbitration Tribunal's decision in The Hague that favored the case brought by the Philippines contesting Chinese maritime claims in the South China Sea. The meeting was tenser than usual, as China urged European leaders to split from the court decision, and possibly from Washington and its East Asian allies.

The 2016 China-Europe summit, held on July 12 and 13, also followed the June 22 release of the new EU strategy towards China, on the eve of the British referendum on EU membership.²¹ One commentator argued that “the noticeable differences in the topics raised by the two sides during the summit vindicates the assumption of deepening discrepancies, including asymmetry in relations at the expense of the EU”²² Europe has become increasingly wary of China's pursuit of unconditional access to the EU consumer market. Without explicit trade agreements enabling increased reciprocity between the EU and China, the prospect of unconstrained entry of Chinese exports into European markets becomes a distinct possibility.

To advance its policy objectives, China has sought to manage its relationships with Europe in multiple ways. First, it has increased its presence and influence in Brussels, headquarters of the European institutions. China's

“Major policy breakthroughs are exceedingly rare. But the political investment in these mechanisms very likely ensures that they will persist in future years.”

²¹ “Joint Communication to the European Parliament and the Council.”

²² Justyna Szczudlik, “China-EU Relations: Post-Summit Perspectives,” Center for Security Studies, ETH Zurich, August 11, 2016, <http://isnblog.ethz.ch/international-relations/china-eu-relations-post-summit-perspectives>.

visibility has been enhanced through media coverage, cultural events, educational exchanges, and sports competition. The number of think tank seminars organized or funded by the Chinese Representative Office to the European Union has also increased significantly. Second, it is also sustaining strong links with Germany, France, and the U.K., using a mix of political contacts, business connections, and soft power means. Third, it has developed a reliable group of friends through the “16+1” mechanism that focuses on the EU’s newer members, many of whom are struggling economically, as well as a handful of non-EU countries in the Balkans, including Serbia, Albania, Macedonia, and Montenegro. It has also sought to use its strong financial commitment to Greece to distance Athens from growing criticisms within the EU of Chinese actions in the South China Sea.²³

China’s OBOR initiative thus has direct implications for Europe, which has been included in OBOR from the outset. Fourteen European countries led by the U.K., France, Germany, Italy, and later Poland also joined the Beijing-led Asian Infrastructure Investment Bank (AIIB) in 2015 as founding members, with U.S. officials voicing clear discomfort over these moves. The new institution has joined other multilateral banks such as the Asian Development Bank, the World Bank and the European Bank for Reconstruction and Development (EBRD) to finance new infrastructure projects across Asia. European countries have been on the receiving end of Chinese courtship over the past three years, as Xi Jinping has aimed to expand the concept. OBOR-related conferences and seminars have multiplied in Europe and in other potential destinations.²⁴ In the first half of 2016, Xi visited the Czech Republic, Poland, and Serbia, three of the seven countries that signed memorandums of understanding at the previous 16+1 meeting.²⁵ There have been attempts to initiate similar mechanisms with Nordic countries and with Southern European countries, to be linked to OBOR, thus far without success.

But China clearly envisions Europe as the location where it can accelerate its involvement and international visibility. Sino-European relations are

²³ Along Hungary and Croatia, Greece was apparently one of three EU members who tried to influence the EU to not issue a joint declaration after the arbitration tribunal’s ruling. Prime Minister Alexis Tsipras had a very successful visit to Beijing in June, weeks after his government agreed to grant China’s COSCO management of Piraeus harbour.

²⁴ Kazakhstan, Georgia, Senegal, Hong Kong, to name just a few venues.

²⁵ The summit took place in Suzhou in November 2015.

less fraught than U.S.-China relations and do not entail a comparable level of strategic competition. In addition, the EU consumer market is attractive to China as it faces a slowing economy and increasing overcapacity. Beijing sees the EU as a weakened political player with numerous ongoing crises, including major problems in the economy, governance, terrorism, and migration; growing cash needs; and frequent internal divisions among its members.

In its recent joint EU-China Joint Communication, the EU stated that it

“must project a strong, clear and unified voice in its approach to China... When Member States conduct their bilateral relations with China they should cooperate with the Commission, the EEAS and other Member States to help ensure that aspects relevant to the EU are in line with EU law, rules and policies, and that the overall outcome is beneficial for the EU as a whole.”²⁶

These unobjectionable sentiments obscure major policy dilemmas for the EU. The problematic state of the European economy has led some new members to look for alternative economic partners, and China holds an undoubted allure for needier states. China's increased efforts to cultivate Europe began in 2008. This included a focus on France (which celebrated the 50th anniversary of diplomatic relations with the PRC in 2014), Germany (China's top economic partner), and other Western European countries, such as Italy, Greece, and Portugal. The courting of Eastern Europe started more recently through investments in Hungary, Poland, and Romania. Many East and Central European states are turning to China for investment under the 16+1 mechanism, a forum originally established to encourage dialogue between the region and China.²⁷ Many envision OBOR as a major economic opportunity for Central and Eastern Europe, hoping to see China establish special economic zones. More specifically, some countries see potential cooperation with China's western regions as an opportunity to increase business connections with regions outside the European zone.

²⁶ “Joint Communication to the European Parliament and the Council.”

²⁷ Philippe Le Corre, “What China's checkbook diplomacy means for Europe,” *Politico*, May 12, 2016, <http://www.politico.eu/article/what-chinas-checkbook-diplomacy-means-for-europe/>.

At the same time, larger EU members such as Germany, France, Italy, and Poland appear intent on engaging jointly with China on important governance issues that align these countries more closely with the U.S. policy agenda. Germany's Chancellor Angela Merkel has been at the core of this new policy. Backed by Berlin and others, the EU has released several statements in support of the international court's decision on the South China Sea. The EU's high representative for foreign affairs and security policy, Federica Mogherini, has also sought to engage China on counterterrorism, cybersecurity, and anti-piracy issues. At the most recent EU-China summit, Donald Tusk, the European Council president, specifically referred to a "rule-based international order, which is in the common interest of China and the EU."²⁸

France has sought to take these steps even further. As one of the few European countries which maintains any naval presence at all in the Pacific, it urged the EU at the most recent International Institute for Strategic Studies (IISS) Shangri-La Dialogue in Singapore to coordinate naval patrols to ensure a "regular and visible" presence in the South China Sea.²⁹ In the words of Defense Minister Jean-Yves Le Drian, "if we want to contain the risk of conflict, we must defend this right, and defend it ourselves." France views the protection of freedom of the seas as critical from an economic standpoint and has voiced concern that a loss of such rights in the South China Sea might lead to similar problems in the Arctic Ocean or the Mediterranean Sea.³⁰

However, the likelihood that the defense minister's call will result in a broader EU agreement seems low. Any accord would require much fuller military coordination within the EU, where defense spending is already inadequate among most member-states, nearly all of whom are focused on

²⁸ "Remarks by President Donald Tusk at the EU-China summit in Beijing," European Council, July 12, 2016, <http://www.consilium.europa.eu/en/press/press-releases/2016/07/12-tusk-opening-remarks-eu-china/>.

²⁹ Philippe Le Corre and Michael O'Hanlon, "France's pivot to Asia: it's more than just submarines," *National Interest*, May 11, 2016, <http://nationalinterest.org/feature/frances-pivot-asia-its-more-just-submarines-16117>.

³⁰ David Roman, "France to push for coordinated EU patrols in South China Sea," *Bloomberg*, June 5, 2016, <http://www.bloomberg.com/news/articles/2016-06-05/france-to-push-for-coordinated-eu-patrols-in-south-china-sea>.

security concerns much closer to home. Although the U.K. remains committed to close defense cooperation within NATO and with major European powers such as France, the period leading to Brexit is not propitious for an enhanced EU security commitment in Asia and the Pacific. At the same time, needier EU member states do not have substantial latitude in deflecting Chinese entreaties. Some countries simply must welcome Chinese investors, which puts them in a weaker position in defending core values of international order. China is therefore able to rely upon Hungary, Croatia, Serbia, and other Central and East European partners to dilute the content of EU policy statements critical of Chinese external behavior.

Although it frequently states the opposite, the Chinese leadership clearly sees advantages in a divided Europe, because it means a weaker West. This applies to trans-Atlantic economic cooperation as well international security. For example, during the Transatlantic Trade and Investment Partnership (TTIP) discussions, Beijing sent emissaries to Europe to try to influence the decision process, viewing such a partnership as an anti-China agreement.³¹ TTIP talks remain at a standstill.

China's predominant economic moves (at least on paper) seek to advance and deepen its involvement across all of inland Asia. The OBOR project is supposedly targeting 60 countries, including many in the Middle East, Africa, Central Asia, and Southeast Asia, with the purpose of extending China's soft power and commercial outreach. Xi Jinping seems to believe that China has entered a period of strategic opportunity, with OBOR providing the connective thread in national strategy. However, Chinese policy banks are already saddled with substantial and very risky investments in financing development projects across Latin America, Africa, and Asia.³² Prudence dictates a much more exacting approval process for new agreements, but the political momentum behind these activities points in the opposite direction.

“Although it frequently states the opposite, the Chinese leadership clearly sees advantages in a divided Europe, because it means a weaker West.”

³¹ Miguel Otero-Iglesias, “The geopolitics of TTIP seen from Beijing,” Real Instituto Elcano, November 12, 2013, http://www.realinstitutoelcano.org/wps/portal/web/rielcano_en/contenido?WCM_GLOBAL_CONTEXT=/elcano/elcano_in/zonas_in/commentary-otero-iglesias-geopolitics-ttip-seen-from-beijing

³² For a detailed and highly sobering assessment, see “China rethinks developing world largesse as deals sour,” *Financial Times*, October 13, 2016, <https://www.ft.com/content/5bf4d6d8-9073-11e6-a72e-b428cb934b78>.

OBOR nonetheless poses a prospective challenge to the existing international order. It treats Asia and Europe as a unified geo-economic space, with China as the driving force underlying this strategy. Central Asia, in particular, has been courted by China for well over a decade, first through the Shanghai Cooperation Organization and now through OBOR. But it has an even longer policy lineage, reflecting Jiang Zemin's earlier concern about the major economic imbalances between inland regions and coastal China. The liabilities and uncertainties of this initiative in Central Asia and the South Caucasus should not be minimized, and success is far from assured. But Beijing (impelled by Xi Jinping's personal endorsement of OBOR) sees obvious opportunities in a broad expansion of its economic role in areas where neither the United States or EU have developed (or seem intent upon) a very strong presence.

Implications for U.S. strategy and for trans-Atlantic relations

As Europe and the United States both contemplate the implications of a much more powerful China, they have yet to realize close strategic coordination. This is less a matter of disinterest on either side or of sharply divergent policy goals, and more a question of the focus of EU and U.S. policymaking. Europe and America are both highly consequential economic actors, and they have a shared interest in upholding a rules-based international order, though they might disagree on some of the particulars. The question is whether there is sufficient political will on both sides of the Atlantic to elevate the importance of China on the EU-U.S. policy agenda.

The United States views China through America's position as the long-dominant political and military power in Asia and the Pacific. The Obama administration's declared intention under its rebalancing strategy was to reaffirm the U.S. regional role but also to realign the focus of its global strategy. The rebalance presumed that Asia and the Pacific in coming decades would increasingly determine U.S. strategic priorities. But the United States did not address the issue of how (or whether) the EU and the United States could reconcile the differing pushes and pulls underlying their respective strategies.

The absence of sustained efforts to reconcile and (ideally) to integrate U.S. and EU strategies reflect the differing interests and policy preoccupations of the United States and Europe. The Obama administration envisioned the rebalance as a three legged stool, involving politico-diplomatic, economic, and military-strategic dimensions. Though the United States insisted that the rebalance was not China-driven, issues pertaining to China hovered over the policy from its very outset. But pursuit of accommodation with China presumed that Beijing's longer term goals would not disrupt the regional order. The United States also assumed that deeper engagement with China was preferable as a means to protect American interests than open-ended strategic rivalry or overt confrontation. At the same time, the United States recognized that heightened contention would severely complicate possibilities for meaningful cooperation with China on crucial regional and global issues. But an accommodation strategy still presumed a vigorous U.S. reaffirmation of its power (especially military power), both to protect American interests and to uphold its long-standing commitments to its allies and partners across the region.³³

Though Europe also cares deeply about its long-term relations with China, there is no outright equivalence between U.S. and EU strategy. Europe's dominant concerns about China are twofold: the terms of economic relations, and the extent to which China is prepared to adhere to a conception of a rules-based order acceptable to the EU. But these are not dissimilar from the preoccupations of the United States. Indeed, President Obama's vigorous commitment to the Trans-Pacific Partnership (an accord now undermined by the explicit opposition to the TPP by both presidential candidates) was expressly premised on the requirements for a 21st century multilateral trade accord, even though China was not a party to these negotiations.

According to President Obama, the TPP is "more than just a trade pact; it also has important strategic and geopolitical benefits...[and] in our shared security and in universal human rights."³⁴ The president's remarks under-

³³ For a careful exploration of these arguments, consult Jeffrey A. Bader, "A Framework for U.S. Policy toward China," Brookings Institution, Asia Working Group Paper 3, March 21, 2016, <https://www.brookings.edu/research/a-framework-for-u-s-policy-toward-china/>.

³⁴ "Remarks by President Obama at ASEAN Business and Investment Summit," Kuala Lumpur, November 20, 2015, <https://www.whitehouse.gov/the-press-office/2015/11/20/remarks-president-obama-asean-business-and-investment-summit>.

score his belief that the rules governing trade and investment will be the driving force in Asia-Pacific international relations in the 21st century: “Without this agreement, competitors that don’t share our values, will rewrite the rules for the global economy. They’ll keep selling into our markets and try to lure our companies over there; meanwhile they’re going to keep their markets closed to us.”³⁵

These sentiments seem comparable to concerns voiced within the EU. China has taken advantage of economic competition within Europe, as well as between the United States and Europe. The challenge for Europe and the United States is to enhance cooperation and policy coordination, thereby enabling development of more effective and sustainable rules of the road for future economic relations with China. Such a process would thereby provide increased incentives for China to agree to mutually acceptable outcomes with both Europe and the United States.

In broad strategic terms, therefore, there is no major divide between the United States and Europe on China. There are undoubted differences of emphasis within major policy bureaucracies, in particular between foreign ministries and defense ministries, but this is not an uncommon phenomenon. The increased convergence between European and American policymakers on the rules of the road for economic engagement provides a clear basis for addressing parallel concerns. Arguably, the EU side is more concerned about the social and economic impact of Chinese products on the European market (including consumer and worker protection rules), while the U.S. side is worried about the growing security challenges posed by China. But these should not be an impediment to a closer consultative process.

The two sides have more shared concerns than they sometimes articulate. For example, European Council President Donald Tusk referred to globalization when visiting Beijing last July:

“Globalization brings so many benefits to our nations. Unfortunately, more and more people feel that it is happening without rules. And if we let these feelings grow, if many start believing that glo-

³⁵ Barack Obama, “Weekly Address: Writing the Rules for a Global Economy,” October 10, 2015, <https://www.whitehouse.gov/the-press-office/2015/10/10/weekly-address-writing-rules-global-economy>.

balization and international trade are happening without or against common rules, then the first victims will be the Chinese and European economies, not to mention people. That is why we are so openly raising these issues, because we believe a frank discussion is in our mutual interest.”

The United States and EU both view China as one of the prime beneficiaries of globalization. But many in the West are starting to question whether the advanced economies are benefitting in commensurate fashion from these transactions. Failure to push through the TTIP agenda is partially attributable to U.S.-EU leaders not explaining the benefits of such a trade deal. By contrast, China increasingly extols its desire to deepen the globalization process, deeming OBOR as part of its provision of public goods for the international community.³⁶ Xi Jinping also characterizes OBOR as a means to stimulate economic growth across Asia. In addition, Chinese leaders argue that enhanced economic links will ameliorate suspicions in the West about the growth of Chinese power. But neither the EU nor the United States has major economic assets at risk in inner Asia.

To achieve outcomes that will address EU and U.S. concerns, both sides must pursue shared, coordinated objectives. Without such efforts, political space will be created that China will be only too eager to exploit. With such efforts, the likelihood of China responding meaningfully to the concerns of the major industrial economies will increase. This issue must therefore be faced directly on both sides of the Atlantic.

Senior officials in the Obama administration assert that the United States pursued a coordinated approach in its dealings with European counterparts. Kurt Campbell, U.S. assistant secretary of state for East Asian and Pacific affairs during Hillary Clinton's tenure as secretary of state, contends that European partners were kept fully informed about the Asia-Pacific rebalance through regular contact and yearly meetings at the assistant secretary level. As Campbell has argued, “coordinating U.S. and European approaches in promoting liberal values is especially useful because it elevates what might otherwise appear to be ideological American criticisms to appeals to widely held international values.”³⁷

³⁶ See, for example, Xi Jinping's keynote speech to the G-20 Summit in Hangzhou, September 3, 2016.

³⁷ Kurt Campbell, *The Pivot*, Twelve Books, New York, 2016, pp. 290-291.

Despite Campbell's claims, it is far from certain that major European partners fully endorsed the rebalance strategy. To many in Europe, it appeared to relegate Europe to a lower priority in U.S. foreign policy. In President Obama's second term, relations improved (partly because of growing security crises on Europe's borders), but the Obama presidency was never considered fully collaborative by many in Europe, though this led some observers to overplay the idea of a "split" between the United States and Europe on China.³⁸

2017 therefore presents a clear opportunity to revisit trans-Atlantic cooperation and coordination in relation to China. Major changes in political leadership loom on both sides of the Atlantic. Following the U.S. elections in November, a new administration will take charge in January 2017; in Europe, the Netherlands (in March), France (in May), and Germany (in September) will select leaders for the next five years to steer Europe through one of the most contentious periods since creation of the EU. In the United Kingdom, Prime Minister Theresa May's main responsibility as the newly elected leader of the U.K. will be to negotiate with other European leaders the terms of Britain's exit from the union. In Italy, Prime Minister Matteo Renzi has taken a huge gamble by calling a referendum this fall on his reform plan; and a number of countries remain heavily indebted and fragile financially.

Instead of retreating into their separate policy deliberations, Europeans and Americans have an opportunity to begin a deeper dialogue on longer-term relations. The Asia-Pacific region should figure prominently in this process. The major European powers increasingly speak with one voice on the South China Sea, the North Korean nuclear and missile threat, humanitarian crises, anti-piracy, and cybersecurity. These all pertain to the role of High Representative Federica Mogherini, who heads the European External Action Service (EEAS) and has been engaging with U.S. counterparts on Asia-Pacific issues. These add to regular bilateral exchanges between French, German, and British officials and U.S. counterparts responsible for Asia and the Pacific.

But the largest challenges pertain to economic relations between China and the United States and between China and Europe. Without enhanced trans-Atlantic coordination, the same problems that have bedeviled U.S. and EU relations with China will recur, and could grow more acute. As

³⁸ Anders Corr, "The US-Europe split on China," *Forbes*, March 17, 2016, <http://www.forbes.com/sites/anderscorr/2016/03/17/the-us-europe-split-on-china/#2726e0a3583e>.

the next U.S. administration weighs its policy priorities, the trans-Atlantic dimension of strategies toward China warrants more careful attention, including at senior leadership levels.

Brexit is another looming issue. As London heads towards negotiations over its withdrawal from the EU, the U.K. should not try to act as “China’s best partner in Europe (or in the West).” The previous government’s go-it-alone policy towards China failed to deliver on its promised results, and London’s influence in Beijing has diminished appreciably. (Some observers, however, believe that Brexit will provide the U.K. with a freer hand in its relations with China.) Though Berlin sometimes seems to claim a preponderant influence over EU China strategy, this seems doubtful. One German expert argues that the Sino-German special relationship has run into “serious difficulties, which neither economic opportunism nor political statecraft can resolve easily. The assertive course of China’s leadership in economic issues, domestic politics and foreign affairs shows that Berlin can’t go it alone when it comes to dealing with Beijing.”³⁹

France and Germany are thus positioned to assume the lead in EU relations with China. As partners, they can also serve in a very prominent role in dealings with the next U.S. administration. Both nations have long experience in working in China and with China, and they both have credibility in China that can complement the EU’s foreign policy voice. In light of the U.K.’s new position, another AIIB-like fiasco needs to be avoided within the EU and across the Atlantic through regular consultations. The quintet, which currently brings together senior officials of the United States and four European nations and the EEAS officials responsible for Asian affairs, should include both security and economic dimensions.⁴⁰

The road ahead

As the United States and leading members of the EU map their foreign policy strategies in coming years, there is a clear need to elevate policy coordination toward China in the hierarchy of political and economic goals.

³⁹ Mikko Huotari, “Beijing-Berlin connection revisited,” MERICS, June 20, 2016, <https://blog.merics.org/en/blog-post/2016/06/15/beijing-berlin-connection-revisited/>.

⁴⁰ France, Germany, Italy, and the U.K.

These can build upon existing mechanisms that both have employed in relations with China, but with closer attention to how their respective agendas can reinforce one another. A short list of possible priorities follows, but it is more illustrative than exhaustive.

Geoeconomics

- **Investment**

A coordinated approach to cross-border investment through an enhanced U.S.-EU dialogue mechanism is very much needed. Both the United States and the EU are currently discussing investment treaties with China that more fully address the expectations and needs of American and European multinationals and of Chinese companies. The latest reports of the EU Chamber of Commerce in China and the American Chamber of Commerce in China both emphasize that the rapid emergence of China as a major global investor renders these issues far more important.⁴¹ In addition to EU-level coordination, this process should include creation of CFIUS-like committees within Europe so that governments on both sides of the Atlantic can exchange information and develop parallel strategies. A common position on China's market economy status is also long overdue.

- **Asian Infrastructure Investment Bank**

Policy coordination should also encompass a fuller exploration of the AIIB, which has demonstrated initial promise as a multilateral lending institution. The United States (though still not a member of the bank) and the EU should not repeat the controversies surrounding founding membership in the bank, which were poorly handled between the United States and its EU partners. It is also appropriate for the U.S. government to consider joining the AIIB as a member, or at least to engage in a formal partnership with the new bank.

⁴¹ See David Dollar, "China as a Global Investor," Brookings Institution Asia Working Group Paper 4, May 18, 2016, <https://www.brookings.edu/research/china-as-a-global-investor/>.

- **One Belt, One Road**

There is an overdue need for a serious trans-Atlantic discussion on OBOR. At the same time, European states need to ensure a coherent approach toward OBOR and its relationship to existing policy mechanisms. The outcome of deliberations within the EU will have major implications for China's power and influence across Europe. To date, the United States has not been especially attentive to the longer-term implications of OBOR. Heightened U.S. awareness should also help advance the EU goal of joining the annual East Asia Summit as an observer.

- **Cybersecurity**

Cybersecurity has emerged as a central security concern in the early 21st century, with China a major factor. Cyberespionage operations for commercial advantage originating in China triggered intense reactions on both sides of the Atlantic, both in the private sector and at a governmental level. U.S. warnings to China about the possible imposition of tough sanctions on Chinese government entities posed a serious risk to Chinese interests and the country's international reputation, and China began to take these issues far more seriously, resulting in a very sharp decline in reports of cybercrime involving Chinese entities. The evident success in eliciting increased Chinese cooperation (both in bilateral dealings and in curbing the actions of bad actors within China) highlights the need to sustain these processes. These should be an issue of vital importance to both the United States and EU. Coordinated policy approaches across the Atlantic will impart seriousness of purpose to the Chinese, and provide China with clear incentives to build on this much improved record.

Geopolitics

- **Multilateral affairs**

The trans-Atlantic partners should ensure that the full spectrum of Asia-Pacific issues are addressed at all levels in the G-7, in United Nations meetings, and in other settings. Given the comprehensive

role of the United States in regional security, the United States necessarily has a larger voice in that domain, but this should not be to the exclusion of Europe. If anything, positions clearly articulated by the EU will lend far greater clarity and credibility on these issues.

- **Rules-based international order**

Common values remain a defining element the trans-Atlantic community. Both U.S. and EU leaders should stress that these are non-negotiable principles. These should include freedom of navigation and overflight rights, and respect for the U.N. Convention on the Law of the Sea (UNCLOS) and related agreements. China claims that it adheres fully and unconditionally to these principles, but it objects to U.S. interpretation of these accords. Much more needs to be done to bridge this policy divide; to minimize any risks to maritime security and international commerce; and to avoid any possible incidents at sea or between aircraft. In this context, the unwillingness of the U.S. Congress to ratify UNCLOS continues to limit the credibility of U.S. policy.

- **Climate change**

Capitalizing on the success of the 2015 Paris conference, the United States and Europe should build on China's commitment to cap emissions by 2020 to foster a trilateral discussion, based on the U.S.-China accord of late 2014. The ratification of the Paris agreement by the United States and China in Hangzhou during the G-20 represents a very important milestone in global cooperation where both countries have demonstrated increased commitment. There is every reason to broaden and deepen these commitments with European counterparts.

Civil society

Many nongovernmental organizations in the West have tried to engage with China on the development of civil society and the building of relevant nongovernmental institutions. But legislation passed in 2016 by the National People's Congress obligating foreign organizations to register with the political authorities has sent shockwaves across the NGO community.

Some expect to reduce their China presence or even to cease their activities within China. At the same time, the detention and conviction of lawyers and various civil society groups in China has cast a pall on American and European interactions with Chinese counterparts. NGOs are equally targeted by the new regulations, underscoring the need for serious trans-Atlantic discussions on how to utilize an enhanced U.S.-EU partnership to advance complementary goals in civil society.

Conclusions

Europe's relations with China emerged differently from U.S.-China relations, but this divergent history should not represent a major impediment to future policy coordination. Because of the 2008 euro debt crisis, many American analysts concluded that Europe's China policy was based purely on mercantile interests. But there is a complex mix of overlapping economic and geopolitical interests upon which both sides of the Atlantic can and must build.

The strategic issue facing Europe and the United States is not whether China becomes the world's largest economy, but whether China pursues concepts of global governance that do not undermine existing European and American practices. Incorporating China within a rules-based international order is not a choice; it is a necessity. The United States and the EU must therefore seek to ensure that China's global rise proves a positive rather than a disruptive force; to explore far more fully how to coordinate European and American approaches; and to weigh EU and U.S. policy responses if more optimistic assessments of China's economic and political future are not validated.

The need for much closer policy coordination is clearly evident in light of contradictory and often troubling domestic and external policy developments within China pursued under Xi Jinping. Europe and the United States have ample incentives to narrow areas of potential policy divergence on matters pertaining to China's rise, and act with a much clearer sense of common purpose. The upcoming political transitions on both sides of the Atlantic will provide a unique opportunity for American and European leaders to engage in a much deeper strategic conversation on issues of vital importance to both, and to the future international order as a whole.

“Incorporating China within a rules-based international order is not a choice; it is a necessity.”

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