China signed a free trade agreement (FTA) with Iceland earlier this year. This is China’s first FTA with a western European state. Once in force it will waive most tariffs in trade between the two countries. However, the tiny size of Iceland’s market and the fact that the agreement does not provide low-tariff entry for China’s products onto other European markets raises questions over China’s motives. In particular, it is suggested that China is using this FTA to promote its strategic goals, such as obtaining better access to shipping routes through the Arctic or to natural resources extracted in the region.

Icelandic trade

Iceland’s international trade is largely based on the export of marine products (42.4% of all exports). Its main imports are industrial supplies. In 2012, other members of the European Economic Area (EEA), including the EU, collectively formed the largest export market for Icelandic products.

In 2012, Icelandic exports to China amounted to ISK 7.65 billion (€47.6 million), while Icelandic imports from China reached ISK 42.6 billion (€265 million). On these figures, China is Iceland’s 19th largest export destination, and the fourth largest importer to Iceland. It is expected that the FTA will facilitate the export of seafood from Iceland, and could give China a foothold in the resource-rich Arctic region.

China-Iceland Free Trade Agreement

The Agreement between Iceland and China was signed on 15 April 2013. It is in essence similar to other FTAs concluded by Iceland. China is increasingly using FTAs to further its divergent trade policy aims in securing resources and markets. China does not follow a model FTA but instead tailors each FTA to the particular situation of the counterparty.

Under the China-Iceland FTA, tariffs on most goods will be removed. Iceland will exclude some goods from tariff-free trade, for example dairy and meat products, while China will exclude certain products made of paper. The FTA also includes rules on trade in goods and services, rules of origin, trade facilitation, intellectual property rights, competition and investment.

The FTA includes a termination clause. This clause would become significant if Iceland should decide to join the EU in future. Whilst Iceland has been negotiating EU accession, negotiations were halted, pending a referendum, following the April 2013 general election in Iceland. Iceland’s Foreign Ministry announced on 23 August 2013 that it was considering dissolving the committee responsible for negotiating its accession to the EU.

It is noteworthy that on 6 July 2013, China also signed a bilateral FTA with Switzerland and is negotiating one with Norway, another Arctic country. The FTA with Iceland, together with that with Switzerland, could help China on its way to negotiating a potential FTA with the EU in the future. The EU is China’s largest economic partner. However, while China has occasionally mentioned a possible FTA with the EU, it is stressed that China would first have to open up its market to foreign companies. Currently many sectors, such as telecoms, are limited to Chinese companies only.

Possible strategic interests

In the past few years, the Chinese Government has become more assertive in its Arctic policy. China is focusing on its capacity to respond to the effects of Arctic climate change on food production and extreme weather in China. It is also endeavouring to secure access to Arctic shipping routes at reasonable cost as well as to strengthen China’s access to Arctic resources and fishing waters.

China, along with five other states, became a permanent observer on the Arctic Council in May 2013, bringing the total number of observer states to 32. The Arctic Council is an inter-governmental advisory body which promotes cooperation in the region, and issues formal, but non-binding declarations.
However, the creation of the Arctic Circle – a separate organisation devoted to Arctic issues – was announced by Iceland’s President on 15 April 2013, the same day as the signature of the FTA. As it will accept all state-and non-state entities interested, the Arctic Circle is seen as a more open and inclusive forum. Chinese organisations will participate in the inaugural session in October 2013.

As an active Arctic Council member, Iceland is of great importance to China, which is attempting to develop its position in the Arctic. It is banking on melting ice facilitating extraction of resources such as gas, oil, and mineral deposits. China’s national Offshore Oil Corporation (CNOOC) recently applied for a licence to explore and produce oil and gas in Arctic waters off Iceland, together with Iceland’s Eykon Energy.

Given the amount of goods which China ships to Europe each year, alternative shipping routes are of great interest. Opening the Northern Sea Route (NSR) could cut about 6400 kilometres and two weeks off the journey between northern Europe and Shanghai. The distance from Shanghai to Rotterdam via the North Sea Route is about two-thirds that of the southern alternative. In addition, many vessels carrying Chinese goods have to pass through waters with regular pirate activity. As a result, ship-insurance premiums are very high.

Chinese interests are also interested in harvesting northern fish stocks.

It is stressed that Iceland could provide China with techniques for harnessing geothermal energy, which, although abundant in China, is not generated there.

Icelanders view Chinese investment with suspicion, fearing hidden geopolitical interests. In 2011 a billionaire Chinese businessman, Huang Nubo, sought to purchase a very large plot of land (some 0.3% of Iceland’s land mass) on the country’s east coast, for the development of a leisure resort. The government rejected his request, as Icelandic law does not allow entities from outside the EEA to purchase land. Huang leased the land instead. The newly elected coalition (April 2013) has demonstrated some willingness to ease the restrictions on foreign land ownership. So far, however, this issue remains unresolved.

### Stakeholders' views

Drilling for oil in the Arctic would present unique environmental challenges and pose real ecological dangers, including preservation of animal and plant species unique to the Arctic, particularly tundra vegetation, caribou, polar bears, seals, whales, and other sea life.

There are also worries regarding the possibility of China exhausting the fish stocks in the high waters of Arctic.

Negotiations on the Iceland-China FTA only started after the collapse of Iceland’s economy in 2008, which raised Iceland’s interest in a potential deal. As the country is still in the recovery phase, landowners and small businesses in Iceland are concerned by the need to attract Chinese foreign investment.

### European Parliament

On 20 January 2011, the European Parliament (EP) adopted a resolution on a sustainable EU policy for the High North. In its resolution, the EP recognised that China’s growing interest in the Arctic region requires a new geopolitical appreciation of the Arctic. The EP further noted that the EU, through its northern Member States and candidate countries (including Iceland) is affected by Arctic policies and has an impact on Arctic policies. The EP also stressed the responsibility of the Arctic states to ensure that the necessary safety technology and expertise are in place on oil rigs and that these states have to be financially prepared to prevent and respond to oil-rig disasters and oil spills.

The EP’s resolution of 14 March 2013 on EU-China relations does not mention the Arctic. It stresses that consideration should be given to the economic, social and environmental impact of increasing Chinese investment in developing countries. The EP also took note of China’s increasing involvement in the exploitation of natural resources in Latin America, as Chinese imports of such resources have increased. The resolution however does not address Chinese investment or extraction interests in developed countries or the Arctic.