ABSTRACT

China is a natural strategic partner for the EU, despite fundamental divergences in some areas, mostly related to state intervention, both in economic and social affairs. Due to growing tensions and geopolitical unpredictability, there is a window of opportunity to develop closer ties between the EU and China. The partnership offers mutually beneficial opportunities, such as comprehensive agreements on investment and on the protection of geographical indications; aviation and maritime cooperation; and dialogues on human rights and legal affairs.

China is navigating a crucial but complex transformation towards more sustainable growth by rebalancing from investment to consumption and from manufacturing to services. Overall, this transition is expected to benefit both China and the world as a whole. Due to economic interdependence, it is also likely to produce certain spill-over effects that will vary by country and by region. Global integration is fundamental for all economies and no one has an interest in a trade war or protectionism.

Maintaining public ownership as the mainstay of the Chinese economy is not sustainable. Reforms are needed to tackle the root causes of overcapacity in various industrial sectors and the role of state owned enterprises. Domestic concerns, such as lifting millions of people out of poverty and reducing ever-growing income inequalities as well as endemic corruption, need to be addressed.

China now plays a crucial role in global governance, the rules-based international order and meeting commitments made in the G20 framework — achieving ‘major country’ status comes with responsibilities. Beijing has demonstrated some movement in shifting away from the pursuit of narrow national aims towards a more active foreign and security policy and increased global financial, economic and peace cooperation. At the same time, China has been increasingly assertive in its Asian neighbourhood and it has called for restraint from all sides to prevent rapidly escalating tensions on the Korean peninsula from turning into a disastrous conflict.
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1 Key issues and developments

- The EU has concerns about trade and investment relations with China, which include the lack of reciprocity and market access as well as the absence of a level playing field in China for foreign investors, while Chinese investments in the EU are free and flows are increasing. No free trade agreement (FTA) can be considered before the conditions are right, including the successful conclusion of the negotiations on a comprehensive EU-China investment agreement, and the Agreement on Protection of Geographical Indications. While the future remains somewhat unclear due to growing global tensions and geopolitical unpredictability, there is a window of opportunity for the EU and China to strengthen their bilateral relations at the summit in June 2017.

- President Xi Jinping, who was elevated to the status of ‘core’ leader in 2016, completes his first five-year term in 2017. Xi has rapidly consolidated his personal power and promoted ideological unity, pursuing the dream of a great ‘rejuvenation of China’. Xi is waging a tough war on corruption and the national security rules may serve to crush any hint of dissent through ‘discipline inspections’. The National Security Law includes sweeping provisions which address economic and industrial policy. It may also further restrict the activities of foreign NGOs, with severe consequences for freedom of expression in the country.

- China’s economic diplomacy entered a new era in 2017. Xi, the first Chinese president to attend the annual World Economic Forum, presented himself in Davos as a true champion of globalisation, committed to developing free trade and investment, promoting trade liberalisation and facilitation, and saying ‘no’ to protectionism.

- In response to its economic slowdown, China is seeking to achieve a ‘new normal’, characterised by economic and social reforms, leading increasingly to more service and technology-oriented economic growth, where market forces are to play a decisive role. In stark contrast, China’s master plan for future manufacturing, entitled Made in China 2025, includes goals to optimise industrial structures by setting specific market-share targets ‘to realise guarantees of self-sufficiency’. The Plan has explicit benchmarks for 10 industries and specifies 10 key policy tools, such as forced technology transfers in exchange for market access, subsidies, and state-owned enterprises (SOEs) to be used in their pursuit. The reform agenda includes the aim of consolidating state-owned enterprises (SOEs) as ‘national champions’ in order to provide more competition to foreign companies and markets. The reforms retain ‘Chinese characteristics’ and still need to demonstrate a major shift away from the strong role of the state in the economy and society.

- China’s transformation requires a shift towards a more efficient and market-based economic model to address the mounting problem of overcapacity, which is much broader and encompasses several other sectors besides steel. Implementing the reforms aimed at cutting overcapacity may not solve the issue in practice as China has a long history of commitments that have not been met.
• **Beijing increasingly acknowledges that achieving 'major country' status comes with responsibilities** as China plays a crucial role in global governance, the rules-based international order and meeting commitments made in the G20 framework. China has demonstrated some movement in shifting away from the pursuit of narrow national aims towards a more active foreign and security policy and increased global financial and economic cooperation, as well as fighting terrorism and protectionism, climate change and migration crises, and promoting fair taxation and food security. At the same time, however, China has been increasingly assertive in Asia, with a number of on-going territorial disputes with its neighbours. Fearing a rapid escalation of tension on the Korean peninsula, China has called on North Korea to stop its nuclear and missile tests and has also halted imports of North Korean coal until the end of 2017. Preventing the protection of economic and strategic interests from turning into disastrous conflicts must remain the prime objective of all, including the major economies.

2 **European Parliament – China: Milestones**

- **14-15 September 2016** Regular Inter-parliamentary exchanges have been frozen by the National People’s Congress (NPC), since the incoming Inter-Parliamentary Meeting (IPM), scheduled for mid-September 2016 was cancelled at short notice, as it coincided with the visit of the Dalai Lama to Strasbourg on 15 September 2016, when he addressed the Committee on Foreign Affairs and met with Martin Schulz, then-president of the European Parliament (EP).

- **6 July 2016** The EP held a debate (2016/2803(RSP)) on the New EU strategy on China adopted by the High Representative and the European Commission on 22 June 2016. The new strategy promotes strategic cooperation between EU and China in three main areas: prosperity and reform agenda; foreign policy and security; and global governance and the multilateral context.

- **16-19 May 2016** The 39th Inter-parliamentary Meeting (IPM) with the National People’s Congress of China was held in Beijing and Chengdu.

- **12 May 2016** In conclusion of several debates held in the European Parliament since the end of 2015, the EP adopted a resolution on China’s market economy status (2016/2667(RSP)), in which it reiterates the importance of the EU partnership with China, but makes clear that until China meets all five EU criteria required to qualify as a market economy, the EU should use a non-standard methodology in anti-dumping and anti-subsidy investigations into Chinese imports.

- **4 February 2016** The EP adopted a resolution on the case of the missing book publishers in Hong Kong (2016/2558(RSP) calling for the immediate release of the five booksellers (Lui Bo, Gui Minhai, Zhang Zhiping, Lin Rongji and Lee Po) and all other persons arbitrarily arrested for exercising their right to freedom of expression and publication.

- **16 December 2015** The EP adopted a resolution on EU-China relations (2015/2003(INI)) stating, inter alia, its position on the escalating tensions between parties in the South China Sea, which called for a peaceful settlement of disputes in accordance with international law and through the UN Convention on the
Law of the Sea (UNCLOS). In the same resolution, Parliament also expressed serious concerns regarding China’s human rights record and violations of the freedoms of expression, assembly, association and religion, especially in Tibet and Xinjiang. The EP also commented on the draft law on counter-terrorism, and the (then draft) Foreign NGO Management Law.

21-23 September 2015 The 38th Inter-Parliamentary meeting (IPM) with the National People’s Congress of China was held in Brussels.

3 Recent political developments in China

The Communist Party of China holds its 19th national congress in 2017. It will assess the performance of President Xi’s first five-year term.

In 2017, President Xi Jinping completes his first five-year term as China’s leader, and the country is due to hold its 19th national congress of the Communist Party of China (CPC), which usually makes a performance assessment of the past five years and sets out political goals for the upcoming five-year period. Five of the seven members of the supreme Politburo Standing Committee have reached the ‘unofficial’ retirement age of 68 years applied according to an ‘unwritten’ rule since 2002, and another six of the 25-member Politburo are also expected to leave office. There is speculation that Xi might break some party rules regarding new appointments.

The last four years, under the leadership of Xi, have seen the systematic strengthening of the Communist Party’s role. The sixth Plenary Session of the 18th Central Committee of the CPC in 2016 approved two documents on the discipline of the Party aimed at comprehensive and stricter intra-party governance. President Xi Jinping was elevated to ‘core’ leader at the session.

President Xi has rapidly consolidated considerable amounts of personal power and promoted ideological unity, pursuing the dream of a great rejuvenation of China in order to restore the people’s trust in the CPC and ensure its survival and supremacy. Although political stability is not in question, at least in the short term, the vast anti-corruption campaign, and the possibility to use new national security rules to crush any hint of dissent by increasing surveillance through ‘discipline inspections’ seem to be intended to ensure the longevity of the Communist regime.

The Party rules also urge that all branches of the system — including the National People’s Congress, the State Council, the Chinese People’s Political...

1 The Central Committee of the Communist Party of China meets once a year, at the most senior members’ level of the Party. The current term is the 18th Party Congress (2012-2017).
3 http://www.hoover.org/sites/default/files/research/docs/clm49am.pdf
6 Xi urges all Chinese to contribute to national rejuvenation, 17.02.2017, http://www.china.org.cn/china/2017-02/17/content_40309410.htm
7 FT, 4.01.2017, The political price of Xi Jinping’s anti-corruption campaign, https://www.ft.com/content/3f1938d6-d1cf-11e6-b06b-680c49b4b4c0

President Xi Jinping has worked to reinforce the Party’s legitimacy by promoting the ‘rejuvenation of China’.
Xi’s consolidation of power began with political manoeuvring against potential political rivals and has culminated in a tough war on corruption. The anti-corruption campaign was initially conceived as a means to increase government transparency and efficiency but has created a massive threat to the bureaucratic elites and has revived concerns about ‘clean-up’ operations. Xi’s anti-corruption campaign has been compared by some commentators to a Stalinist political purge especially after the entry into force on the 1 January 2016 of the Disciplinary Code of the Chinese Communist Party — the harshest disciplinary code since the time of Mao. The CPC Central Commission for Discipline Inspection (CCDI) is, notably, responsible for supervision and inspection of the implementation of the Party’s line, principles, policies and resolutions, complying with China’s laws and regulations. The CCDI disciplined 415 000 people for violating the Party’s code of conduct and for other irregularities in 2016. Moreover, an estimated 900 suspects, 122 of whom were government officials, were arrested for corruption and the CCDI reclaimed about RMB 2.3 billion (EUR 313 million) in the 11 months to November 2016.

Xi’s consolidation of power sought to restore China’s powerful role in the world and in global governance. China, a member of the G20 group, is striving for relevance in global affairs through the UN and other international organisations and bilateral and regional initiatives reaching far beyond its neighbourhood, such as Latin America, the Arctic, the Antarctic and the Middle East, as well as the major ‘One Belt - One Road initiative’.

Xi Jinping, the first of China’s top leaders to attend the World Economic Forum, in Davos, in 2017, claimed the mantle of globalisation champion. At Davos, Xi pointed out that many of the problems troubling the world are not caused by economic globalisation, which has powered global growth and facilitated the movement of goods and capital, advances in science, technology and civilisation, and interactions among peoples. According to him, currently the most pressing task is to steer the global economy out of difficulty and make the process of economic globalisation more invigorated,

inclusive and sustainable, pointing out that the richest 1% of the world’s population own more wealth than the remaining 99%. Xi presented himself in Davos as the true defender of globalisation, committing to develop free trade and investment, promoting liberalisation and facilitation, and saying ‘no’ to protectionism.

China’s unelected legislature, the 3,000 delegates of the National People’s Congress (NPC), representing China’s 31 provinces, municipalities and autonomous regions, as well as Hong Kong, Macau and the military, held its annual meeting from 10 to 15 March 2017. The NPC passes major bills, approves the budget and endorses appointments. In 2016, according to the annual work report of the State Council, it submitted 13 legislative proposals to the Standing Committee of the National People’s Congress (NPC) for approval. The chair is Zhang Dejiang, a former vice-premier and the third most senior person in the Communist Party after President Xi Jinping and Premier Li. Most delegates are hand-picked by local-level officials, but there are also delegates for self-ruled Taiwan, mostly made up of defectors and their descendants.

At this meeting, Premier Li presented a work report, giving China’s version of a State of the Union address. According to the report, a wide range of economic policies and foreign policy goals for 2017 include continued economic restructuring and reforms, revamped efforts on poverty and (air) pollution reduction, and shaping a more prominent role for China on the global stage. The report also specifies as an objective for the government to ‘hold high the banner of socialism with Chinese characteristics’ and maintain ‘political integrity’.

In the report, Li explicitly stated Beijing’s position on ‘Hong Kong independence’, that the ‘notion of Hong Kong independence would lead nowhere’.

On 26 March 2017, Hong Kong’s 1194-member Election Committee elected Carrie Lam as its new chief executive from among three candidates for the fifth term of the Chief Executive of Hong Kong Special Administrative Region. In 2016 pro-democracy activists secured 325 seats.

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18 The race for Hong Kong’s top job has narrowed down to three candidates in an election set for 26 March 2017, when retired judge Woo Kwok-hing, former chief secretary Carrie Lam, and ex-financial secretary John Tsang selected by an election committee to run for Chief Executive, http://www.cnbc.com/2017/03/01/carrie-lam-leads-race-for-hong-kong-chief-executive.html
on the committee — the highest number ever. **Calls for fully free elections in the semi-autonomous region have failed**, despite a series of street demonstrations since 2014’s Occupy Central movement, known as the ‘umbrella protests’. Beijing has shown its readiness to dictate the course of events in Hong Kong and a certain part of the population is increasingly worried by China’s growing influence.\(^\text{20}\)

Moreover, for the first time in the three years since Premier Li began giving ‘state of the union’ addresses, China’s policy on **Taiwan, the ‘One China Principle’** was mentioned. According to the Freedom in the World 2017 report, Taiwan’s civil liberties rating improved from 2 to 1 (**1=Most Free, 7=Least Free**) due to improvements on media independence and academic freedom in recent years, including in media coverage of the 2016 elections.

Regarding the control of the security apparatus, as the ultimate guarantor of power, the **People’s Liberation Army (PLA)** has been somewhat restructured.\(^\text{22}\) Beijing announced on 4 March 2017, apparently its lowest defence spending increase in recent years — an ‘around 7 %’ increase over the current allocation of RMB 954 billion (USD 147 billion), taking Chinese defence spending to approximately RMB 1.020 billion (USD 157 billion).\(^\text{23}\)

Some defence analysts have assessed that China’s actual defence spending is 25 % to 50 % higher than the official figure, which excludes spending on nuclear and missile arsenals, on research and development and large components of the defence industry. In 2017, the US announced a 10 % increase to its defence budget bringing it to USD 603 billion in total.\(^\text{24}\)

**Greater focus has recently been placed on environmental concerns** in China. The government approved a new **Environmental Protection Law (EPL)** — the country’s most progressive and stringent so far — which entered into force on 1 January 2015 and tightened the controls on local government officials dealing with environmental enforcement.\(^\text{25}\) This has even led to the suspension or relocation of major environmentally-risky industrial projects. Investigations into environmental violations by companies are also on the rise and standards are expected to become stricter for foreign companies.

\(^\text{20}\) According to a poll conducted by the Chinese University of Hong Kong (CUHK) in July 2016, 17.4 % somewhat supported or strongly supported independence for Hong Kong, while ‘Maintenance of One Country Two Systems’ beyond expiry in 2047, received 69.6 % of support. The survey respondents were aged 15 or above, with 3.5 % aged between 15 and 17. ‘Direct governance by China’ received 13.8 % of support and 81.2 % of those surveyed stated that the possibility for Hong Kong to attain independence in the future was ‘not possible,’ while 3.6 % stated that it was ‘possible’. Source: https://www.hongkongfp.com/2016/07/25/17-hongkongers-support-independence-2047-especially-youth-cuhk-survery/

\(^\text{21}\) https://freedomhouse.org/report/freedom-world/2017/taiwan


\(^\text{23}\) Business Standard, 5.03.2017,

\(^\text{24}\) http://www.reuters.com/article/us-usa-trump-budget-idUSKBN1661R2

4 China’s economy, social indicators and trade

4.1 Macro-economic update

Despite its economic slowdown, China remains an engine of global growth, generating a fifth of world growth in 2016.

As Asia’s largest economy, and the third largest in the world, China plays a significant role, generating around 18% of global growth in 2016 (IMF). In 2016 China’s economy grew at its slowest pace since 1990 with its GDP growth rate down to 6.7% from 6.9% in 2015. Although China’s growth is outpaceing most other economies, it is expected to continue to slow over the medium term (see below Figure 2: Real GDP growth of selected economies). Despite the slower growth the additional value created by China’s gross domestic product in 2016 is estimated to USD 823 billion, an equivalent of a medium sized G20 economy.

China is navigating a crucial, but complex transformation towards more sustainable growth by rebalancing from investment to consumption and from manufacturing to services. In 2016, growth continued to be led by strong domestic consumption, amounting to 65% of China’s GDP growth. Total retail sales of consumer goods hit RMB 33.2 trillion (USD 4.84 trillion). Over 28 million cars were sold in China in 2016, up 14% from 2015 and the sales of new-energy vehicles grew 53%.

The number of middle-class households (with an annual income of USD 11,500 – 43,000) rose rapidly in China from 5 million in 2000 to 225 million in 2015. Retail sales of consumer goods are estimated to increase around 10%, exceeding RMB 37 trillion in 2016.

GDP based on PPP, % share of world: China - 17.9%, European Union - 16.8% and US - 15.6%

26 REPORT ON THE WORK OF THE GOVERNMENT, Delivered at the Fifth Session of the 12th National People’s Congress, 5.03.2017, states ‘30% of the global growth. 


29 China Consumption Growth Down -- And Heading Lower Fast, 22.01.2017, 

30 The State Council, 21.02.2017, 
http://english.gov.cn/state_council/ministries/2017/02/21/content_281475574171522.htm

31 China’s term new energy vehicles (NEVs) refers to vehicles that are partially or fully powered by electricity, such as battery electric vehicles (BEVs) and plug-in hybrids (PHEVs). Forbes, New Leaks Show Volkswagen To Launch 8 New Energy Vehicles In China, 16.01.2017, 

32 State Council, 
http://english.gov.cn/state_council/ministries/2017/02/21/content_281475574171522.htm

33 Human Development Report 2016, 
The IMF’s growth outlook for China remains broadly unchanged, with a slight upward adjustment in 2017 to 6.5%.

The IMF’s\(^{35}\) growth outlook for China remains broadly unchanged, with a slight upward adjustment in 2017 to 6.5%, 0.3 percentage points higher than their October 2016 forecast. The outlook\(^{36}\) assumes that China manages its transformation process well and gradually reduces its reliance on credit stimulus and other vulnerabilities, such as high and rapidly rising debt level and ‘adjusted’ corporate balance sheets. Another key assumption is the absence of significant disruptions to trade and investment.

The government’s GDP growth target for 2017 is set at ‘around 6.5%’, showing an acknowledgment of the continuing economic slowdown.

China’s transition, or so-called rebalancing, is estimated to be positive overall for the global economy, but is likely to continue to produce spillover effects — through trade, commodity prices, investment and financial markets — that vary by country and by region.

According to the IMF forecast, the share of China’s contribution to the world’s GDP growth is estimated to be around 22% in 2017 (see below Figure 1). The additional value created by China’s gross domestic product is estimated to reach USD 970 billion in 2017.

![Figure 1: Top 10 countries contributing to World nominal GDP growth in 2017 (IMF forecast)](chart)

(Left: % of world growth, right: value of growth in USD billion)

According to the World Bank\(^{37}\), global growth is estimated to increase marginally beyond 2018, reaching 3.8% by 2022. Growth in China is projected at 6.6% in 2017, slowing to 6.2% in 2018. Nevertheless, it is

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China is the world’s third largest economy in terms of GDP after the US and the EU.

In 2016, China accounted for 15% of the world’s nominal GDP (USD 11.4 trillion) (see below Figure 3) after the US with 24.7% (USD 18.6 trillion) and the EU with 22% (16.5 trillion). The three top economies account for around 62% of the world economy.

Source: IMF DataMapper (POLDEP March 2017)

39 IMF, A Middle Ground, Finance & Development, March 2017, Vol. 54, No. 1
According to the National Bureau of Statistics (NBS) data, **China’s service sector accounted for 51.6 % of GDP** in 2016, (up 1.4 % from 2015), and investment in the service sector increased 10.9 % in 2016.

According to the WTO, investment accounted for more than half of China’s GDP growth in 2012-2013, but had fallen to 39 % in 2016.

In 2015 (WB data), the value added of agriculture, including animal husbandry, forestry and fishing (primary sector) accounted for 8.9 % of GDP, while industry accounted for 40.9 %. The contribution of the **service sector to economic growth** reached 50.2 %, for the first time accounting to over half of GDP.

**Figure 4:**
China’s and-EU’s economic sectors (in % of GDP), 2015

![Diagram](source:World Bank)

The ‘rebalancing’ potentially generates the largest adverse spill-overs for economies heavily involved in the ‘Asia value chain’.

**Potential spill-over effect of the ‘rebalancing’**

A study estimates that a spill-over effect of the ‘rebalancing’ as an average annual slowdown of GDP in China of one % point would probably reduce global GDP by about 0.2 percentage points. It is also estimated that a 1 % investment-driven drop in China’s output growth would reduce the whole of the G20’s growth by a quarter of a percentage point.

As the largest exporter in the world and second largest importer, China is at the centre of the global trade network and is among the top trading partners of nearly all countries in the world. The IMF study estimates that China’s **move up the value chain**, i.e. production of higher added value

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41 WTO: Source : WTO, WT/TPR/S/342, China
42 The rebalancing strategy is implemented through two major channels: (1), following World Bank (2014) baseline scenario, assumption that the share of investment in total GDP gradually falls from 46.7 % to 35.5 % in 2030, while the difference accrues to household consumption; (2) structural shift in the Chinese economy allows the importance of the services sector to grow as a share of total value added from 50 % in 2015 to 61 % in 2030.
44 IMF: World Economic Outlook, April 2016.
products (and services), has the potential to generate the largest adverse spill-overs for economies heavily involved in the ‘Asia value chain’ such as Taiwan and South Korea and to a lesser extent Japan and Germany. Another analysis by the IMF\textsuperscript{46} suggests that a 1 % decline in China’s growth implies a 0.3 % reduction in growth for ASEAN Emerging Market Economies (Indonesia, Malaysia, and Thailand) and a 0.2 % decline for Frontier Developing Economies (Cambodia, Lao PDR and Vietnam) in ASEAN.

### 4.2 Development plans and economic reforms

Reforms under the 13\textsuperscript{th} five-year plan for 2016-2020 are centred on rebalancing the economy. China is aimed at attaining a ‘New Normal’ featuring lower, but more service and technology-oriented economic growth.

**The 13\textsuperscript{th} five-year development plan of China**

In response to the country’s economic slowdown, the 13\textsuperscript{th} five-year development plan of China (FYP) for 2016-2020\textsuperscript{47}, endorsed by the National People’s Congress (NPC) in March 2016, translates the reform agenda of the third Plenary Session of 2013\textsuperscript{48, 49} into a set of concrete actions. The economic and social reform process is aimed at achieving greater efficiency, through the ‘New Normal’ that is characterised by somewhat lower, but increasingly more service and technology-oriented, economic growth. By 2020, China aims to double its 2010 GDP and 2010 per capita income of both urban and rural residents\textsuperscript{50}.

**The main structural changes** in the 13\textsuperscript{th} FYP are centred on rebalancing the economy. This aims to boost consumption, expand the service sector and public services, protect the environment, open up the economy and reduce poverty and social imbalances as well as improve access to education and healthcare. The Chinese government plans to continue the process of economic transformation, including the promotion of private-sector participation as well as to strike a balance between the role of the government and that of the market, and society, open up the economy and ‘let the market play the decisive role in allocating resources’\textsuperscript{51}.

However, the reforms have gradually revealed their ‘Chinese characteristics’, as market forces have been given less prominence than expected from the third plenum proposals — a quite different approach from ‘Western supply side economics’.

\textsuperscript{47} China Headlines: Xi expounds on guideline for 13\textsuperscript{th} Five-year Plan, 3.11.2015, http://news.xinhuanet.com/english/2015-11/03/c_134780377.htm
\textsuperscript{49} Communiqué of the Third Plenary Session of the 18\textsuperscript{th} Central Committee of the Communist Party of China, http://www.china.org.cn/china/third_plenary_session/2014-01/15/content_31203056.htm
\textsuperscript{50} http://news.xinhuanet.com/english/2015-11/03/c_134780050.htm
China’s ‘Made in China 2025’ master plan for manufacturing does not appear to give the market a more decisive role, as it includes goals to optimise industrial structures.

The 13th Five-Year Plan for Trade in Service Development actively seeks FTAs to strengthen China’s position in the service market in specific countries.

A master plan for China’s future manufacturing entitled ‘Made in China 2025’ of May 2015 does not appear to give the market a more decisive role since it includes goals optimising industrial structures, notably by setting specific market-share targets ‘to realise guarantees of self-sufficiency’\(^{52}\). The Plan aims at substitution of exports as it sets ‘semi-official’ targets\(^{53}\) for the domestic market share of certain products\(^{54}\). The ‘Made in China 2025’ Plan has explicit targets for 10 industries\(^{55}\) and specifies 10 key policy tools (such as forced technology transfers in exchange for market access, standards, subsidies, financial policy, SOEs and public-private partnerships\(^{56}\)) to be used in their pursuit. Nevertheless, the 13th FYP, for instance, contains targets to rationalise industrial excess capacity (e.g. steel, coal, cement, aluminium, glass and shipbuilding) and to cut state support to ‘zombie’ state-owned firms (SOEs).

The 13th Five-Year Plan for Trade in Service Development

The 13th Five-Year Plan for Trade in Service Development\(^{57}\) (Plan) aims inter alia to promote supply-side structural reforms of the service trade sector, optimising the service-trade system and policy framework, and liberalising and facilitating service-trade and related outward investment. It also strengthens export capacity, including the development of new types of services, such as cross-border e-commerce, supply chain management and service outsourcing and seeks to make active use of Free Trade Agreements (FTA) to strengthen China’s position in the service market in specific countries.

According to the Plan, the expansion of China’s trade in services faces challenges such as weak foreign demand, trade protectionism and other unfavourable factors including increased international competition and reconstruction of international rules on trade in services. China has established trade ties with 230 countries and regions, and the volume of trade in goods is beneficial to the development of related services trade. The number of countries and regions from which China undertook international service outsourcing has reached 197. China has also signed a Memorandum of Understanding on trade in service cooperation with seven countries and regions, and established a trade in service promotion work mechanism to conduct bilateral ‘pragmatic cooperation.


\(^{53}\) According to MERICS PAPERS ON CHINA, such benchmarks are (e.g.): 40 % of mobile phone chips on the Chinese market to be produced in China by 2025, as well as 70 % of industrial robots and 80 % of renewable energy equipment. https://www.merics.org/fileadmin/user_upload/downloads/MPOC/MPOC_Made_in_China_2025/MPOC_No.2_MadeinChina_2025.pdf

\(^{54}\) http://english.gov.cn/premier/news/2017/01/29/content_281475554068056.htm

\(^{55}\) 10 industrial sectors of the ‘China Manufacturing 2025’ strategy, https://www.csis.org/analysis/made-china-2025 ;

\(^{56}\) EU Chamber of Commerce in China: ‘China Manufacturing 2015’, see link above.

\(^{57}\) The 13th Five-Year Plan for Trade in Service Development, 13.03.2017, Ministry of Commerce Website
China has continued to reform its SOEs but is keeping public ownership as the mainstay of the economy.

The on-going reform of state-owned enterprises (SOEs)

Although China is continuing its reforms of state owned enterprises (SOEs), it is keeping public ownership as the mainstay of the economy, while allowing diverse forms of ownership to develop on the side. The State-Owned Assets Supervision and Administration Commission is attempting to deepen the reform of SOEs, prioritising the restructuring of steel, coal and power businesses, and other sectors, including petroleum, gas, railways, telecommunications, civil aviation and military-related industries, to conduct ‘mixed ownership’ reforms. As result, the private sector is ‘dominant’ in industries such as clothing, food, and assembly for export. At the same time, sectors of strategic importance remain dominated by large SOEs (e.g. energy, utilities, transport, financial services, telecommunications, education, health care and defence industries). ‘The Guiding Opinion on Further Deepening the Reform of State-Owned Enterprises’, released in August 2015, divides SOEs into non-profit entities and commercial entities, thus many SOEs function as if they were ‘private’ enterprises. Notably, there is an increasingly urgent need to address China’s corporate debt load — which at 145 % of GDP poses certain risks.

The central government has announced the reorganisation of 22 central SOEs, creating national champions that can push down the profit margins of global competitors as they continue to benefit from state funding.

The profits of China’s SOEs grew 7 % on average in 2016.

58 More reforms in pipeline for SOEs, 24.02.2017
http://english.gov.cn/state_council/ministries/2017/02/24/content_2814755576610165.htm
60 Financial Times, IMF sounds warning on China’s corporate debt, 12.06.2016
https://www.imf.org/en/News/Articles/2015/09/28/04/53/sp061016:
http://www.ft.com/cms/s/0/3f8dcf22-304c-11e6-bda0-04585c31b153.html#axzz4INEA0tDv
61 Including China Ocean Shipping (Group) Co and China Shipping Group, CNR Corp and CSR Corp; new businesses such as AECC Commercial Aircraft Engine Co and China Tower Corp Ltd.
62 http://docs.dpaq.de/12007-european_chamber_cm2025-en.pdf
63 http://english.gov.cn/news/top_news/2017/03/02/content_281475582191280.htm
64 State Council, 9.03.2017,
http://english.gov.cn/state_council/ministries/2017/03/09/content_281475589799681.htm
Transformation of China and global economic interdependence

According to the Chinese National Statistics\(^65\), the total number of enterprises reached 12.6 million in 2015, of which 12.4 million (98\%) were domestically funded; 115 168 were funded from Hong Kong, Macao and Taiwan; and a total of 122 288 enterprises were funded with foreign investment. At the end of 2015, there were 19.08 million `private-owned' enterprises (compared to 845 520 at end-2010)\(^66\).

The People’s Bank of China (PBOC) modified the Chinese currency — the Renminbi (RMB) — exchange-rate fixing mechanism in 2016. The new mechanism to fix the RMB midpoint is based on the closing price from the previous day and by reference to a basket of currencies. The RMB faced depreciation pressure against the USD in the aftermath of the UK referendum in mid-2016\(^67\), and on 14 July 2016, the exchange rate per USD stood at 6.6848\(^68\). On 10 March 2017, the RMB/USD exchange rate stood at 6.9107. It is estimated that RMB/USD rate will reach 7.2 by the end of 2017\(^69\).

The RMB is fully convertible for current account transactions and partly convertible for some capital account transactions. Since 2011, all residents and non-residents have been able to use RMB for foreign direct investments. The Chinese regulators stepped up the rules around off-shoring the currency, requiring from January 2017 that in Shanghai, for every RMB 100 taken out of the country, the inflow needed to be matched.

Portfolio investment continues to be controlled by quotas and can only be done through the Qualified Foreign Institutional Investors\(^71\) licensed to trade RMB, and foreign borrowing is subject to a ceiling (short-term borrowing) or approval requirements (long-term borrowing). Holding of cross-border accounts requires an approval of the State Administration of Foreign Exchange.

In 2015, the IMF decided to include the RMB in the Special Drawing Rights (SDR) currency basket, and on 1 October 2016 it became a freely usable currency along with the US dollar (0.58252), euro (0.38617), Japanese yen

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\(^{65}\) http://www.stats.gov.cn/tjsj/ndsj/2016/indexeh.htm


\(^{67}\) Focus Economics: http://www.focus-economics.com/country-indicator/china/gdp-per-capita-USD


\(^{70}\) G20 China : http://www.g20.org/English/Dynamic/201608/20160801_3106.html

\(^{71}\) https://www.pwc.de/de/kapitalmarktorientierte-unternehmen/assets/fuer-qualified-foreign-institutional-investors-oeffnet-sich-die-tuer-zu-chinas-kapitalmarkt-allmaehlich.pdf
(11.900) and pound sterling (0.085946), as a currency with the third (1.0174) biggest weight in the basket. In 2015, the People’s Bank of China continued its interest rate liberalisation policy and removed the upper limit on deposit interest rates, which marked the end of controls on the interest rates. In 2017, China’s central bank tightened monetary policy by raising the interest rates it charges in open-market operations and on funds lent via its Standing Lending Facility.

Tax reform is an on-going priority. The Chinese authorities, which are likely to release a specific plan in the first half of 2017. As a result of the implementation of the value added tax (VAT) reform on services, taxes have been reduced by an estimated RMB 500 billion (USD 72.7 billion) since May 2016 for businesses across the nation.

China also completed negotiations with the US on an intergovernmental agreement (in substance) on the US Foreign Account Tax Compliance Act (FATCA) in 2015. FATCA requires foreign financial institutions to report to the IRS information about financial accounts held by US taxpayers, or by foreign entities in which US taxpayers hold a substantial ownership interest.

As China’s economic growth enters the phase of ‘New Normal’, it is addressing convictions, such as employment is the foundation of the livelihoods of the people. The government is implementing the ‘Employment First Strategy’ and a more active employment policy, strengthening regulation and improving services, as well as promoting entrepreneurship and innovation. It is also working to develop vocational education and training and improve the social protection system.

At the end of 2016, the total number of employed people in China was 776 million: 414 million in urban areas and 362 million in rural areas. The total number of migrant workers in 2016 was 282 million, up by 1.5 %

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The registered urban unemployment rate remains about 4%, roughly the same since 2010. China’s sole legally mandated trade union, the All-China Federation of Trade Unions (ACFTU), has a presence in many workplaces but the union representatives are largely under the sway of management.

The total wage bill in 2015 amounted to RMB 112 trillion, of which state owned enterprises represented 36%, collectively owned 2% and ‘other types of ownership’ 62%. The average annual wage of employed persons in state-owned units was RMB 65,296, compared to RMB 60,906 in the other types of ownership unit. The per capita disposable income nationwide of RMB 20,167 was about double of the per capita disposable income of rural households of RMB 10,489 in 2015.

### 4.3 Social indicators

There were over 55 million poor in rural areas in 2015. However, China’s extreme poverty rate has fallen.

According to China’s current poverty standard (per capita rural net income of RMB 2,300 per year, (EUR 313 or USD 330 per year), there were 55 million poor in rural areas in 2016, in comparison to 70.2 million in 2015. According to the State Council, China lifted 12.4 million people out of poverty in 2016. The official figure for the average income of the poorest 5% of households in Chinese cities is about USD 1,128 (RMB 7,521) a year, more than three and a half times greater than China’s rural poverty line. One of the targets of the 13th Plan is to increase the urbanisation ratio, based on the number of registered residents who have official residence status, so called ‘hukou’, to reach around 45% by 2020.

The results of China’s poverty reduction have been acknowledged in the World Bank Global Monitoring Report 2015-2016, as well as in the UN Report on Sustainable Financing for Poverty Alleviation in China.

In parallel, income inequality overall has gone up in China. The most commonly used measure of income inequality, the Gini coefficient, went from less than 30 in the early 1980s to 46.2 in 2015.

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80 [http://www.clb.org.hk/content/wages-and-employment](http://www.clb.org.hk/content/wages-and-employment)
83 State Council, 21.03.2017, [http://english.gov.cn/state_council/vice_premiers/2017/03/21/content_281475602361911.htm](http://english.gov.cn/state_council/vice_premiers/2017/03/21/content_281475602361911.htm)
87 ADB: The Gini coefficient of per capita household income (or consumption) is a commonly used measure of income inequality, and it ranges from 0 indicating perfect equality to 100 (or 1) indicating perfect inequality. [http://www.adb.org/sites/default/files/publication/186143/wdp-489.pdf](http://www.adb.org/sites/default/files/publication/186143/wdp-489.pdf)
88 The Economist: Inequality in China - Rising rural incomes are making China more equal,
4.4 Trade policy issues

China, with other G20 partners, recognised in July 2016 that structural problems, including excess capacity in steel and other industries, had a negative impact on trade and workers. Overcapacity

China, with other G20 partners, recognised in July 2016 that structural problems, including excess capacity in steel and other industries, exacerbated by a weak global economic recovery and depressed market demand, had a negative impact on trade and workers. The G20 steelmaking economies agreed to participate in the global community’s actions to address global excess capacity.

As a result, the G20/OECD Global Forum on Steel Excess Capacity which was established on 16 December 2016. It will report annually to the G20 and has a three-year, renewable mandate. China has taken steps to cut excess production capacity.

China’s problem of overcapacity is much broader and encompasses several other sectors besides steel. According to the State Council, measures have included discouraging production and there are 23 projects in industries with excess capacity, such as the iron and steel, electrolytic aluminium, cement, plate glasses and vessels (ship) industries. In 2015, excess production capacity was reduced by 13 million metric tons of iron, 17 million metric tons of steel, 38 million metric tons of cement, 300 000 metric tons of electrolytic aluminium, and 11 million weight cases of plate glass. Efforts were stepped up to tackle the coal industry. According to the State Council, in 2016 China’s production of steel and coal was reduced by 45 million metric tons and 250 million metric tons, respectively.

The government’s capacity reduction targets in the coal and steel sectors were set at 100 million metric tons tonnes to 150 million metric tons by 2020 (10–15 % of existing capacity over the next five years).

According to the Human Resources Ministry, a further 500 000 jobs across the coal and steel sectors should be cut in 2017, and total jobs cut from 2016 through 2017, for both steel and coal, are estimated at about 1.2 million. If accurate, these figures would indicate that the target — set by the government in early 2016 — of cutting 1.8 million jobs (in aluminium, cement, coal, construction, plate glass, and steel sectors) would be met. A RMB 100 billion restructuring fund was set up to re-employ and resettle the estimated 1.8 million (1 % of total employment) affected workers.

The government’s figures would indicate that the target, set in early 2016, would mean cutting 1.8 million jobs.

China has taken steps to cut excess production capacity.

91 Full text: Report on China’s economic, social development plan, 23.03.2016.
The problem of overcapacity in a number of heavy industries has its roots in state support to state owned enterprises and in some trade-distorting practices. In January 2017, because of alleged breaches of WTO rules, the US\textsuperscript{96} requested WTO consultations with China concerning subsidies that China appears to provide to certain producers of primary aluminium through artificially cheap loans from banks and through artificially low-priced inputs for aluminium production, such as coal, electricity, and alumina.

The State Council issued punishments to two steel producers for violating China’s capacity cut rules in 2016\textsuperscript{97}. Despite Chinese reassurances, \textbf{Chinese steel production is estimated to grow by 1.6 % over the year 2016.} China now produces 49.6 % of all crude steel in the world.

![Crude steel production](source: World Steel Association, World Steel in Figures 2016)

\textbf{Figure 5:} China’s Crude steel production

The \textbf{Global Enabling Trade Report 2016}, co-published by the World Economic Forum and the Global Alliance for Trade Facilitation\textsuperscript{98}, measures 136 countries on the basis of domestic and foreign market access; border administration; transport and digital infrastructure; transport services; and operating environment. \textbf{China is ranked in 61\textsuperscript{st} place in the index, behind the best countries in its neighbourhood} - Singapore (first), Hong Kong (third) and Japan (16\textsuperscript{th}) - as well as the US (22\textsuperscript{nd}). The country performs best in the transport infrastructure category, where it ranks 12\textsuperscript{th} globally. Countries such as India (102\textsuperscript{nd}), Brazil (110\textsuperscript{th}) and Russia (111\textsuperscript{th}) are beyond the 100\textsuperscript{th} mark.

\textsuperscript{95} Aluminium wars will unfold between China and the West, 3.08.2016.
\textsuperscript{97} 30.12.2017, \url{http://english.gov.cn/policies/latest_releases/2016/12/30/content_281475528934632.htm}
\textsuperscript{98} WEF, \url{https://www.weforum.org/agenda/2016/12/china-approach-to-free-trade}
Although China became the world’s largest exporter in 2010\(^9\), it remains relatively closed to exports from other countries. According to the index, with average applied tariffs of 11.1%, the country ranks 121\(^{st}\) out of 136 countries for domestic market access. There are signs that the country is committing to open up duty-free and quota-free access to its markets for least-developed countries. This in turn helps China’s own economic development, as lower-priced inputs from commodity-exporting countries help to enhance its competitiveness in the manufacturing sector.

4.5 Key economic indicators

In the World Bank’s Ease of Doing Business 2017 data, China is ranked in 78\(^{st}\) place (out of 190 economies), gaining two places since the 2016 report\(^10\). According to the data, starting a business in China requires 9 procedures, takes 28.9 days, and costs 0.7% of income per capita. Most indicator sets refer to a case scenario in the largest business city of an economy. Globally, China stands at 127 in the ranking of 190 economies on the ease of starting a business.

In the Global Competitiveness Index (2016-2017), China ranks 28\(^{th}\) (out of 138 economies), with a score of 4.95 (7 is most competitive score). China’s position is ahead of several EU Member States such as Estonia (30), Czech Republic (31), Spain (32), Lithuania (35) and Poland (36), while Taiwan is in 14\(^{th}\) place.

According to the Transparency International, Corruption Perceptions Index (2016)\(^101\), which measures the perceived levels of public sector corruption worldwide, China’s ranking moved up to 79\(^{th}\) place — out of 176 economies — but retains the poor score of 40 out of 100. Combatting China’s endemic corruption is high on the agenda of President Xi\(^102\).

In the Rule of Law Index 2016 issued by the World Justice Project, China ranks 80\(^{th}\) out of 113 countries\(^103\) with a score of 0.48. Performance (scores range from 0 to 1) is measured using 44 indicators across eight primary rule of law constraints: government powers; absence of corruption; open government; fundamental rights; order and security; regulatory enforcement; civil and criminal justice. Western Europe and North America accounts for eight of the top 10 places in the rankings, with Denmark remaining the highest-ranked country, followed by Norway, Finland and Sweden.

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\(^{9}\) WTO, https://www.wto.org/english/res_e/booksp_e/anrep_e/wtr11-1_e.pdf

\(^{10}\) World Bank: http://www.doingbusiness.org/~/media/wbg/doingbusiness/documents/profiles/country/chn.pdf


4.6 Trade and investment

According to the World Bank[^104], China is deeply integrated into the world economy, as its imports account for one tenth of global imports, its output makes up one tenth of the global total and its investment accounts for one fifth of world investment.

In 2016 China was, in value terms, the world's 3rd largest trader[^105] (excluding intra-EU28 trade), with a total import and export volume of USD 3.69 trillion, down 6.8 % from 2015. The EU was on the top, with the total trade volume of USD 3.82 trillion; followed by the US, with USD 3.71 trillion. Together with Japan, the 4th largest trader (USD 1.25 trillion), they represent around 50% of the total world trade in value terms in 2016.

The trade surplus of China, although down 14.1 % from 2015, accounted to USD 510 billion. Both exports and imports of goods continued to decline in 2016:

- exports amounted to USD 2.10 trillion, down 7.7 %; and
- imports declined to USD 1.59 trillion, down 5.5 % from 2015.

As China is an integral part of the global value chain, much of its exports are foreign-produced components delivered for final assembly in the country. The import content of Chinese investment spending fell from around 30 % in 2004 to 18 % in 2014 as China sourced intermediate goods domestically[^106].

![Figure 6: China’s main export Commodities (2016)](image)

<table>
<thead>
<tr>
<th>Commodities</th>
<th>Value (in USD 100 million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Clothes and clothing accessories</td>
<td>10 413</td>
</tr>
<tr>
<td>Automatic data processing machines and components</td>
<td>9 068</td>
</tr>
<tr>
<td>Handheld mobiles and car telephones</td>
<td>7 643</td>
</tr>
<tr>
<td>Textile yarns and textile articles</td>
<td>6 925</td>
</tr>
<tr>
<td>Rolled steel</td>
<td>3 587</td>
</tr>
<tr>
<td>Furniture and parts</td>
<td>3 151</td>
</tr>
<tr>
<td>Footwear</td>
<td>3 113</td>
</tr>
</tbody>
</table>


Combined January-February 2017 data[^108] shows an increase of 13.3 % (year-on-year), as the total import and export volume reached USD 563.5 billion. China's trade surplus was down by 50.4 %, given the surge of imports by 26.4 %, to USD 260.7 billion, while exports increased only 4 % to USD 302.8 billion in the same period.


[^107]: [http://english.gov.cn/archive/publications/2017/03/01/content_281475581314953.htm](http://english.gov.cn/archive/publications/2017/03/01/content_281475581314953.htm)

In the first quarter of 2017, it is estimated that China’s total imports grew by 31.1 %, while its exports growth was 14.8 %.

In February 2017, exports fell 1.3 % from the previous year, but imports soared 38.1 %, with the result that China ended up with a rare trade deficit of USD 9.15 billion — the first since February 2014. In January 2017, China recorded a trade surplus of USD 51.35 billion. It is difficult to assess China’s trade situation in January-February due to volatility created by the impact of the Chinese New Year holiday.

In the first quarter of 2017, it is estimated that China’s total imports grew by 31.1 % (year-on-year), while its exports growth was 14.8%.

![China's trade in goods](image)

**Figure 7:** China’s trade in goods in USD billion

![China’s production/assembly](image)

**Figure 8:** China’s production/assembly (2015) % of world production

<table>
<thead>
<tr>
<th>Chinese production or assembly (estimate)</th>
<th>% of world production</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cars</td>
<td>28</td>
</tr>
<tr>
<td>Ships</td>
<td>41</td>
</tr>
<tr>
<td>Computers</td>
<td>80</td>
</tr>
<tr>
<td>Mobile phones</td>
<td>90</td>
</tr>
<tr>
<td>Refrigerators</td>
<td>50</td>
</tr>
<tr>
<td>Air conditioners</td>
<td>80</td>
</tr>
<tr>
<td>Colour TV sets</td>
<td>60</td>
</tr>
<tr>
<td>Steel</td>
<td>50</td>
</tr>
</tbody>
</table>


The main destinations for China’s merchandise exports remained the United States (18 %); the EU (16 %); Hong Kong (15 %); Japan (6 %); and the Republic of Korea (4 %). In this context, China’s statistics indicates that ASEAN region absorbs 12 % of its exports. Chinese merchandise exports to the Russian Federation increased by 14.4 %, by far the highest increase in 2016, but representing 1.8 % of the total volume.

In 2016 imports under processing trade accounted for 26.6 % of China’s total goods. The main sources of its imports were the EU (13.0 %); the Republic of

110 [http://english.gov.cn/archive/publications/2017/03/01/content_281475581314953.htm](http://english.gov.cn/archive/publications/2017/03/01/content_281475581314953.htm)
Korea (10 %); the United States (8.5 %); Japan (9.2 %); Taiwan (8.8 %); and the Russian Federation (2 %).

In 2016, China continued to be a net importer of agricultural product. The main import commodities\(^{111}\) included: cereals and cereals flour; soybean; edible vegetable oil; crude oil; iron ore and concentrate; aluminium oxide; plastics in primary forms; and vehicles.

Economic interdependence has helped to reduce certain political tensions that China faces within its neighbourhood.

**Figure 9:**
China's top five trade in goods partners in 2016 (in 100 million yuan)

<table>
<thead>
<tr>
<th>#</th>
<th>Origin</th>
<th>100 million yuan</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>EU</td>
<td>13 747</td>
<td>13.1</td>
</tr>
<tr>
<td>2</td>
<td>ASEAN</td>
<td>12 978</td>
<td>12.4</td>
</tr>
<tr>
<td>3</td>
<td>South Korea</td>
<td>10 496</td>
<td>10.0</td>
</tr>
<tr>
<td>4</td>
<td>Japan</td>
<td>9 626</td>
<td>9.2</td>
</tr>
<tr>
<td>5</td>
<td>Taiwan</td>
<td>9 203</td>
<td>8.8</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>#</th>
<th>Destination</th>
<th>100 million yuan</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>US</td>
<td>25 415</td>
<td>18.4</td>
</tr>
<tr>
<td>2</td>
<td>EU</td>
<td>22 369</td>
<td>16.2</td>
</tr>
<tr>
<td>3</td>
<td>Hong Kong</td>
<td>19 009</td>
<td>13.7</td>
</tr>
<tr>
<td>4</td>
<td>ASEAN</td>
<td>16 894</td>
<td>12.2</td>
</tr>
<tr>
<td>5</td>
<td>Japan</td>
<td>8 529</td>
<td>6.2</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>#</th>
<th>Partner</th>
<th>100 million yuan</th>
<th>balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>EU</td>
<td>36 116</td>
<td>+ 8 622</td>
</tr>
<tr>
<td>2</td>
<td>US</td>
<td>34 302</td>
<td>+ 16 528</td>
</tr>
<tr>
<td>3</td>
<td>ASEAN</td>
<td>29 872</td>
<td>+ 3 916</td>
</tr>
<tr>
<td>4</td>
<td>Hong Kong</td>
<td>20 116</td>
<td>+ 17 902</td>
</tr>
<tr>
<td>5</td>
<td>Japan</td>
<td>18 155</td>
<td>- 1 097</td>
</tr>
</tbody>
</table>


**Figure 10:**
China’s exports and imports of services (in USD billion)

Source: World Bank - World Integrated Trade Solutions (WITS); WTO Press/791

**China’s Imports of commercial services have surged**\(^{112}\) since the beginning of 2010, from USD 140.9 billion to USD 468.9 billion in 2015, but slightly declined to USD 449 billion in 2016. Total commercial services imports represented more than a quarter of total imports in 2016\(^{113}\).

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\(^{112}\) WTO, https://www.wto.org/english/news_e/pres17_e/pr791_e.htm

Services accounted for over 16% of China’s total foreign trade in 2015.

Exports of services more than doubled from USD 117.5 billion in 2010 to USD 286.5 billion in 2015\(^\text{114}\), but decreased to USD 207 billion in 2016. In exports of services tourism constitutes the biggest share, but it has been growing much less rapidly than imports. Total commercial services exports were around 10% of total imports in 2016.

According to the WTO\(^\text{115}\) the EU remained at the top, with both exports and imports of commercial services, amounting to USD 879 billion and USD 725 billion, respectively in 2016.

The government’s figures for 2016 are: China’s imports (USD 314.8 million) and exports (USD 592.4 million) of services totalled USD 907.2 million. The trade in services accounts for 18% of China’s total foreign trade (the total of trade in goods and trade in services). China has become one of the most important services exporters (ranking in sixth place in the world in 2015). Travel, transport, and other business services have become the largest exporting sectors for China in the past few years. China’s exports in computer and information services in 2015 amounted to USD 24.55 billion (8.6% of the total). The value of international service outsourcing undertaken by Chinese business amounted to USD 64.64 billion in 2015. Hong Kong has also emerged as a prime financial services export hub.

Figure 11:
World exports of commercial services by selected economy, 2006-2015 (in USD billion)

Source: WTO Statistics Database

China is one of the most active countries in opening up various industries to foreign investors. The ‘Catalogue for the Guidance of Industries for Foreign Investment’ stipulates in which of over 400 industry sectors foreign investment is ‘encouraged’, ‘restricted’ or ‘prohibited’. In 2015 the Catalogue was revised, cutting the number of industries in which foreign investment is restricted by 50%. The number of industries in which the amount of foreign investment is limited was reduced by 40% and over 95% of all foreign investment projects are now only required to be registered with the relevant


China has continued to seek to attract FDI through facilitating procedures and a number of incentive schemes including the four pilot Free Trade Zones (Shanghai, Guangdong, Tianjin and Fujian). In April 2015, the State Council issued the ‘Special Administrative Measures of Pilot Free Trade Zone for Admittance of Foreign investments’ so-called ‘Negative List’. The 2015 Negative List sets out 122 prohibited or restricted areas, reduced from 139 in the 2014 Negative List. In August 2016117, Chinese authorities decided to set up seven new Free Trade Zones across the country, bringing the total number to 11, as China looks to replicate the success of previous pilot zones.

On 17 January 2017, the State Council released the Circular on ‘Several Measures concerning the Expansion of Opening-up and Active Use of Foreign Capital’, unveiling new guidelines on Chinese foreign investment policy for the next five to 10 years with a view to facilitating foreign investment, including measures aimed at relaxing market access of foreign investment. The measures include making manufacturing sector more attractive to foreign capital, including the ‘Made in China 2025’ strategy and the strategy of innovation-driven development.118 The implementing measures are to be finalised in the near future. The Catalogue of Investment Projects Subject to Government Verification lists specific projects in areas such as: agriculture, energy, transportation, information technology, raw materials, manufacturing of machinery, light manufacturing, high and new technology and construction in urban areas, which would require verification (i.e. approval) for both domestic and foreign investment119.

Inward Investment to China

According to UNCTAD, global foreign direct investment (FDI) flows fell 13 % in 2016, reaching an estimated USD 1.52 trillion120 but the decline was not equal across regions as FDI flows to developed economies fell 9 % to an

\[ \text{Sources: UNCTAD, WTO, International Organizations, and National Statistics} \]

120 WTO 2016, WT/TPR/S/342 • China
estimated USD 872 billion, but their share in world FDI flows as a whole is estimated to 57% of the total. However, total FDI flows to Europe fell 29% to an estimated USD 385 billion. The United States remained the largest recipient of FDI, with an estimated USD 385 billion in inflows, followed by the United Kingdom with USD 179 billion, jumping up from the 12th position in 2015.

**In 2016 China remained in third position, with a record inflow of USD 139 billion** and a 9% share of the total. In contrast, investment flows in absolute terms declined in Hong Kong (China) — from USD 175 billion to an estimated USD 92 billion. In 2016, a total of 12 753 Hong Kong-funded projects, worth USD 81.5 billion (which is down 5.7% in 2015), were approved in China.

**Chinese Outward Investment**

According to China’s Ministry of Commerce (MOFCOM), Chinese investors provided direct investment overseas in 2016 to 7 961 enterprises in 164 countries and regions. Direct overseas outbound investment (excluding banking, securities and insurance)\(^{122}\) amounted to RMB 1.13 trillion, up 44% from 2015 — equivalent to USD 170.1 billion (up 44.1% from 2015\(^{123}\)). Among these, investment in equity and debt instruments totalled RMB 1 trillion (equivalent to USD 152.1 billion, up 50.3% from 2015), accounting for 89.4% of total investments; the re-investment of earnings reached RMB 119.6 billion (equivalent to USD 18 billion, up 7.1% from 2015), accounting for 10.6%\(^{124}\).

Chinese enterprises provided direct investments of USD 14.5 billion in 53 countries for the 'One Belt One Road' (OBOR) initiative in 2016, making up 8.5% of the total FDI outflow of USD 170.1 billion. The destinations of these investments were mainly Singapore, Indonesia, India, Thailand and Malaysia.

**In 2016, China's investment in Hong Kong reached USD 86.2 billion, accounting for 50.7% of the total** of USD 170.1 billion. By the end of 2016, direct investment in Hong Kong had accumulated to USD 492.2 billion, accounting for 52.9% of the total investment stock.

UNCTAD shows that outward FDI from China rose by 3.6% to EUR 115.0 billion\(^{125}\) in 2015. As a result in 2015 China was the third-largest investor worldwide, after the United States and Japan. China has been by far the largest foreign owner of US government debt for several years owning about 8% of the total stock. Japan took the lead with USD 1.13 trillion, compared to China’s USD 1.12 trillion at the end of October 2016. As of January 2017, the US debt to China amounted to USD 1.05 trillion after Japan's USD 1.10 trillion\(^{126}\).

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\(^{123}\) China’s outbound investment to slow in 2017, 10.02.2017, [http://english.gov.cn/state_council/ministries/2017/02/10/content_281475563839316.htm](http://english.gov.cn/state_council/ministries/2017/02/10/content_281475563839316.htm)

\(^{124}\) Brief Statistics on China’s Non-Financial Direct Investment Overseas in January-November of 2016, Ministry of Commerce

\(^{125}\) Calculations done by POLDEP, exchange rate: EUR 1 = USD 1.1095 (average 2015)

\(^{126}\) [MAJOR FOREIGN HOLDERS OF TREASURY SECURITIES, 15.03.2017, [http://ticdata.treasury.gov/Publish/mfh.txt](http://ticdata.treasury.gov/Publish/mfh.txt)]
One of the key outcomes of China’s G20 presidency was the establishment of the Trade and Investment Working Group (TIWG) in 2016 that delivered the G20 Guiding Principles for Global Investment Policymaking (G20 Guiding Principles). The G20 Guiding Principles, although voluntary, include important elements such as fostering an open, transparent, coherent and non-discriminatory global policy environment for investment, avoiding protectionism and providing protection for investment. It has also a strong statement around key areas of investment policy-making (whether at the domestic or international levels), such as entry and establishment, treatment and protection, promotion and facilitation, and the settlement of disputes.

Source: UNCTAD

**Figure 12:**
China FDI flows with world in EUR million


**Figure 13:**
China FDI stocks with world in EUR million

Source: UNCTAD

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127 Calculations done by POLDEP, exchange rate: 1 EUR=1.1095 USD (average 2015)
128 Ibid.
129 [http://g20chn.org/English/Documents/Current/201609/t20160914_3464.html](http://g20chn.org/English/Documents/Current/201609/t20160914_3464.html)
Whilst China has been active in the multilateral trading system since its accession to the WTO, it is now fulfilling its ambition to become a **world trade leader** by implementing its comprehensive Free Trade Agreement (FTA) strategy, which consists of regional, sub-regional and bilateral trade and investment liberalisation and facilitation as well as cooperation arrangements.

Currently, **China is the top trading partner** of over 120 countries/regions\(^{131}\). Its commercial strategy extends far beyond its close neighbourhood, reaching out to Latin American, Central Asian and European countries (see below a table of FTAs).

Moreover, China’s objective is to deepen international industrial capacity cooperation, with a view to promoting the export of Chinese equipment, technologies, standards, and services, for example, through **the ‘OBOR’ Forum for International Cooperation**.

Currently, China has nine negotiations on a preferential trade agreement (FTA) ongoing and 14 of 17 signed agreements are in force. China is also considering negotiations with several partners on the basis of a ‘feasibility study’.

Since 2014, China has continued to deepen its integration with Hong Kong and with Macao through the signing of supplementary agreements to their respective **Closer Economic Partnership Arrangements** (CEPAs). China is a member of the Asia-Pacific Economic Cooperation (APEC) forum, and a signatory to the Asia-Pacific Trade Agreement. The fourth Ministerial Council of Asia-Pacific Countries Trade Agreement was held on 13 January 2017 in Thailand\(^ {132}\).

China and the Association of Southeast Asian Nations (ASEAN) signed the ‘CAFTA’ FTA in November 2015 and the upgrading Protocol of CAFTA\(^ {133}\), aimed at improving the original CAFTA agreement, at the end of 2016.

Within the framework of **South-South cooperation**, China continues to provide technological assistance and grant **unilateral preferences to the least developed countries (LDCs)**. As of December 2015, duty-free treatment on 97% of tariff lines is granted to 33 LDCs.

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**Figure 14:** China’s free trade agreements

<table>
<thead>
<tr>
<th>List of notified RTAs in force(^ {134})</th>
<th>Free Trade Agreements under Negotiation(^ {135})</th>
<th>Under Feasibility Study</th>
</tr>
</thead>
<tbody>
<tr>
<td>ASEAN - China FTA (Upgraded)</td>
<td>China-GCC (Gulf Cooperation Council) FTA</td>
<td>China-India Regional Trade Arrangement Joint Feasibility Study</td>
</tr>
<tr>
<td>Asia Pacific Trade Agreement (APTA)</td>
<td>China-Norway FTA</td>
<td>China-Canada FTA Joint Feasibility Study</td>
</tr>
</tbody>
</table>

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\(^{134}\) WTO - Participation in Regional Trade Agreements: [http://rtais.wto.org/UI/PublicSearchByMemberResult.aspx?MemberCode=156&lang=1&redirect=1](http://rtais.wto.org/UI/PublicSearchByMemberResult.aspx?MemberCode=156&lang=1&redirect=1)

<table>
<thead>
<tr>
<th>Country 1</th>
<th>FTA</th>
<th>Country 2</th>
<th>Country 3</th>
</tr>
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<tbody>
<tr>
<td>Pakistan</td>
<td>China-Japan-Korea FTA</td>
<td>China-Columbia FTA</td>
<td>Joint Feasibility Study</td>
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<tr>
<td>China</td>
<td>China-India FTA</td>
<td>China-Moldova FTA</td>
<td>Joint Feasibility Study</td>
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<tr>
<td>China</td>
<td>China-Israel FTA</td>
<td>China-Jamaica FTA</td>
<td>Joint Feasibility Study</td>
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<tr>
<td>China</td>
<td>China-Taiwan FTA</td>
<td>China-Mauritius FTA</td>
<td>Joint Feasibility Study</td>
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<td>China</td>
<td>China-Singapore FTA</td>
<td>China-Pakistan FTA</td>
<td>Joint Feasibility Study</td>
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<tr>
<td>China</td>
<td>China-Sri Lanka FTA</td>
<td>China-Nepal FTA</td>
<td>Joint Feasibility Study</td>
</tr>
<tr>
<td>Peru</td>
<td>China-Maldives FTA</td>
<td>China-Mauritius FTA</td>
<td>Joint Feasibility Study</td>
</tr>
<tr>
<td>Chile</td>
<td>China-Georgia FTA</td>
<td>China-Mauritius FTA</td>
<td>Joint Feasibility Study</td>
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<tr>
<td>China</td>
<td>China-New Zealand FTA</td>
<td>China-Pakistan FTA (second phase)</td>
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<td>China</td>
<td>China-Hong Kong FTA</td>
<td>China-Pakistan FTA (second phase)</td>
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<td>China</td>
<td>China-Hong Kong FTA</td>
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<td>Iceland</td>
<td>China-Pakistan FTA</td>
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<td>Switzerland</td>
<td>China-Pakistan FTA</td>
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<td>China</td>
<td>China-Pakistan FTA</td>
<td>China-Pakistan FTA (second phase)</td>
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<td>Australia</td>
<td>China-Pakistan FTA</td>
<td>China-Pakistan FTA (second phase)</td>
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<td>Pakistan</td>
<td>China-Pakistan FTA</td>
<td>China-Pakistan FTA (second phase)</td>
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<tr>
<td>The Cross-Straits Economic Cooperation Framework Agreement (ECFA) 136</td>
<td>Asia Pacific Trade Agreement (APTA) - Accession of China</td>
<td>Asia Pacific Trade Agreement (APTA) - Accession of China</td>
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</tbody>
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Despite tensions over competing territorial claims in the resource-rich South China Sea, the 12th round of negotiations on the trilateral China, South Korea and Japan FTA agreement took place on 13 April 2017 in Tokyo137. The three parties exchanged views on issues, such as trade in goods, trade in services and investment. In the joint declaration138 of the 11th round held in January 2017, the parties reiterate their intention to accelerate the negotiations and conclude a comprehensive, high-level and mutually beneficial FTA. On this occasion, South Korea also introduced its initiative to create a Northeast Asia Development Bank (NEADB). The Trilateral Investment Agreement came into effect in May 2014. The 11th trilateral Economic and Trade Ministers’ Meeting139 on 29 October 2016 reaffirmed the commitment to make greater efforts to accelerate negotiations for both the Regional Comprehensive Economic Partnership (RCEP) and the trilateral FTA.

The bilateral FTA between China and the Republic of Korea was signed in June 2015. The FTA governs almost USD 300 billion in trade in goods and

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136 ECFA entered into force 12.09.2010, but many follow up agreements under negotiations. Taipei Times: TPP must come before China deals, [http://www.taipeitimes.com/News/editorials/archives/2016/02/19/2003639680/2](http://www.taipeitimes.com/News/editorials/archives/2016/02/19/2003639680/2)


China's FTA with Australia was signed in 2016.

FTA negotiations are continuing with the Gulf Cooperation Council.

The first meeting on the China-Canada FTA was held in February 2017 with a view to deciding whether the parties should launch FTA negotiations in future.

China is party to the negotiations on the Regional Comprehensive Economic Partnership (RCEP) with ASEAN.

services. Upon the FTA’s entry into force, Korea and China will fully eliminate 50% and 20% of tariff lines, respectively. Within 10 years the Republic of Korea and China will liberalise 79% and 71% of tariff lines, respectively. It will progressively eliminate tariffs within 20 years on the majority of Republic of Korea-China trade in terms of import value: 85% for China and 91% for Korea.

The China-Australia FTA was signed on 17 June 2016 and officially implemented as of 20 December 2016. The Australian talks with China were delayed for several years due to concerns from Australia’s agricultural sector. The first meeting of the China-Australia FTA Joint Committee was held in February 2017. The China-Australia FTA covers over 10 areas including goods, service and investment and is one of the highest-level trade and investment liberalisation agreements that China has so far signed with other countries. The FTA further promotes the growth of trade in services in areas such as bilateral aviation, tourism, education and finance. In 2016 China’s direct investment in Australia reached USD 3.68 billion, up 56.1% from 2015, covering many fields such as real estate, leasing and business services industry, transportation and warehousing industry and manufacturing industry.

Regarding China-Gulf Cooperation Council (GCC), the ninth round of FTA negotiations took place in December 2016, when the two parties conducted far-reaching negotiations on the content of leftover problems such as services trade, investment, e-commerce and trade in goods, and concluded the negotiation on chapters such as economic and technical cooperation.

The meeting of ‘Feasible Study and Exploratory Discussion’ on China-Canada FTA was held in February 2017, when the two sides analysed the potential for bilateral trade and economic cooperation with a view to deciding whether to launch the FTA negotiations in the future.

The Regional Comprehensive Economic Partnership (RCEP) is a 16-party FTA on which negotiations centred around ASEAN were launched in the margins of the East Asia Summit in Phnom Penh, Cambodia, on 20 November 2012 by the leaders of the 10 ASEAN countries and the existing FTA partners of ASEAN — Australia, China, India, Japan, Republic of Korea and New Zealand. The 17th round of negotiations for RCEP was held in Japan, from 27 February to 3 March 2017. The round included working group meetings on goods, services, investment, intellectual property, e-commerce,
The RCEP is seen as China’s alternative or response to the Trans Pacific Partnership agreement and laws and mechanisms in other fields. The RCEP negotiation plan for 2017 aims to speed up the progress of the negotiations and the 18th round of negotiations is scheduled for 2-12 May 2017 in the Philippines.

The RCEP is seen as China’s alternative or response to the Trans Pacific Partnership agreement (TPP)\(^\text{147}\), from which China has been excluded\(^\text{148}\). In 2017, the Chinese foreign minister, Wang Yi, called for joint efforts to conclude the RCEP negotiations at an early date, and stated that ‘Either the RCEP or TPP or other regional arrangements is a possible path to the broader Free Trade Area of the Asia-Pacific’ (FTAAP)\(^\text{149}\).

However, in contrast to the TPP, the RCEP is not a ‘new generation’ trade agreement and will represent an agreement consisting of some WTO plus commitments, at best. Differences between the TPP and the RCEP, based on the current negotiations, include chapters such as state-owned enterprises, environment and government procurement\(^\text{150}\). For example, the TPP covers basic, yet comprehensive, rules for creating a level playing field when state-owned companies compete with private ones.


Figure 15: RCEP - TPP

China has grown to be a major business and economic partner for Africa. Since 2000, China has emerged as Africa’s largest trading partner and a major source of investment finance as well. The China Africa Development Fund (CAD Fund) has, since its establishment in 2007, invested in 88 projects in 37 African countries with a total of USD 4 billion as of the end

\(^\text{149}\) China Daily, http://www.chinadaily.com.cn/business/2017-02/08/content_28135604.htm \\
\(^\text{150}\) OECD, Economic Outlook for Southeast Asia, China and India 2017: Addressing energy challenges.
China has become a strategic business and economic partner for Africa. Since 2000, China has emerged as Africa’s largest trading partner and a major source of investment. China and Africa traded goods worth over USD 210 billion in 2014, and over half China’s foreign aid is distributed in Africa. Africa’s exports to China dropped by almost 40% in 2015 due to lower energy and mineral export revenues. At least 2,500 large and medium-sized Chinese companies are estimated to be registered to operate in the extractive sector with a view to securing longer-term strategic supplies. This is sometimes characterised as the ‘Angola model’ — a top trading partner in Africa exporting close to 50% of its crude oil to China (2014). Chinese investments are also taking place in Copperbelt countries such as Zambia, the Democratic Republic of Congo and Congo (Brazzaville). Large numbers of Chinese workers and entrepreneurs have moved to Africa in recent years, with estimates running as high as one million.

On 29 July 2016, China and African countries held a Coordinators’ Meeting on the Implementation of the Action Plan (2016-2018) of the Forum on China-Africa Cooperation (FOCAC) at which the two sides signed 63 different types of cooperation agreement, worth about USD 18.287 billion, of which the volume of commercial loans and FDI in Africa by Chinese financial institutions and businesses was about USD 16.228 billion, making up 88.74%. In January 2017, Foreign Minister Wang visited Madagascar, Zambia, Tanzania, the Republic of Congo, and Nigeria.

In October 2014, 22 Asian countries signed a Memorandum of Understanding (MOU) to establish the Asian Infrastructure Investment Bank (AIIB). China is a founding member of the new AIIB, which was formally set up on 25 December 2015, with its headquarters in China. So far 34 founding countries hold over 74% of shares in the bank and have ratified the AIIB agreement. In total, 57 countries, including 13 EU Member States, have signed for membership of the AIIB, including 14 G20 nations. However, the US is not an AIIB member. The AIIB’s Articles of Agreement create two classes of membership: regional members, which hold 75% of the total voting power, and non-regional members. China’s voting share (28.7%) is substantially larger than the second-largest AIIB member, India, which holds (8.3%). The AIIB may pose a challenge to the World Bank and International Monetary

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155. FOCAC, Over 100 Ministerial Officials Gathered in Beijing, 25.08.2016: http://www.focac.org/eng/
156. China hopes Africa to boost confidence, unite to meet various challenges, 13.01.2017 http://www.focac.org/eng/nt/1_1_2_2_1/1430240.htm
159. CRS Report, Asian Infrastructure Investment Bank (AIIB), February 2017.
The ‘One Belt, One Road’ initiative is put at risk by the on-going fighting and terror attacks.

In 2017 China holds the rotating chair of the emerging-market bloc of BRICS. The Chinese Strategy on International Cooperation in Cyberspace sets out four basic principles for international cooperation: peace, sovereignty, shared governance and shared benefits.

Fund\textsuperscript{160}. It is seen as an alternative bank, in which China will play a dominant role in international lending to developing countries, not only for economic development, but also for the pursuit of geostrategic interests and accelerating its 'One Belt, One Road' (OBOR) initiative\textsuperscript{161} (see page 38). In 2016 the AIIB formed partnerships with some key global institutions, including the World Bank, the European Bank for Reconstruction and Development and the European Investment Bank. Three of the AIIB’s first loans were co-financed with the bank’s partners. The loans AIIB approved in 2016\textsuperscript{162} included energy, urban development and transport sectors in Pakistan, Oman, Bangladesh, Indonesia, Tajikistan, Myanmar and Azerbaijan.

In 2017 China holds the rotating chair of the emerging-market bloc of BRICS (Brazil, Russia, India, China and South Africa) and hosts its ninth summit in Xiamen in September 2017. China continues to play a key role in the BRICS-backed\textsuperscript{163} New Development Bank, which opened in Shanghai\textsuperscript{164} in July 2015, notably through a strategic cooperation agreement with China’s second-largest lender, the Construction Bank.

On 1 March 2017 the Chinese authorities released a Strategy on International Cooperation in Cyberspace (the ‘Strategy’), which sets out four basic principles for international cooperation: ‘peace, sovereignty, shared governance and shared benefits’. It also includes China’s six strategic goals including safeguarding sovereignty and security; developing a system of international rules; promoting fair internet governance; protecting the legitimate rights and interests of citizens; promoting cooperation on digital economy and building a platform for cyber culture exchange\textsuperscript{165}.

Legitimate security concerns related to cyber security should be addressed in a proportionate way, which does not create unnecessary market access barriers or deviate from WTO commitments. China’s Cybersecurity Law of November 2016 seems to contain far-reaching trade restrictions on imported ICT products and services in China\textsuperscript{166}.

\textsuperscript{160} SSRN, Why China Established the Asia Infrastructure Investment Bank: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2737888
\textsuperscript{161} https://ec.europa.eu/epsc/publications/strategic-notes/asian-infrastructure-investment-bank_en
\textsuperscript{165} 7.03.2017, http://www.lexology.com/library/detail.aspx?g=fc2ab933-7ff5-4f7d-bb5a-2e283ad5482e
4.8 China in the multilateral fora

China’s accession to the WTO in December 2001 was a major step.

Transitional arrangements were included in China’s accession protocol to take into account the legal and economic particularities of China’s transition economy. These specific arrangements have enabled WTO members, among others, to deviate from the general rules set out in the WTO Anti-dumping Agreement and the WTO agreement on Subsidies and Countervailing Measures in their relations with China.\(^{167}\)

In turn, China’s accession required the country to make bold reforms and liberalise important parts of its economy. Yet, notwithstanding some progress, a number of China’s WTO commitments to open and liberalise the Chinese economy in order to offer a more predictable environment for trade and foreign investment in accordance with WTO rules have still not been met.

According to the World Bank, notably reforms addressing excess industrial capacity, which have been initiated, remain to be completed. The Global Forum to tackle root causes of overcapacity of steel was set up in December 2016 following the commitments made at G20 level\(^{168}\) at the Hangzhou Summit in September 2016, and further talks at the OECD Steel Committee in 2016\(^{169}\). World crude steel production for the 67 countries reporting to the World Steel Association was 136.5 million tonnes (Mt) in January 2017, a 7% increase compared to January 2016\(^{170}\).

China has participated actively, notably, in the Doha Development Agenda (DDA) negotiations. China was among the first WTO members to complete national ratification of the Trade Facilitation Agreement (TFA) that was concluded at the 2013 Bali Ministerial Conference. The TFA entered into force on 22 February 2017 following its ratification by two-thirds of the WTO membership. It contains provisions for expediting the movement, release and clearance of goods, including goods in transit, and sets out measures for effective cooperation between customs and other appropriate authorities on trade facilitation and customs compliance issues\(^{172}\). Nevertheless, in 2016, the G20 countries have taken more trade-restrictive measures than trade-facilitating ones\(^{173}\).

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\(^{167}\) A possibility of treating China as a non-market economy (NME) stems from Section 15 of China’s accession protocol to the WTO, [https://www.wto.org/english/thewto_e/acc_e/completeacc_e.htm#chn](https://www.wto.org/english/thewto_e/acc_e/completeacc_e.htm#chn)


\(^{171}\) WTO, [https://www.wto.org/english/tratop_e/tradfa_e/tradfa_e.htm](https://www.wto.org/english/tratop_e/tradfa_e/tradfa_e.htm)

\(^{172}\) MOFCOM Department of WTO Affairs Interprets Items of the Trade Facilitation Agreement, March 10, 2017

China remains an observer to the WTO **Plurilateral Agreement on Government Procurement** (GPA), but continues to negotiate its accession thereto.

5 China’s external economic relations

China's foreign policy and domestic development are interlinked. Foreign policy remains largely an instrument to underpin domestic development, serving the **overarching goal of the Communist Party to remain in power and maintain stability** by delivering economic growth. But the new generation of leaders, under President Xi's dominant rule, is more ambitious and assertive, following the slogan 'lie low and bide its time' but seeking to regain its rightful place in the world. As result of globalisation, an acknowledgment is being made of the growing global responsibilities and obligations which come with 'major country' status, including the chairmanship of the G20 in 2016.

China’s 'One Belt One Road' (OBOR) economic diplomacy initiative is the foremost example of Beijing’s re-energised, ambitious and refocused ‘Go Global strategy’. It aims to improve connectivity and infrastructure along the three main routes linking China with the Baltic Sea, the Persian Gulf and the Indian Ocean; to strengthen its **energy security** and diversify supplies; to provide access to **additional export markets** and help solve China’s **overcapacity problems**; and to promote the development of its western regions, particularly Xinjiang, where Beijing’s believe that improved economic development and better living standards could eventually eradicate discontent and reduce the ‘terrorist threat’ from ethnic Uighur nationalists. Despite some investments in infrastructure in 2016 (see ‘OBOR’ funding page 29), China expects other countries to take part in the elaboration of the OBOR.

**Figure 16:**
'OBOR' initiative
'The road refers to ancient maritime routes between China and Europe, while the belt describes the Silk Road’s better-known trails overland (see map)'.


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174 The G20, China: Calculations done by POLDEP, exchange rate: 1 EUR=1.1095 USD (average 2015)
China espouses a ‘new type of international relations’, and emphasise the leading role of the UN, including Security Council resolutions.

UNCLOS ruled against China in the South China Sea dispute.

In 2017, China is pushing the coastal states of the South China Sea to establish a new ‘cooperation mechanism’.

China continues to underline peaceful, non-hegemonic and non-expansionist intentions, and its foreign policy has been assuming a more confident, multidimensional stance. China espouses a ‘new type of international relations’, based on win-win cooperation, and emphasising the leading role of the UN, including Security Council resolutions.

But some aspects of this new policy are sometimes at odds with increased assertiveness, which, combined with Beijing’s desire to construct a stronger, rejuvenated China — politically as well as economically — and to reclaim what China sees as its rightful place combine to make an assertive foreign policy, particularly in the North and South East Asian region.

The UN Permanent Court of Arbitration for the UN Convention on the law of the Sea (UNCLOS) ruled on 12 July 2016\(^\text{176}\) that China’s claim to ‘indisputable sovereignty since ancient times’ in the South China Sea was not based on evidence under international law. This ruling was on a case filed by the Philippines against the People’s Republic of China. The judges ruled that the specific portion of the South China Sea claimed by both China and the Philippines belongs to the Philippines alone. The EU supports the swift conclusion of an effective Code of Conduct between ASEAN and China implementing the 2002 Declaration on the Conduct of Parties in the South China Sea.

In 2017, China is pushing the coastal states of the South China Sea to establish a new ‘cooperation mechanism’\(^\text{177}\), which according to Vice Foreign Minister Liu would be ‘complementary’ to existing regional relationships, such as ASEAN and multilateral fora between China and ASEAN, including the 2002 Declaration of the Conduce of Parties in the South China Sea (DOC). A first draft of a Code of Conduct (COC) on the South China Sea was issued by ASEAN and China\(^\text{178}\) but no clear progress was made. Some see the negotiations as never-ending given that the idea for a COC came up 21 years ago and the DOC was signed 15 years ago.

In this context, reference should be made to the white paper outlining priorities for ‘China’s Policies on Asia-Pacific Security Cooperation’, which China’s Foreign Ministry released in January 2017\(^\text{179}\). The white paper outlines a vision to improve the existing regional multilateral mechanisms and strengthen the framework for supporting peace, security and stability in the Asia-Pacific region.

\(^{176}\) Permanent Court of Arbitration, Press release, 12.6.2016, [https://www.pcacases.com/web/sendAttach/1801](https://www.pcacases.com/web/sendAttach/1801)


China is involved in another dispute, in the East China Sea, which complicates its relations with Japan. China has also halted imports of North Korean coal until the end of 2017.

China is increasingly involved in Central Asia because of security concerns, which also relate to part of its own territory. Security plays an increasingly important role in China's policy towards Central Asia, given concerns regarding possible Muslim radicalisation in the region (including links with the so-called Islamic State (IS) group (or Da'esh), potential spill-over of radical elements in restive Xinjiang or negative influence over groups like the East Turkestan Islamic Movement (ETIM).

China considers the Shanghai Cooperation Organisation (SCO) as a primary instrument for consultations to reinforce Central Asian security, while emphasising economic ties and using the organisation to promote its new regional connectivity initiatives, such as the ‘OBOR’. In June 2016 President Xi Jinping attended the 16th Meeting of the Council of the Heads of State of the SCO, when the leaders signed the Tashkent Declaration on the 15th Anniversary of the SCO, approved the Action Plan for 2016-2020 on Implementation of the SCO Development Strategy Towards 2025, and adopted the Memorandums of the Obligations on the Entry of the Republic of India and the Islamic Republic of Pakistan to the SCO.

North Korea’s latest launch of a ballistic missile into the Sea of Japan on 5 April 2017 occurred just ahead of the summit between President Trump and Chinese President Xi Jinping on 6-7 April 2017. It remains to be seen whether the US policy of ‘strategic patience’ with North Korea has ended.

China’s announcement in February 2017 that it was halting its imports of North Korean coal until the end of 2017, in compliance with the UN.
During President Xi Jinping’s three-day visit to Finland it was made clear that no one has an interest in a trade war and economic globalisation is in the fundamental interests of all.

China is not directly affected by the Syrian conflict but it does have economic and security interests in stability in the Middle East.

Security Council resolutions, may make a difference, since about 85% of North Korea’s external trade is with China.

China, fearing a rapid escalation of tension on the Korean peninsula, has called on North Korea to stop its nuclear and missile tests and on South Korea and the United States to stop joint military drills and seek consultations instead. North Korea’s latest launch of a ballistic missile into the Sea of Japan on 5 April 2017 came just ahead of the summit between President Trump and Chinese President Xi Jinping on 6-7 April 2017.

During Chinese President Xi Jinping’s three-day visit to Finland, on a stop-over on the way to the US in April 2017, the two heads of state shared concerns, notably on the negative effects on the global economy caused by any kind of trade war or protectionism, as well as rising populism. The two heads of state also discussed the North Korea situation, including the latest test-fire of a ballistic missile on 5 April 2017. In the economic and trade sector, due to flagging international trade and uncertainty of the global economic recovery, it was noted that the bilateral trade volume between Finland and China stood only at USD 5.27 billion from January to October in 2016, marking a decrease of 11.9% from the same period of 2015.

In January 2016 the diplomatic engagement of China was partly due to the realisation that China has economic and security interests in stability in the Middle East region. Not only because Iraq is among its main oil suppliers, but is also due to the on-going fighting and terror attacks that are putting at risk the ‘OBOR’, or so called Silk Road initiative and mega project worth USD 900 billion that aims to connect China/Asia, the Middle East, Africa, and Europe through a wide-ranging infrastructure network.

Moreover, China is worried that Uighurs, a mostly Muslim people from western China’s Xinjiang region, have ended up in Syria and Iraq fighting for militant groups there, having travelled illegally via Southeast Asia and Turkey. According to an August 2015 UNHCR fact sheet, the Chinese government does not provide assistance to refugees in China.

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188 [http://english.cctv.com/2017/04/04/ARTI3ndE0Iw5Y9v3TZP8EH3170404.shtml](http://english.cctv.com/2017/04/04/ARTI3ndE0Iw5Y9v3TZP8EH3170404.shtml)
189 Joint Declaration between the People’s Republic of China and the Republic of Finland on Establishing and Promoting the Future-oriented New-type Cooperative Partnership, [http://english.cctv.com/2017/04/04/ARTI3ndE0Iw5Y9v3TZP8EH3170404.shtml](http://english.cctv.com/2017/04/04/ARTI3ndE0Iw5Y9v3TZP8EH3170404.shtml)
190 FT, Finland urges US and China to compromise to avert trade war, 6.04.2017, [www.ft.com](http://www.ft.com)
191 [http://english.cctv.com/2017/04/04/ARTI3ndE0Iw5Y9v3TZP8EH3170404.shtml](http://english.cctv.com/2017/04/04/ARTI3ndE0Iw5Y9v3TZP8EH3170404.shtml)
6 The EU and China

6.1 Overview

Relations between the EU and China have developed in a number of different areas, which are set out in the EU-China 2020 Agenda for Cooperation.

It was clear at the last EU-China Summit that the relationship is experiencing some difficulties.

The EU’s engagement with China is principled, practical and pragmatic. The EU expects China to assume responsibilities in line with its global impact and to support the rules-based international order from which it, too, benefits. The promotion of human rights and the rule of law will continue to be a core part of the EU’s engagement with China in accordance with the EU Strategy on China.196

The EU-China relationship has developed significantly. Besides of the annual summits, more than 60 high level dialogues reflect the wide-ranging scope of the bilateral cooperation. The Joint Communication on elements for a new EU strategy on China197 was adopted by the High Representative and the European Commission on 22 June 2016 (see chapter 6.2. page 45).

The EU-China 2020 Strategic Agenda for Cooperation198, a top-level joint document adopted in 2013199, guides the EU-China Comprehensive Strategic Partnership. It sets out cooperation in the areas of peace, prosperity, sustainable development and people-to-people exchanges.

The 7th EU-China Strategic Dialogue200 took place on 19 April 2017. The exchange of views covered various bilateral issues as well as elements of cooperation between the EU and China on various regional and global issues in view to prepare the upcoming EU-China Summit in June 2017.

While the future of China-US relations remains somewhat unclear201, there is a window of opportunity for the EU to strengthen its bilateral relationship with China. In order to maximise EU cohesion and effectiveness, dealing with such a unique strategic partner as China requires a ‘whole-of-the EU’ approach. The EU’s relationship with China should bring reciprocal benefits in both political and economic terms. In particular, a greater opening-up of the Chinese market to European business and investment is a must.

Contrary to past practice, no joint summit statement was issued at the 18th EU-China Summit in Beijing in July 2016. This is seen as confirmation of the

196 Council conclusions (18 July 2016), 11252/16
201 Financial Times, ‘Finland urges US and China to compromise to avert trade war’, 6.04.2017 https://www.ft.com/content/510d2860-1ac0-11e7-bcac-6d03d067f81f
Differences between the EU and China include the conditions for negotiating a bilateral free trade agreement and China’s market economy status.

The 18th Summit established 2017 as the EU-China ‘Blue Year’. The EU and China agreed to set up a bilateral steel ‘platform’ to address the issue of China’s overcapacity.

EU-China cooperation has intensified in recent years in areas such as: research and technological development, energy, urban development and maritime transport and aviation.

Differences between the two sides. On the one hand, the summit coincided with the announcement of the tribunal ruling on the South China Sea dispute. Therefore, China’s attention was directed towards reaffirming its position on its sovereignty over the disputed areas. On the other hand, during the summit, growing divergences between the EU and the Chinese positions were revealed on key issues relating to their bilateral commercial relations. China attempted to persuade the EU to launch negotiations on an EU-China free trade agreement (FTA) and to obtain recognition by the EU of China’s Market Economy Status (MES). No compromise was found on either of these issues at the summit.

The EU’s immediate top priorities remain the conclusion of a Comprehensive EU-China Agreement on Investment (including reciprocal market access) and an Agreement on the Protection of Geographical Indications. Broader ambitions, such as a deep and comprehensive FTA, could only be considered once these agreements have been concluded, and more ambitious reforms, such as liberalising China’s economy and reducing the role of the state-owned enterprises — creating a level playing field for domestic and foreign companies — have been implemented.

The 19th EU-China Summit is scheduled to take place on 2 June 2017 in Brussels.

The 18th Summit established 2017 as the EU-China ‘Blue Year’ and 2018 the EU-China Year of Tourism. On 2 March 2017, the third EU-China High Level Dialogue on Ocean Affairs took place in Brussels. An exchange of views with the Chinese State Oceanic Administration covered issues such as ocean governance, blue growth and international ocean developments.

Building on the results of China’s G20 presidency in 2016, the sixth annual EU-China High-level Economic and Trade Dialogue on 18 October 2016 covered a range of strategic issues, such as strengthening policy coordination, promoting sustainable growth and tackling China’s overcapacity, notably on steel. The EU and China agreed to set up a bilateral steel ‘platform’ to address the issue of China’s overcapacity. Although talks only concentrated on China’s steel production, various other EU industrial sectors are concerned by China’s overcapacity.

Other aspects of EU-China bilateral relations are progressing well, such as China’s partnership in Horizon 2020, a recent programme for research and technological development with a budget of EUR 80 billion for 2014-2020. Chinese researchers and companies can participate as equal partners and team up with European research teams. It remains to be seen whether the EU is given reciprocal access.

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Amongst the jointly identified priority areas for cooperation are food, agriculture and biotechnology, sustainable urbanisation with its different dimensions of energy, environment, transport, ICT and social sciences and humanities, and aviation. On 29 June 2016, the EU and China endorsed the Connectivity Platform’s work plan and objectives. The Platform is raising mutual understanding of European and Chinese transport policies; exploring synergies on financing and infrastructure plans with a view to ensuring smooth transport operations between the two continents. The EU-China Aviation Partnership Project (APP)\(^\text{206}\), managed by the European Aviation Safety Agency (EASA), links technical cooperation with policy dialogue between the European and Chinese aviation authorities, including the Civil Aviation Administration of China (CAAC).

A dedicated high level dialogue on EU-China energy cooperation\(^\text{207}\) covers notably renewable energy, smart grids and energy efficiency in the building sector, clean coal, nuclear energy and energy law. China, so far, has been the biggest single recipient of the EU’s financial and technical assistance in the field of energy and climate change.

The Urbanisation Partnership\(^\text{208}\), launched on 3 May 2012, focuses on the economic, social and environmental challenges of urbanisation in China. The EU and China are developing city twinning schemes and other mechanisms to foster exchanges of experience and joint projects in a broad range of sectors, such as low-energy buildings, integrated water and waste treatments, social inclusion, local infrastructure and efficient public services\(^\text{209}\).

The security and defence dimensions of EU-China are growing. The EU and China enjoy good practical cooperation on counter-piracy with regular contacts between the EU’s ATALANT’ mission\(^\text{210}\) and the Chinese People’s Liberation Army (PLA)-Navy. Multilateral action on security problems in the EU’s neighbourhood, such as Russia/Ukraine, Libya, Syria and the Middle East Peace Process requires foreign policy engagement with China, which is a Permanent Member of the UN Security Council. Concerns with regard to North Korea\(^\text{211}\) are an additional example. Following the United Nations Security Council resolution (UNSCR) 2321 of 30 November 2016\(^\text{212}\), the EU Council adopted further restrictive measures against North Korea on 27 February 2017 and on 6 April 2017. In the latter the EU decided to extend the ban on investments in North Korea to new sectors, namely the conventional

\(^{207}\) https://ec.europa.eu/energy/en/topics/international-cooperation/china
\(^{210}\) http://eunavfor.eu/
\(^{211}\) CNBC, 8.03.2017, China’s foreign minister calls on North Korea to halt missile tests
The ‘16+1’ initiative, set up economic and political cooperation between China and 16 Central and Eastern European countries in 2012.

The ‘16+1’ initiative, set up in 2012 for economic and political cooperation between China and 16 Central and Eastern European countries (CEE), identifies trade and investment promotion as one of its priorities in the communique of the 5th annual meeting in November 2016.

6.2 The EU strategy on China

The new EU strategy on China calls for closer cooperation with China in three main areas:

1) prosperity and reform agenda;
2) foreign policy and security;
3) global governance and the multilateral context.

A broader ambition, such as a free trade agreement, could only be considered after a comprehensive agreement on Investment is concluded.

The Joint Communication on elements for a new EU strategy on China was adopted by the High Representative and the European Commission on 22 June 2016. The EU is seeking strategic cooperation with China in three main areas: 1) prosperity and reform agenda; 2) foreign policy and security; 3) global governance and the multilateral context.

On the prosperity and reform agenda, the EU is pursuing a greater opening-up of the Chinese market to European business. The Strategy states that it dovetails with the European Commission’s Trade for All strategy and takes into account the views of the European Parliament in its December 2015 resolution on the EU’s relations with China. The Strategy maps out the EU’s relationship with China for the next five years.

According to the Strategy, a Comprehensive Agreement on Investment is the EU’s immediate priority in pursuing the objective of deepening and rebalancing relations with China. The conclusion of such an agreement, as well as progress with China’s reforms towards liberalising its economy and thereby creating a level playing field for business, would open new market opportunities and allow both sides to envisage broader ambitions such as a free trade agreement.

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213 11 EU Member States (Bulgaria, Croatia, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovakia, Slovenia) and 5 Balkan countries (Albania, Bosnia and Herzegovina, FYR Macedonia, Montenegro and Serbia).
218 WTO, https://www.wto.org/english/tratop_e/scm_e/notif_e.htm
An agreement on Geographical Indications (GIs) based on the highest standards would benefit both sides.

The Agenda for Cooperation includes the digital economy, protection and enforcement of intellectual property rights (IPRs) and connectivity.

With China playing a greater role in global governance, the EU is seeking to work with it to find common solutions.

The EU attaches high priority to the rapid conclusion of an agreement with China on Geographical Indications (GIs) for the protection of food names, based on the highest international standards. As demonstrated by the 2012 agreement between China and the EU on the protection of 10 agricultural products and foodstuffs with GIs in each other’s territories — the so-called 10+10 agreement — both sides would benefit from the conclusion of an agreement on GIs based on the highest international standards of protection. The GIs create value for local communities, as they are also known to be a useful marketing tool.

The Strategy also identifies further areas of mutually beneficial cooperation, such as the digital economy, protection and enforcement of intellectual property rights (IPRs), development of the EU-China Connectivity Platform, which could be seen as one part of the EU’s contribution to the ‘One Belt One Road’ initiative (OBOR). With regard to the OBOR initiative, China should respect market rules and international norms, including public procurement. As innovation remains essential in the transformation of China’s development model, the EU aims also to ensure a level playing field, including reciprocal access to respective research and innovation programmes.

In supporting China’s reforms, the Strategy address the need to promote human rights, the rule of law and the role of civil society as well as the need to strengthen the role of the annual EU-China human rights dialogue and the EU-China Legal Affairs dialogue, launched in June 2016.

The EU Strategy on China addresses global governance issues, such as finding common solutions to global challenges (e.g. climate change and environmental challenges, migration, humanitarian crises, etc.), promoting effective multilateralism and respecting international law and universal values.

On foreign policy and security, the EU calls for China’s greater adherence to international rules and standards (e.g. respect for the UNCLOS and the peaceful resolution of the South China Sea dispute, through the ASEAN Code of Conduct) and mobilisation of resources to provide security as a global public good, for instance in Afghanistan and Syria. China is also viewed as an important contributor to ensure peace and security in the EU’s eastern and southern neighbourhood and an essential partner in meeting common goals related to disarmament, non-proliferation, counter-terrorism and cyberspace (see page 36). Bilateral cooperation seeks to create a more secure world for all, and one of the objectives is the denuclearisation of the Korean Peninsula in view to ensure stability in the region and beyond.

6.3 EU-China trade and investment relations

6.3.1 Trade in goods and services

EU-China trade in goods is worth over EUR 1.5 billion a year.

Although the EU and China have a very close economic relationship, the business climate in China for EU investment and trade is seen as challenging. The EU has concerns about the lack of reciprocity and market access as well as
The EU posted a record trade deficit with China in 2015. The EU posted a record trade deficit with China in 2015. Trade and investment relations between the EU and China should be strengthened on the basis of a shared understanding of reciprocal and mutual benefits. China’s economic reforms, notably those that are aimed at giving the market a more decisive role and levelling the playing field, are key for a deeper bilateral relations.

In 2016, the EU continues to be China's largest trading partner and China is the EU's second biggest trading partner, after the US, representing 17.7% of the total EU trade in goods. China and Europe now trade goods worth well over EUR 1.5 billion a day. Trade with China is worth a total of EUR 345 billion in terms of EU goods imports and EUR 170 billion in terms of EU goods exports. The EU continues to record a significant trade deficit with China, amounting to EUR 175 billion in 2016. The main country of origin of goods imported into the EU in 2016 remained China - 20% of all extra-EU imports.

China is one of the EU's main agriculture and food trading partners: the second for EU exports, worth EUR 11.4 million, (6.7%) and the fourth importer, worth EUR 5.1 million. Manufactures are the top traded products for both sides, representing 98% of EU imports from China, and 93% of the EU's exports, of which machinery and appliances accounted for 30.5%, transport equipment 24% and chemicals 10.4%.

Figure 17: EU trade with China

<table>
<thead>
<tr>
<th></th>
<th>Imports from China:</th>
<th>Exports to China:</th>
<th>Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Trade in goods 2016: (in billions of euro)</td>
<td>344.6</td>
<td>170.1</td>
<td>-174.5</td>
</tr>
<tr>
<td>% of EU total</td>
<td>20.2 %</td>
<td>9.7 %</td>
<td></td>
</tr>
<tr>
<td>Trade in services 2015: (in billions of euro)</td>
<td>26.4</td>
<td>37.3</td>
<td>+ 10.9</td>
</tr>
<tr>
<td>% of EU total</td>
<td>3.9 %</td>
<td>4.4 %</td>
<td></td>
</tr>
</tbody>
</table>

Source: Eurostat, DG Trade

6.3.2 Bilateral investment

The EU-China Investment Agreement

Negotiations, launched in 2013, on the EU’s first bilateral Comprehensive Agreement on Investment are the EU’s immediate top priority with a view to deepening and rebalancing relations with China. Both investment and investor protection and reciprocal market access are important aspects for the EU. The EU Member States’ Bilateral Investment Treaties (BITs) with China do not provide for investment market access.

The aim is to reach the same level of openness in China’s markets that is already available in the EU’s market. The objective is to facilitate market access by addressing both discriminatory and quantitative restrictions. Hence, an exchange of market access offers that was scheduled to take place in 2016 is

Transformation of China and global economic interdependence

crucial as early as possible. So far, 12 rounds of negotiations have taken place, the most recent one in December 2016.

The issues under negotiation include investment market access and protection; a regulatory framework for investment, including transparency, licencing and authorisation procedures; sustainable development and dispute settlement.

**Inward investment in China from Europe**

According to the EU-China Investment Monitor, Chinese foreign direct investment (FDI) activity in the EU continues to be strong. In contrast, **EU FDI transactions in China are estimated to have declined from USD 11 billion in 2015 to USD 8 billion in 2016, a drop of 23 %**. This is notably due to the sharp drop in EU Mergers and Acquisitions (M&A) activity in China from USD 1.9 billion in 2015 to USD 740 million in 2016. In 2016, Germany remained by far the top investor (USD 3.6 billion), followed by France (USD 840 million), the UK (USD 785 million), the Czech Republic (USD 614 million), Sweden (USD 255 million), the Netherlands (USD 146 million) and Italy (USD 287 million). The automotive industry dominated the EU investment in China in 2016 and semiconductors recorded growth. EU investment in chemicals and basic materials, drivers of FDIs in the past decade, decreased to lowest level since 2009\[^221\].

**Figure 18:**
**EU inward FDI flows\[^222\]**

In 2016 Chinese FDI flows into the EU reached a new record of USD 40 billion, up from USD 22 billion in 2015.

**Chinese outward investment in Europe**

Chinese FDI into Europe has risen sharply, having nearly tripled since 2011, and **in 2016 Chinese FDI flows into the EU reached a new record of USD 40 billion, up from USD 22 billion in 2015**. In 2016, Germany (USD 12 billion), the UK (USD 9 billion) and France (USD 3 billion) accounted for over two thirds or 60 % of Chinese FDI. They were followed by Finland (USD 7.4 billion) and Ireland (USD 2.5 billion).

\[^221\] DG TRADE, EU-China FDI Monitor, January 2016

\[^222\] Source: Eurostat
A multilateral system for the resolution of investment disputes — a permanent Multilateral Investment Court — is under consideration.

Figure 19:
EU outward FDI flows

Figure 21:
China’s outward FDI flows compared to US and EU-28 (in USD million)

Figure 22:
China’s inward FDI flows compared to US and EU-28 (in USD million)

Source: UNCTAD

Considering the contribution FDI makes to their respective economies, the EU and China have recognised the importance of having access to a rules-based, predictable system for resolving disputes linked to investments. However, the objective is to explore a permanent, multilateral system for the resolution of investment disputes, which could achieve greater consistency, predictability and legitimacy in this area worldwide. It is important to create a forum for a ‘neutral dispute resolution’ that is separate from the local court system, in which the state has an inherent advantage, as

223 ibid.
in the case of the existing ISDS cases — 36.4 % of them were concluded in favour of the state and 26.7 % in favour of the investor. According to UNCTAD\textsuperscript{225}, in 2016 investors initiated 62 known ISDS cases pursuant to international investment agreements.

**EU Trade Defence Instruments — China’s overcapacity**

The possibility of treating China as a non-market economy (NME) stems from Section 15 of China’s accession protocol\textsuperscript{226} to the WTO. The EU has established five criteria\textsuperscript{227} to determine whether or not a country should be considered a market economy.

From the outset, the EP has been an important actor shaping the discussions within the EU on the issue of granting MES to China and ensuring the appropriate involvement of all the stakeholders. On 12 May 2016, the EP adopted a resolution, by a large majority (546 votes to 27, with 77 abstentions), clearly opposing granting China MES ‘until China meets all five EU criteria required to qualify as a market economy... ’ In the resolution, the EP urges the EC to come forward with a WTO-compatible non-standard methodology for calculating dumping from China, which takes duly into account the state’s interference in the economy (e.g. in-built subsidisation, overcapacity, costs and prices not resulting from market forces). The EP wants to ensure that the EU’s anti-dumping instrument remains effective in addressing trade distortions that can, otherwise, seriously harm EU industry’s competitiveness as well as growth and jobs in Europe. On process, it is the EP’s view that the EU response to China’s request to be granted MES should be coordinated with other major WTO members, notably the US.

The EU lists China as a non-market economy in the EU Basic Regulation on anti-dumping (CE 1225/2009) (See Annex 1, EU Trade Defence Instruments). This entitles the European Commission, the investigating authority in the context of EU anti-dumping investigations, to use a methodology ‘not based on a strict comparison with domestic prices or costs in China’, known as the ‘analogue country method’\textsuperscript{228}.

The EU has in place an unprecedented number, totalling 39, of anti-dumping and anti-subsidy measures targeting unfair imports of steel products.

\begin{itemize}
\item The possibility of treating China as a non-market economy (NME) stems from Section 15 of China’s accession protocol to the WTO.
\item The EP has been an important actor shaping the discussions within the EU on the issue of granting MES to China.
\item The EU has in place an unprecedented number, totalling 39, of anti-dumping and anti-subsidy measures targeting unfair imports of steel products.
\end{itemize}

\textsuperscript{225} http://investmentpolicyhub.unctad.org/ISDS
\textsuperscript{226} WTO, WT/L/432, 23.11.2001
\textsuperscript{227} To be considered a ‘market economy’ for the purposes of anti-dumping investigations, a country must have a floating exchange rate, a free market, a non-intrusive government, effective business accounting standards and, lastly, a clear definition of property rights and bankruptcy laws.
\textsuperscript{228} The rationale of the analogue country method is to enable the importing member to determine the ‘normal value’ (i.e. the actual sales price of a product on the domestic market) when market economy conditions do not prevail in the market of origin. The difference between the export price and the ‘normal value’ determines the ‘dumping’ margin.
The human rights situation in China is deteriorating under Xi’s leadership. The human rights situation has been steadily deteriorating under the rule of President Xi Jinping. There is a strong contradiction between the official Chinese acknowledgement of the universality of human rights and the worsening human rights situation in the country. Another contradiction is that while the China is opening to the world it is closing down internally despite the fact that Beijing is currently a member of the UN Human Rights Council (until the end of 2019).

Human rights defenders and other civil society activists are increasingly harassed, arbitrarily arrested and tortured. In 2014 China launched an unprecedented attack on human rights lawyers. Several of them have been charged with the crime of ‘subversion of state power’, which carries a sentence of 15 years in prison. Enforced disappearances carried out abroad, charges against labour activists, and limits to freedom of expression and freedom of movement are increasing. The media and the internet are heavily controlled and censored and numerous websites and social media platforms are blocked. Journalists are obliged to pass ideology exams before receiving press cards.

The clampdown includes new restrictive legislation on security, anti-terrorism and NGOs. A new national security law was passed in July 2015. This law defines security in broad and vague terms, which include state control of the ‘ideological sphere’. A cyber security bill was also published in July 2015. It obliges internet companies to censor online content, register users’ real names and assist the authorities with surveillance. The new government directives ban foreign-owned media companies from publishing any kind of information without government approval.

China’s first Counter-Terrorism Law came into effect on 1 January 2016. It builds upon drafts previously released for public consultation, which attracted widespread international concerns, including wide-ranging provisions on telecommunications and internet services. The Chinese authorities took up a number of key EU suggestions submitted in April 2015. However, the law maintains a number of problematic provisions and introduces uncertainty for

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231 Websites blocked in China: www.blockedinchina.net
233 http://www.independent.co.uk/news/world/asia/china-set-to-ban-all-foreign-media-from-publishing-online-a6883366.html
234 China Law Translate: http://chinalawtranslate.com/%E5%8F%8D%E6%81%90%E6%80%96%E4%B8%BB%E4%B9%89%E6%83%95-%EF%BC%882015%E7%94%9F%E8%BC%89/?lang=en Source of text: http://news.xinhuanet.com/politics/2015-12/27/c_128571798.htm
down further on human rights and civil liberties. The foreign NGOs management law will curtail and control the activities of international NGOs. Tensions between the authorities and ethnic minorities have increased. The EU regularly urges China to meet its international obligations on human rights.

civil society, the media and economic operators. In particular, the definition of terrorism is vague and is considered likely to be deployed to prosecute groups or individuals who refuse to adhere to state political and socio-economic policies.

A law on the management of foreign NGO activities came into effect on 1 January 2017. The law increases the role of the Ministry of Public Security in supervising foreign NGOs and requires government permission and a burdensome registration procedure to conduct even temporary activities while also increasing official supervision of internal NGO affairs, such as personnel and finances, including restrictions to overseas funding.

According to estimates there may be between 6 000 and 10 000 foreign NGOs operating in China; many of them have so far registered as businesses. There are serious grounds for fearing that the restrictions imposed will severely hamper the work of business associations, academia, and experts undertaking economic or technical work, or active in political, social and cultural fields. The new charity law, adopted on 17 March 2016, creates a friendlier environment for charitable organisations operating in China.

The rights of people belonging to minorities, especially in Tibet and Xinjiang, are constantly violated. Xinjiang is the subject of an on-going counter-terrorism campaign and is characterised by a dangerous cycle of violence and repression. The authorities continue to arrest and mistreat peaceful Tibetan protesters. The decrease in the number of self-immolations in Tibetan areas is linked to harsher repressive measures against people accused of having a link with self-immolators, rather than being an indication of an improvement in the situation.

The EU regularly issue statements urging China to abide by its international obligations, including respect for the Universal Declaration of Human Rights. The EP has also noted, through several resolutions, the deterioration in the situation of human rights and freedoms. For many years Parliament has been attempting to highlight the issue of Tibet and keep it on the international agenda including by welcoming the Dalai Lama. The EU holds a regular dialogue on human rights with China and supports civil society activities through the European Instrument for Democracy and Human Rights (EIDHR). A Dialogue on Legal Affairs has been launched which also covers issues related to the rule of law.

236 Freedom House, Freedom in the World 2016: China
237 The Diplomat, The China-Russia NGO Crackdown, 23 February 2015
240 Amnesty International: China 2015/2016
241 Statement by the Spokesperson on the cases of several human rights defenders in China (28/01/2017);
Annex 1: (new) EU Trade Defence Instruments

The two Commission proposals\(^{243}\) regarding trade defence instruments, which both amend the same basic regulations on dumped and subsidised imports from non-EU countries, are currently being discussed. The instruments are also meant to better address trade distortion, resulting from overcapacity, notably in China. The Commission proposal regarding the new method for calculating anti-dumping duties does not address China specifically, but simply abolishes the distinction between market and non-market economies. Abandoning the ‘lesser duty rule’ for steel production would allow levying of higher import duties. The new methodology is likely to take more time and resources from European companies in terms of providing proof of dumping. The European Parliament will adopt two reports on the Commission proposals:

- **New Methodology for Trade Defence Instruments (EP Rapporteur Fjellner EPP-SWE)**
  
The new Methodology Proposal is a reaction to the expiration of protocol number 15 to China’s WTO accession on 11 December 2016. From the moment of this expiration, countries are no longer allowed to calculate their duties based on the ‘analogue-country method’ hitherto used by the EU for non-market economies. Although the Chinese expect now to be treated by others as a market economy with corresponding lower levels of anti-dumping duties, due to state influenced system the China cannot be considered a market economy.

- **Modernisation of Trade Defence Instruments (EP Rapporteur Cicu EPP-IT)**
  
According to the WTO rules, trade measures can be imposed in the case of proven dumping or subsidisation, injury to the domestic industry and a causal link between these. Trade measures are allowed to go beyond WTO rules, as is the case with the current EU anti-dumping legislation, if they lead to a less protectionist, non-discriminatory, and transparent approach. As such, the EU applies the so called ‘Lesser Duty Rule’ (LDR) which determines that the EU imposes anti-dumping or anti-subsidy measures at a level lower than the margin of dumping or subsidisation found during the investigations. The proposal aims at limiting the application of the ‘Lesser Duty Rule’ and allowing the EU to apply duties based on the actual dumping or subsidy margins. The main differences between the EU institutions and within certain EU Member States, relate to how far the EU should go regarding these limitations. The EP adopted a resolution in first reading on 16 April 2014, which allows for not applying the ‘Lesser Duty Rule’ in more cases than the Commission proposed. The Council finally adopted a compromise position on 13 December 2016 which takes a more liberal approach than that of the Commission’s. Trialogues between Parliament, Council and Commission began on 21 March 2017.

### Annex 2: Basic data

#### People and geography

<table>
<thead>
<tr>
<th>Category</th>
<th>Data</th>
<th>Source</th>
</tr>
</thead>
<tbody>
<tr>
<td>Population</td>
<td>1 371 220 000</td>
<td>World Bank (2015)</td>
</tr>
<tr>
<td>Capital city</td>
<td>Beijing 21 240 000</td>
<td>UN (2016)</td>
</tr>
<tr>
<td>Other major cities</td>
<td>Shanghai 24 484 000</td>
<td>UN (2016)</td>
</tr>
<tr>
<td></td>
<td>Chongqing 13 744 000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Guangdong 13 070 000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Tianjin 11 558 000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Shenzhen 10 828 000</td>
<td></td>
</tr>
<tr>
<td>Surface area</td>
<td>9 562 911 km²</td>
<td>World Bank (2015)</td>
</tr>
<tr>
<td>Life expectancy at birth</td>
<td>Women 77.3, Men 74.3</td>
<td>World Bank (2014)</td>
</tr>
<tr>
<td>Literacy rate</td>
<td>96.4%</td>
<td>World Bank (2015)</td>
</tr>
</tbody>
</table>

#### Rankings

<table>
<thead>
<tr>
<th>Category</th>
<th>Score/Rankings</th>
<th>Source</th>
</tr>
</thead>
<tbody>
<tr>
<td>Human development index</td>
<td>'High', 90/188</td>
<td>Human Development Index, United Nations Development Programme, 2016.</td>
</tr>
<tr>
<td>Press freedom index</td>
<td>77.66/100, 176/180</td>
<td>World Press Freedom Index, Reporters Without Borders, 2017 (0 being the best possible score and 100 the worst)</td>
</tr>
<tr>
<td>Freedom in the world</td>
<td>'Not free', 7/7, 6/7</td>
<td>Freedom in the world, Freedom House, 2017. (1 represents the most free and 7 the least.)</td>
</tr>
<tr>
<td>Corruption perceptions index</td>
<td>40/100, 79/176</td>
<td>Corruption Perceptions Index, Transparency International, 2016. (0 represents the highest level of corruption, 100 the lowest)</td>
</tr>
<tr>
<td>Global terrorism index</td>
<td>6.108/10, 23/163</td>
<td>Global Terrorism Index, Institute for Economics &amp; Peace, 2016. (0 represents the lowest impact of terrorism, 10 the highest)</td>
</tr>
</tbody>
</table>