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A new era in EU-China relations: more wide-ranging strategic cooperation?

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ABSTRACT

China is an important strategic partner for the EU, despite fundamental divergences in some areas, mostly related to state intervention and fundamental human rights. The partnership offers mutually beneficial cooperation and dialogue in areas ranging from investment and transport to human rights and cybersecurity.

China is navigating in new directions, guided by Xi Jinping's 'Thought on Socialism with Chinese Characteristics for a New Era'. Despite President Xi's repeated avowals that 'the market will have a decisive role', public ownership remains the mainstay of the Chinese economy, whereas profound reforms would be needed to tackle the root causes of overcapacity in various industrial sectors. Xi's 'Belt and Road Initiative', now also included in the Constitution, is the flagship international connectivity and infrastructure programme dominated by Chinese state-owned companies.

Overall, China's crucial, but complex transition towards more sustainable growth would eventually benefit both, China and the world as a whole. Global economic interdependence, however, makes certain spill-over effects of China's rebalancing unavoidable.

China plays a pivotal role in global governance and the rules-based international order, and this comes with responsibilities. Beijing has begun to shift away from the narrow pursuit of national aims towards a more assertive foreign and security policy, and increased financial, economic and security cooperation with a global outreach.

China is also facing domestic concerns, such as lifting millions of people out of poverty and reducing ever-growing income inequalities, deterioration in the situation of human rights and freedoms as well as endemic corruption.

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1 Key issues and developments

- The future remains undetermined due to growing global tensions, increasing protectionism and geopolitical unpredictability. This offers a prospect for **the EU and China to demonstrate their shared commitment to safeguarding rules-based multilateral trading system and to conquering protectionism, while pressing forward with free trade**, which is a powerful tool for sustainable economic growth and prosperity. Such an opportunity would be a successful conclusion of the long overdue negotiations on a **comprehensive EU-China Investment Agreement**. 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. No free trade agreement (FTA) can be considered before the conditions are right.

- President Xi Jinping has rapidly **consolidated his personal power and promoted ideological unity, pursuing the dream of a great** '**rejuvenation of China**'. In 2018, an amendment to the constitution was unanimously passed, enshrining 'Xi Jinping Thought on Socialism with Chinese Characteristics for a New Era' as one of the guiding principles of the Party, hence granting him the same exalted status as the nation's founding fathers, Mao Zedong and Deng Xiaoping. The ambition of pursuing the 'Belt and Road Initiative' (BRI), Xi Jinping's flagship, an international trade and investment project, which builds China-sponsored infrastructure and connectivity around the world, was also written into China's Constitution.

- The **human rights situation in China has been steadily deteriorating** under the rule of President Xi Jinping. There is a strong contradiction between the official Chinese declarations and the worsening human rights situation in the country.

- **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 should be playing a more decisive role. In stark contrast, however, China's master plan 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 - as global leaders - 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 'matching' 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. Xi's remarks about upholding the sanctity of the United Nations, his commitment to a multipolar world and his vision of building a community with a shared future indicates China's resolve to shoulder greater responsibilities in the global economic and political system.

- **Preventing the protection of economic and strategic interests from turning into disastrous conflicts must remain the prime objective of all, including the major economies.** China continues to be assertive in Asia, with a number of on-going territorial disputes with its neighbours. Fearing a rapid escalation of tensions on the Korean peninsula, China has called on North Korea to stop its nuclear and missile tests, as part of adopted resolutions within the UN framework. China has also steadily increased economic pressure on Pyongyang, limiting exports of oil, steel and other metals to North Korea, and has also halted imports of North Korean coal in 2017.
- **The unpredicted meeting on 26-28 March 2018 between Chinese President Xi Jinping and the North Korean leader**, Kim Jong-Un, re-engaged both sides to finding a solution for the denuclearisation of the Korean Peninsula; and working towards the normalisation of the bilateral relations. As North Korea's most important trading partner and main source of food and energy, China has leverage and influence on the regime. Beijing has continued to advocate for **the resumption of the Six Party Talks**, the multilateral framework aimed at denuclearising North Korea. The North Korean Leader made a second surprise visit to meet Chinese president on 8 May 2018, ahead of the North Korea-US summit on 12 June 2018.

2 EU - China political relations

2.1 Overview

European Union (EU)-China relations have come a long way under the strategic partnership formed in 2003.

European Union (EU)-China relations have come a long way under the comprehensive strategic partnership formed in 2003. The EU-China 2020 Strategic Agenda for Cooperation, a top-level joint document adopted in 2013, guides the comprehensive Strategic Partnership. Given the changes in both the EU and China and China's renewed emphasis on 'going global', the Joint Communication on elements for a new EU strategy on China, (adopted on 22 June 2016) is setting out the EU's own interests.

The EU expects China to assume responsibilities in line with its global impact and to support the rules-based international order.

The joint communication states that 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. 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. The EU's top priorities remain the conclusion of the **Comprehensive EU-China Agreement on Investment** (see Chapter 3.3. page 13), which would provide proper reciprocity in terms of market access, a level playing field and a reliable and more transparent regulatory environment for investors and investments. A deep and comprehensive bilateral FTA would be subject to more ambitious reforms, such as liberalising China's economy and reducing the role of

The new EU strategy on China calls for closer cooperation with China in three main areas:
- prosperity and reform agenda;
- foreign policy and security; and
- global governance and the multilateral context.

the state-owned enterprises; thus levelling the playing field for domestic and foreign companies. The EU's strategic cooperation with China covers three main areas: prosperity and reform agenda; foreign policy and security; and global governance and the multilateral context.

On the prosperity and reform agenda, the EU is pursuing a greater opening-up of the Chinese market and ensuring reciprocity and a level playing field in all aspects of its trade and investment relationship with China. The Strategy dovetails with the Commission's '**Trade for All'** strategy and takes into account the views of the European Parliament resolution on the EU's relations with China. It recalls China's WTO commitment to notify its subsidies, amongst other measures, and to **reform its state-led economy so as to give more space to market forces to address problems, such as industrial overcapacity**.

China is also viewed as an important contributor to ensure peace and security in the EU's eastern and southern neighbourhood

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 cybersecurity** (see Chapter 7.6. page 40). International security and denuclearisation of the Korean Peninsula in view to ensure stability in the region and beyond, are top on the international agenda for both the EU and China.

On global governance, the EU Strategy on China focusses on finding common solutions to global challenges (e.g. climate change and environmental challenges, migration, humanitarian crises, etc.), **promoting effective multilateralism and the rules-based international order, and respecting international law and universal values.**

In supporting China's reforms, the EU Strategy highlights the need to promote human rights, the rule of law and the role of civil society. It also underlines the need to strengthen the role of the annual EU-China human rights dialogue. The EU-China Legal Affairs dialogue, launched in June 2016, also addresses issues related to the rule of law. The Commission President Juncker in February 2018 referred to as the South China Sea dispute, and human rights in China where there are 'no unified EU positions'.

The eight EU-China Strategic Dialogue on 1 June 2018, addressed a wide range of issues in preparing for the upcoming Summit scheduled for 16 and 17 July 2018.

The eight EU-China High Level Strategic Dialogue on 1 June 2018, addressed a wide range of issues in preparing the 20th bilateral Summit that took place from 16 to 17 July 2018. EU and Chinese leaders adopted a joint summit statement, including a statement on climate change and clean energy. The latter reflects the importance of fighting climate change and multilateral cooperation on the implementation of the 2015 Paris Agreement. The Leaders reaffirmed their commitment to deepening and reinforcing the global dimension of their partnership for peace, security, economic growth and sustainable development, reform and civilisation, by comprehensively implementing the EU-China 2020 Strategic Agenda for Cooperation. The main topics on the agenda, included the

It was clear at the EU-China Summits in 2016 and 2017 that the relationship was experiencing some difficulties.

on-going EU-China Comprehensive Investment Agreement negotiations; joint engagement to reform the World Trade Organisation (WTO) as the centre of the rules-based multilateral trading system; and to forge synergies between the China's Belt and Road Initiative under the EU-China Connectivity Platform, and the EU Investment Plan (Trans-European Networks (TEN-T). Aside from the bilateral issues, foreign policy and security agenda included issues, such as the nuclear deal with Iran (JCPOA).; the situation on the Korean Peninsula; the peace process in Afghanistan; a two-state solution in the Middle East; Syrian conflict and the stabilisation of Libya; as well as cooperation on Africa. Both sides also welcomed the holding of the EU-China Human Rights Dialogue in July 2018.

Progress was made on the negotiations for an Agreement on the Cooperation on, and Protection of, Geographical Indications (GI).

At the July 2018 summit, EU and China agreed to accelerate the negotiation of the Agreement on the Cooperation on, and Protection of, **Geographical Indications** (GI) in view to conclude the negotiations, if possible, by the end of October 2018. In June 2017, progress was made on the negotiations for the GI agreement, as the EU and China agreed on the publication of one hundred GI names by both sides. This opened the process for protecting the listed GI products against imitations and usurpations and is expected to result in reciprocal trade benefits and increased consumer awareness regarding high-quality products.

Contrary to past practice, **no joint summit statement were issued at the 19th** EU and China summit that took place in June 2017 in Brussels (as was the case on the 18th EU-China Summit). At both summits, divergences between the EU and the Chinese positions were revealed on key issues, such as China's attempt 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) in the WTO. In order to address the impact on EU industry of China's overcapacity in steel, the EU and China agreed to set up a bilateral 'steel platform' in 2016, with similar objectives to those of the G20 Global Forum on Steel Excess Capacity**.** Although talks only concentrated on China's steel production, various other EU industrial sectors are concerned by China's overcapacity.

The EU and China agreed in 2016 to set up a bilateral steel 'platform' to address China's overcapacity.

The 18th EU-China Summit declared 2018 the EU-China Year of Tourism, which was launched on 19 January 2018. The first EU-China Tourism Business summit was organised in parallel. Building on the success of the 2017 EU-China Blue Year, the EU and China have concluded a Partnership Agreement on Oceans in July at the 2018 summit.

The 13th EU-China Business Summit on 16-17 July 2018, provided an opportunity for EU and Chinese leaders to exchange views with representatives of the business community on topical economic issues, such as EU-China Bilateral Investment Agreement, digital economy, climate change and sustainability, and connectivity.

EU-China trade and investment (see Chapter 3, page 12)

The EU and China are two of the biggest traders in the world: and

The EU and China are two of the biggest traders in the world: the European Union is China's biggest trading partner, while China is the EU's second largest trading partner. China has become a hub of global supply chains and is the top trading the EU is China's biggest trading partner.

partner of an estimated 120 countries or regions. Technology developments, business innovations and decreasing trade costs continue to transform global patterns of production. China is increasingly sourcing intermediate goods domestically. The shift in global value chain puts economies heavily involved in the 'Asia value chain' under competitive pressure[1]. Some EU countries were recently leading the calls for a more proactive EU approach towards China, particularly on EU policy initiatives, such as the on-going potential EU-wide investment screening mechanism.

Some of the EU's key partners, including China, Australia, Canada, India, Japan and the US have screening mechanisms to address possible risks of FDI.

On 28 May 2018, the EP International Trade Committee (INTA) adopted a draft legislative resolution on the proposal of the Commission of 13 September 2017, for a Regulation establishing a framework for screening of foreign direct investments (FDI). On 13 June 2018 the EU Council's stance was agreed on the proposed regulation, hence the negotiations between the two institutions are expected to start soon. Several of the EU's key partners, including China, Australia, Canada, India, Japan and the US have screening mechanisms to address possible risks of foreign direct investment (FDI).

EU - China : Belt and Road Initiative (BRI)

The EU does not have a unified position on the Belt and Road Initiative.

There is no unified EU policy position toward the 'Belt and Road Initiative' (BRI), and some concerns have been expressed about Beijing's 'divide and rule' approach towards the EU. A division within the EU was demonstrated in April 2018 when twenty-seven of the 28 Ambassadors of EU Member States in Beijing issued a report, which appears to have raised concerns on the China's BRI ('runs counter to the EU agenda for liberalizing trade, and pushes the balance of power in favour of subsidised Chinese companies').

An alliance known as 16+1 has sparked tension between China and the EU.

Moreover, **an alliance known as 16+1** has sparked some tension between China and the EU**.** China has signed memorandums of understanding with all 16 Central and Eastern European countries (CEEC)[2], including Bulgaria, the Czech Republic, Hungary, Poland and the three Baltic States that have agreed to align with the BRI. The 16+1 identifies trade and investment promotion as one of its priorities in the communique of the 6th annual summit on 27 November 2017 in Hungary. According to data of the China' Commerce Ministry, the trading volume between China and 16 CEE countries reached USD 67.98 billion in 2017, up 15.9 % from 2016. The 7th 16+1 summit is scheduled to take place on 6 and 7 July 2018 in Bulgaria. Chinese investment in the 16 CEEC countries exceeded USD 9 billion in 2017, while about 20 projects have been completed or are under construction, including the Hungary-Serbia railway (for which Serbia borrowed USD 297.6 million from China's Exim Bank). The European Commission is being assessing the compliance of this project with EU law, as for a potential violation of financial rules (such as the EU transparency requirements in public tenders). The construction of the Hungarian section of the railway, worth around USD 2.1

The EC is investigating a Budapest-Belgrade railway, a seminal BRI project in the region, for potentially violating financial rules (the EU transparency

[1] IMF Working Paper, Quantifying the Spill-overs from China Rebalancing, published 15 November 2016.
[2] 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).

requirements in public tenders).

billion, is expected to start in 2020, with China's Exim Bank providing 85 % credit coverage.

The BRI needs to be an open, transparent and all-inclusive initiative, which adheres to international and multilateral market rules, requirements and standards.

The ambitious 'Belt and Road Initiative', Xi Jinping's flagship state-to-state trade project that is building China-sponsored interconnected infrastructure around the world, should present **opportunities for regional productivity-enhancing value chains.** The success of projects such as the 'Belt and Road Initiative' depends on their mutual benefits, not only for China and Europe, but also for third countries involved. To this end, the BRI needs to be an open, transparent and all-inclusive initiative, which adheres to international and multilateral market rules, requirements and standards.

Wide-ranging EU-China bilateral cooperation

Beside the annual summits, more than 60 high level dialogues reflect the wide-ranging scope of the bilateral cooperation. Amongst the jointly identified priority areas for cooperation are human rights, agriculture and biotechnology, sustainable urbanisation with its different dimensions of energy, environment and climate change (see Chapter 5, page 21), transport, ICT and social sciences and humanities, and aviation.

The EU-China 'Connectivity Platform'

The EU-China 'Connectivity Platform' exchanges of information on transport policies, such as the Trans-European transport (TEN-Ts) framework and the Chinese projects under the BRI.

The EU-China 'Connectivity Platform' (set up on 29 June 2016) held its third meeting in the margins of the EU-China Summit 2018, raising mutual understanding of European and Chinese transport policies; and exploring synergies on infrastructure plans and investments projects of common interest in the transport field, such as the Trans-European transport (TEN-Ts) framework in the EU (a list of European transport infrastructure projects was presented) and the Chinese projects in Central Asia along the Belt and Road Initiative. The joint 'Connectivity Platform' aims to promote cooperation in hard and soft kinds of connectivity through interoperable maritime, land and air transport, energy and digital networks.

The maritime transport agreement of 2002 between the Commission, the EU Member States and China is another good example in this context. On 8 December 2017, the EU and China concluded negotiations for two agreements, the Bilateral Civil Aviation Safety Agreement (BASA), and the Horizontal Aviation Agreement aiming to facilitate market access and boost the competitiveness of the EU's aeronautical industry, as well as strengthen further bilateral aviation cooperation. The implementation of the 'Near-term Action Plan of the EU-China Connectivity Platform' is expected to further promote infrastructure connectivity between the EU and China.

EU-China partnership: Horizon 2020

The EU-China bilateral partnership in Horizon 2020, one of the EU's key research, innovation and technological development

Other aspects of EU-China bilateral relations are also progressing well, such as the EU-China partnership in Horizon 2020, one of the EU's key research, innovation and technological development programmes, with a budget of EUR 80 billion, for a Work Programme 2018-2020. Chinese researchers and companies can participate as equal partners and team up with European research teams. On 26 March 2018, the first call for proposals/joint projects between European and programmes, is also progressing well.

Chinese universities, research institutions and companies under the EU-China Co-funding Mechanism for Research and Innovation (CFM) was published. The Urbanisation Partnership, launched on 3 May 2012, a strategic joint EU-China research and innovation cooperation in sustainable urbanisation, is pursued with a number of joint projects under the EU's 7th Framework Programme and Horizon 2020.

EU-China: energy cooperation

A dedicated high level dialogue on EU-China energy cooperation covers notably renewable energy, smart grids and energy efficiency.

A dedicated high level dialogue on EU-China energy cooperation guided by the EU-China Roadmap on energy cooperation (2016-2020), covers notably renewable energy, smart grids and energy efficiency in the building sector, market mechanisms for environmental protection, clean coal, and nuclear energy. The Work Plan 2017-2018 of the EU-China Roadmap on Energy Cooperation was signed in the margins of the 19th EU-China Summit in June 2017. 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. According to the joint statement of 16 July 2018, the EU and China commit to significantly intensify their political, technical, economic and scientific cooperation on climate change and clean energy.

EU-China: the security and defence dimension

The security and defence dimensions of EU-China relations are growing.

The security and defence dimensions of EU-China are growing. The EU supports the establishment of regular and substantial EU dialogue with China in view to pursue greater common ground on disarmament, non-proliferation, counter-terrorism, migration, and, cyber-security through the EU-China Cyber Taskforce.

While, the EU's position on the arms embargo to China remains unchanged, China no longer use 'the practice' of making any progress on international security cooperation with Europe conditional on the lifting of the embargo.

The EU and China enjoy good practical cooperation on counter-piracy within the EU's first ever Naval Force operation, the EU's ATALANTA mission and the Chinese People's Liberation Army (PLA)-Navy. The Action Plan concerning EU-China Customs Cooperation on IPR (2018-2020) was one of the priorities of the EU-China Strategic Framework.

The EU-China Peace and Security Forum in December 2017 called to enhance concrete cooperation, notably in the Korean Peninsula (see Chapter 8.3., page 47), Africa, Middle East Peace Process, Syria, Afghanistan, and the Iran nuclear deal. Multilateral action on security problems in the EU's neighbourhood requires foreign policy engagement with China, which is a Permanent Member of the UN Security Council.

2.2 Parliamentary dimension of EU - China relations

The EP Delegation for Relations with China is closely monitoring EU-China political, economic and trade developments.

The European Parliament (EP) Delegation for Relations with China is closely monitoring political, economic and trade developments in the relationship, together with the EP committees, notably the Committees on Foreign Affairs (AFET) and International Trade (INTA).

The National People's Congress (NPC) of China suspended the regular Inter-parliamentary exchanges, in the form of Inter-parliamentary Meetings (IPMs), in mid-September 2016 when the incoming IPM was cancelled at short notice because 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 EP.

The 40th inter-parliamentary meeting (IPM) was held on 15 and 16 November 2017 in Strasbourg, after over one year suspension by Chinese side.

The 40th inter-parliamentary meeting (IPM) was held on 15 and 16 November 2017 in Strasbourg, after over one year suspension by Chinese side. The parliamentarians held lively exchanges of views about the situation on the Korean peninsula, global security issues, climate change, trade and investment, cybersecurity and the digital economy. The Chinese side also debriefed MEPs on the outcome of the 19th Communist Party Congress in October 2017.

The 41st EP-China IPM was held from 7 to 9 May 2018 in Beijing & Hangzhou (China).

The Parliament's Committee on Foreign Affairs (AFET) in association with the Committee on International Trade (INTA), and the Committee on Environment, Public Health and Food Safety (ENVI) have been finalising an own-initiative report '**on the state of EU China relations'** (2017/2274 INI) in April 2018. The vote on the draft EP resolution is scheduled for the September 2018 Plenary session.

3 EU - China trade and investment relations

3.1 Overview

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.

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 level playing field in China for foreign investors, while Chinese investments in the EU are free and flows are increasing. 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 basis for deeper bilateral relations.

3.2 Trade in goods and services

In 2017, the EU continues to be China's largest trading partner.

In 2017, the EU continues to be China's largest trading partner and China is the EU's second biggest trading partner in trade in goods, after the US. China and Europe trade goods worth well over EUR 1.5 billion a day. Trade with China is worth a total of EUR 375 billion in terms of EU goods imports and EUR 198 billion in terms of EU goods exports. The EU continues to record a significant trade deficit with China, amounting to EUR 176 billion in 2017.

Figure 1:
EU trade with China

	Imports from China:	Exports to China:	Balance
Trade in goods 2017: (EUR billions)	374.6	198.2	- 176.4
% of EU total	20.2 %	10.5 %	
Trade in services 2016: (EUR billions)	29.6	38.3	+ 8.8
% of EU total	3.9 %	4.6 %	

Source: Eurostat; DG Trade

An agreement on Geographical Indications (GIs) based on the highest standards benefits both sides.

The EU also attaches high priority to an agreement with China on Geographical Indications (GIs) for the protection of food names, based on the highest international standards. An agreement was reached at the EU-China Summit in June 2017 on the publication of 100 names on both sides. 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, both sides would benefit from the conclusion of an agreement on GIs based on the highest international standards of protection.

China continues to be a priority country for the EU in the area of protection and enforcement of Intellectual Property Rights (IPR). More than 80 % of the seizures of counterfeit and pirated goods come from China or Hong Kong.

3.3 Bilateral investment relations

Foreign direct investment (FDI) brings substantial benefits to the EU, such as growth and jobs.

Foreign direct investment (FDI) brings substantial benefits to the EU, linking EU companies with global value chains and boosts productivity, competitiveness and resource allocation, bringing also capital, technologies and expertise, and innovation, while opening new markets for EU's exports.

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.

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. The aim is to reach the same level of openness in China's market that is already available in the EU's market. The objective is to facilitate market access by addressing both discriminatory and quantitative restrictions. 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.

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

So far, 17 rounds of negotiations have taken place, the most recent one from 22 to 24 May 2018. 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. In the margin of the 20th EU-China summit a first exchange of offers on market access took place, bringing the negotiation into a new phase.

Such a comprehensive 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 pursue ambitions, such as a free trade agreement.

3.4 EU - China Foreign Direct Investment

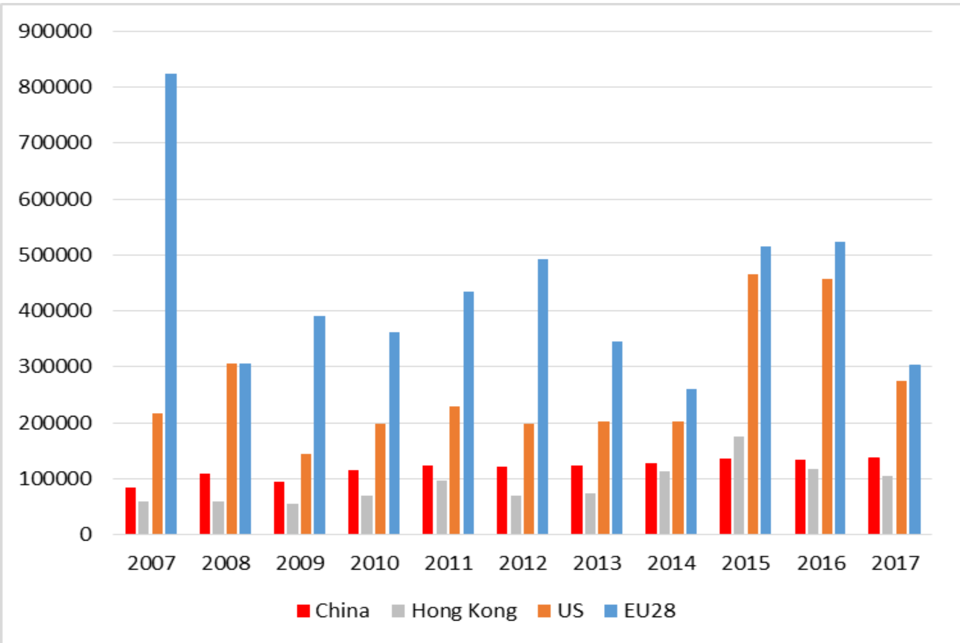
According to China's Ministry of Commerce, outbound FDI by Chinese companies dropped by 29 % in 2017.

According to the OECD, FDI flows into EU countries decreased by 45 % (from USD 531 billion recorded a year earlier to USD 290 billion in 2017). China, the second largest investor globally in 2016, was out of the top five, as its outflows decreased by about a half from USD 217 billion to USD 102 billion in 2017. China's outward FDI positions represent 12.3 % of the GDP in 2017.

FDIs between China and the EU

Chinese foreign direct investment (FDI) activity in the EU fell 17 % compared to 2016, worth to EUR 30 billion in 2017. The EU FDI transactions in China also fell from EUR 8 billion to around EUR 6 billion in 2017.

Figure 2: China's inward FDI flows compared to US and EU-28 (in USD million)



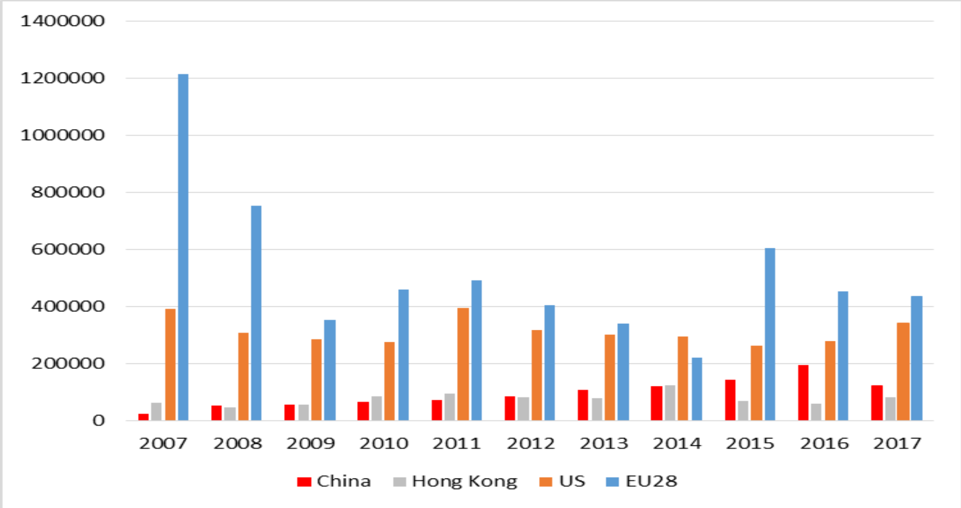
Source: UNCTAD, World Investment Report 2018

Chinese outward investment in Europe

Foreign direct investment (FDI) in Europe from China hit a record 65 billion euros (USD 79 billion) in 2017, thanks largely to ChemChina's takeover of agribusiness company Syngenta for USD 43 billion in Switzerland in May 2017. Without that deal, Chinese FDI into Europe would have fallen by 22 %, to around USD 38 billion, according to Chinese authorities. In 2017, EU countries experienced large declines in Chinese FDI, such as Germany, Spain, and France, with declines of 84 %, 79 %, and 58 %, respectively.

The tightening of controls by the Chinese authorities as well as some EU member states effectively explains the unusual number of investment operations cancelled during the first half of 2016 and the beginning of the year 2017.

Figure 3: China's outward FDI flows compared to US and EU-28 (in USD million)



Source: UNCTAD, World Investment Report 2018

Multilateral Investment Court System

The EU and China have recognised the importance of having access to a rules-based, predictable system for resolving disputes linked to investments.

Considering the contribution that 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.

A permanent, multilateral system for the resolution of investment disputes could achieve greater consistency, predictability and legitimacy in this area worldwide. A 'neutral dispute resolution' that is separate from the local court system, in which the state may have an inherent advantage, is considered important in the light 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, 65 arbitrations were initiated in 2017. In total China is respondent state in 3 cases and as claimant state in five cases pursuant to international investment agreements. Four of these five cases were decided in favour of the state. The case Hela Schwarz GmbH v. China (ICSID Case No. ARB/17/19), initiated in 2017 on the basis of China - Germany BIT (2003), is still pending.

A multilateral system for the resolution of investment disputes — a permanent Multilateral Investment Court — is under consideration.

A way forward, with more flexibility and over a longer-term, could be the Commission's proposal of September 2017 for a Multilateral Investment Court system, which is currently being reflected on within the EU. On 20 March 2018, the Council adopted the negotiating directives authorising the Commission to negotiate for a Convention establishing a multilateral court for the settlement of investment disputes.

3.5 Trade defence instruments and anti-dumping

The revised trade defence instruments rules are expected to enter into force by the end of May 2018.

On 5 December 2017, the Parliament and Council reached an agreement on the Commission's proposal on trade defence instruments (TDIs) of the EU i.e. anti-dumping and anti-subsidy measures. The aim of this modernisation is to ensure the continued effectiveness of the EU's TDI in the face of new global challenges, for instance various global overcapacities in products like steel and aluminium.

Following the adoption by the Council on 16 April 2018, these new rules entered into force as of 8 June 2018.

The EU's new methodology for calculating anti-dumping and anti-subsidy margin for imports coming from 3rd countries entered into force on in December 2017.

On 3 October 2017, the European Parliament and the Council reached agreement on the Commission's proposal on the new methodology for calculating anti-dumping and anti-subsidy margin for imports coming from countries where there are significant market distortions or where the state has a pervasive influence over the economy. The revised legislation entered into force on 20 December 2017, and the new methodology can apply to any WTO member.

Given that investigations and measures against China account for the largest proportion of the EU's anti-dumping investigations and trade defence measures, the Commission published a report on state induced distortions existing in China 20 December 2017. In 2017, the EC initiated three new anti-dumping investigations and two anti-subsidy investigations against products originating from China.

WTO complaint by China against the 'old' EU current methodology

The final report of the WTO Panel on China's case against EU on 'Price Comparison Methodologies' is not expected before the second half of 2018.

The old methodology, was the subject of a complaint launched at the WTO by China against the EU on 12 December 2016 (WT/DS516: EU — Price Comparison Methodologies). China objects to certain provisions of the EU regulation pertaining to the determination of normal value for 'non-market economy' countries in anti-dumping proceedings involving products from China.

In line with the China's Accession Protocol to the WTO (subparagraph 15 (a) (ii)), China considers that it should be treated as a market economy country. Countries that have expressed their third-party rights to the WTO panel composed on 10 July 2017 are Australia; Bahrain; Canada; Colombia; Ecuador; India; Indonesia; Japan; Kazakhstan; Republic of Korea; Mexico; Norway; Russia; Chinese Taipei; Turkey; United Arab Emirates; and the United States.

In its request, China indicates that the complaint should target especially the provisions for price comparison methodology, but that the request should also concerns 'any modification, replacement or amendment to the measure identified above, and any closely connected, subsequent measures'. The WTO Panel is expected to issue its final report during the second half of 2018. In the meantime, the EU legislation was modified and this old methodologies has been repelled, which diminish the importance of the WTO case.

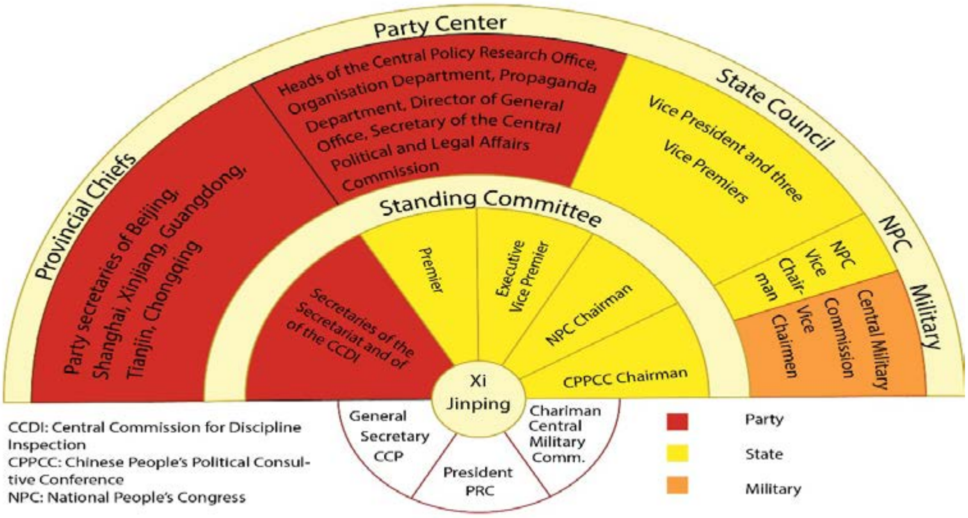
4 Recent political developments in China

4.1 Overview

President Xi Jinping's new leadership team was unveiled at the Communist Party's 19th national congress, in October 2017.

The new composition of the Communist Party's top decision-making body, the Politburo Standing Committee, was unveiled on 25 October 2017, at the end of the 19th National Congress of the Communist Party of China (CPC), held from 18 to 24 October 2017 in Beijing. Five of the seven members of the Standing Committee had reached the 'unofficial' retirement age of 68 years applied according to an 'unwritten' rule since 2002. The new members, along with the reconfirmed President Xi Jinping and Premier Li Keqiang, are Han Zheng, Wang Huning, Li Zhanshu, Wang Yang and Zhao Leji. The 25-member Politburo includes the seven members of the Standing Committee.

Figure 4:
China's political apparatus (2018)



Sources: © European Parliament, DG Expo Policy Dept., 2017, AS/GM, based on Merics Institue illustration of Politburo of 18th Central Committee in 2013

President Xi Jinping is promoting the 'rejuvenation of China'.

President Xi, **elevated to 'core' leader at the 18th** Central Committee of the CPC in 2016, has rapidly **consolidated considerable amounts of personal power** and promoted ideological unity, pursuing the dream of a great 'rejuvenation of China'.

He has secured the same exalted status, under the constitution, as the nation's founding father Mao.

The 19th National Congress of the Communist Party of China (CPC) in October 2017 unanimously passed an amendment to the Constitution to include '**Xi Jinping Thought on Socialism with Chinese Characteristics for a New Era**' as one of its guiding principles, hence granting him the same exalted status as the nation's founding father, Mao Zedong and Deng Xiaoping.

The Belt and Road Initiative is also written into the Chinese constitution.

The ambition of **pursuing the Belt and Road Initiative' (BRI),** Xi Jinping's flagship state-to-state trade project that is building China-sponsored interconnected infrastructure and other links around the world, was also written into China's Constitution at the CPC's 19th National Congress.

China's economic diplomacy entered a new era in 2017, when Xi Jinping, attended the World Economic Forum in Davos, as the first Chinese president to do so.

Xi is seeking to restore China's powerful role in the world and in global governance.

President Xi Jinping is seeking to restore China's powerful role in the world and in global governance. In his opening address to the 19th national congress, which lasted over three hours, he outlined the 14 basic policy points that underpin the Party's endeavours for the next five years (and beyond), with a view to 'securing the success of socialism with Chinese characteristics for a new era'.

He also mapped out a two-stage, longer-term future plan for China's rise on the global stage.

He also mapped out a two-stage, longer-term future plan for China's rise on the global stage. He predicted that China would become 'a global leader in innovation' during the first stage from 2020 to 2035. In the second stage from 2035 to 2050, the country would 'become a global leader in terms of composite national strength and international influence'. According to President Xi, major developments are irreversible, such as changes in the global governance system and the international order; the interconnected and interdependent global economy; the widening gap between rich and poor; and increasing unconventional security threats, such as terrorism and cyber-insecurity.

Foreign trade and investment

President Xi promised that China would ‘significantly ease market access, further open the service sector, and protect the legitimate rights and interests of foreign investors’.

At the 19th CPC, President Xi emphasised the importance of foreign trade, new models and new forms of trade, and policies to promote high-standard liberalisation, and facilitation of trade and investment. He promised that China ‘will implement the system of pre-establishment national treatment', with nationwide implementation of a 'negative list' of foreign investment, which is was released at the end of June 2018. He also undertook to treat equally all businesses registered in China, as well as to significantly ease market access, further open the service sector, and protect the legitimate rights and interests of foreign investors.

On 10 April 2018, President Xi Jinping in his speech at the 17th annual Boao Forum for Asia, promised (again) to open up China’s economy, including the reduction of car tariffs, strengthening the protection of intellectual property, opening up of various service sectors to foreign investment and increasing imports. These announcements are not new, hence China, for its own credibility, needs to make a shift and effectively tackle the opening up of its economy (and levelling the playing field) that it has long promised.

The 'Belt and Road Initiative', now enshrined in the Constitution, is a priority for Xi in opening up China further.

The renamed **'Belt and Road Initiative' (BRI)**, enshrined in China’s Constitution at the 19th CPC, is a priority for President Xi Jinping. In his speech to the 19th CPC, called on China to pursue the Belt and Road Initiative as a priority and to give equal emphasis to 'bringing in and going global', and ‘hoping to make new ground in opening China further through links running eastward and westward, across land and over sea’, with the aim to build a global trade, investment and infrastructure network.

Hong Kong and Macao, special administrative regions and Taiwan

On Hong Kong and Macao, Xi insists that China is upholding the principle of 'one country, two systems'.

At the 19th national congress, President Xi acknowledged progress in work related to **Hong Kong and Macao**, **'upholding the one-China' policy**, while asserting that the principle of 'one country, two systems' must continue to be upheld.

Hong Kong’s pro-democracy party won two out of four seats in March 2018 Legislative Council by-election, shedding light upon political divisions, as a high-profile candidate (Agnes Chow) was barred from standing, because her party promotes self-determination for the semi-autonomous city. This comes as China has taken an increasingly tough line against any attempt to undermine its ‘One China’ policy. The Hong Kong legislature now consists of 26 pro-democracy and 42 pro-Beijing candidates.

China resolutely opposes and deters separatist elements advocating 'Taiwan independence'.

Regarding **Taiwan**— whose government China does not recognise — Xi referred to China's response as ‘appropriate to the political developments in Taiwan’. He resolutely opposed and deterred separatist elements advocating 'Taiwan independence’. He also underlined the importance of safeguarding peace and stability in the Taiwan Straits, stating that China would never allow anyone 'to separate any part of Chinese territory from China'. As part of the plan, Chinese nationalism is growing and the **'Chinese Dream'**, a vision of a powerful military, a 'world-class force under the Party's command' is being realised. In March 2018, Foreign Minister Wang Yi reminded the international community that there was only one China and Taiwan was an inalienable part of it.

Tensions have risen between China and Taiwan since Tsai Ing-wen was elected president of Taiwan in 2016.

Tensions have risen between China and Taiwan since Tsai Ing-wen was elected president of Taiwan in 2016, bringing the Democratic Progressive Party (DPP) back to power for the first time since 2008. China has stressed that Taiwan must accept the so-called '1992 Consensus', which holds that China and Taiwan are part of 'one China', but allows for different interpretations.

The 'Taiwan' issue has emerged one of the most crucial issues for China ever since it was founded as a country, largely thanks to a 'behavioural style' by the US.

The **'Taiwan'** issue has recently emerged one of the most crucial issues for China, largely thanks to a 'behavioural style' by the US. China views it is as an integral territory, requiring respect of the 'One China' principle. The US' 'Taiwan Travel Act' of March 2018 recognises Taiwan as a 'beacon of democracy in Asia', and encourages visits between officials from the US and Taiwan at all levels.

China has also prevented the World Health Organization and International Civil Aviation Organization from inviting Taiwan. Another example is that Panama severed its diplomatic relations with Taiwan and established them with China for the first time in June 2017.

On 22 March 2018 Taiwan and the EU held their first Human Rights consultations.

Fight against corruption

Xi is waging a tough war on corruption and exercising full and rigorous governance over the Party.

In domestic affairs, Xi further warned at the 19th national congress, that **corruption remained the greatest threat to the party's survival** despite a five-year war on graft that he claimed had been 'built into a crushing tide'. **Xi continues to wage a tough war on corruption and is exercising strict Party governance after the 19th CPC National Congress.** Under the 2016 **Disciplinary Code of the Chinese Communist Party** — said to be the harshest disciplinary code since the time of Mao — the CPC Central Commission for Discipline Inspection (CCDI) is responsible for the supervision and inspection of the implementation of the Party's line, principles, policies and resolutions, in compliance with China's laws and regulations. In 2017, the CCDI disciplined a total of 159 100 people (compared to 415 000 people in 2016) for violating the Party's code of conduct and corruption in China.

4.2 Parliamentary dimension - the 13th NPC

The National People's Congress (NPC) held its annual meeting from 5 to 18 March 2018.

China's unelected legislature, the National People's Congress of the People's Republic of China (NPC), held its 13th annual session from 5 to 18 March 2018. **The NPC passes major bills, approves the budget and endorses appointments**. In 2018, the NPC approved constitutional changes abolishing the maximum two consecutive term limits for China's president, while also confirming President Xi Jinping's re-election. This could allow President Xi Jinping to remain in power after 2023.

The vision of 'Xi Jinping Thought on Socialism with Chinese Characteristics for a New Era' was also enshrined in the constitution's preamble, following Marxism-Leninism, Mao Zedong 'Thought', and Deng Xiaoping 'Theory'.

The inclusion of President Jinping's Belt and Road Initiative in the Constitution further cements Xi's command of Chinese society and history.

The inclusion of President Jinping's Belt and Road Initiative in the Constitution as adopted in October 2017, further cements Xi Jinping's command into Chinese society and history, as well as adding a political edge to what was previously viewed as a solely economic initiative.

The 13th NPC also approved an institutional reshuffle of central government to lessen bureaucratic disorder and reinforce Xi's *entourage*. The restructuring scrapped eight ministries and merged the banking and insurance commissions to transfer more of their roles to the central bank.

President Xi Jinping is also offering a 'new type of political party system' for the development of political parties around the world.

President Xi Jinping is also offering a 'new type of political party system' — a Chinese solution that contributes to the development of political parties around the world. The eight so-called democratic parties are allowed to participate in the political system, (deputies in the NPC or members of the National Committee of the CPPCC), but they are almost completely subservient to the Communist Party of China

Figure 5: Overview of the so-called democratic political parties

Name	Date of foundation	Composition
Revolutionary Committee of the Chinese Kuomintang (RCCK)	1948 (Hong Kong)	
China Democratic League (CDL)	1941	mainly consists of intellectuals working in the fields of culture, education, science, and technology
China National Democratic Construction Association (CNDCA)	1945	mainly consists of patriotic industrialists, business people, and intellectuals
China Association for Promoting Democracy (CAPD)	1945	mainly consists of intellectuals working in the fields of culture, education, publishing, and science
Chinese Peasants and Workers Democratic Party (CPWDP)	1930	mainly consists of intellectuals in the fields of health care, population resources, and ecological protection
China Zhi Gong Party	1925	mainly consists of overseas Chinese who have returned to the mainland, relatives of nationals living abroad as well as those with close connections with overseas Chinese
Jiusan Society	1945	mainly consists of senior and mid-level intellectuals engaged in science, technology, culture, education, medical and health work
Taiwan Democratic Self-Government League	1947	mainly consists of Taiwanese living in the mainland

Source: Global Times, 07.03.2018

5 Environment and climate change

President Xi's New Year speech in 2018 focussed on internal affairs but referred to China's international obligations, for example on climate change.

President Xi's New Year 2018 speech focussed on internal affairs, including improving the livelihoods of the Chinese people, with the concrete target of lifting all people out of poverty by 2020. His speech indicated that China would strive for relevance in global affairs through the United Nations, and assume greater responsibilities in the global economic and political system by fulfilling China's international obligations and duties in a multipolar world, such as those related to climate change and world peace.

Greater focus has recently been placed on environmental concerns in China. At the 19th CPC Xi pledged to build a 'Beautiful China' with a clean environment, high-tech companies and responsive government.

The Five Year Plan on Energy Development 2016-2020 sets targets for 2020 compared with the situation in 2015.

On 5 January 2017, China's 13th Five Year Plan on Energy Development 2016-2020 (Energy 13FYP) was unveiled. It sets targets for 2020 compared with the situation in 2015, covering total energy consumption target, reduction of the use of coal; increasing wind energy capacity; and promotion of energy savings and green development, as well as **setting up a carbon emission trading market** in China. In December 2018, China announced that its carbon cap-and-trade scheme initially involved only the power generation sector, instead of the initially announced eight biggest industries (electricity, chemicals, petrochemicals, construction, steel, nonferrous metals, paper and aviation). However, China has one of the world's largest emissions trading systems, bigger than the equivalent EU Emissions Trading System (ETS), and it covers over 1 700 companies and an estimated 4 billion metric tons of emissions. The EU and China signed a Memorandum of Understanding to Enhance Cooperation on Emissions Trading in July 2018.

The Environmental Protection Law (EPL) entered into force on 1 January 2015.

The Environmental Protection Law (EPL), the country's most progressive and stringent so far, entered into force on 1 January 2015. It tightened controls on local environmental enforcement, and major environmentally-risky industrial projects. The State Council has detailed rules for enforcement of the Environment Protection Tax law, which took effect on 1 January 2018, when China started collecting an environment tax.

A coalition of the EU, China and Canada plays an important role following the US decision in June 2017 to pull out of the Paris Agreement.

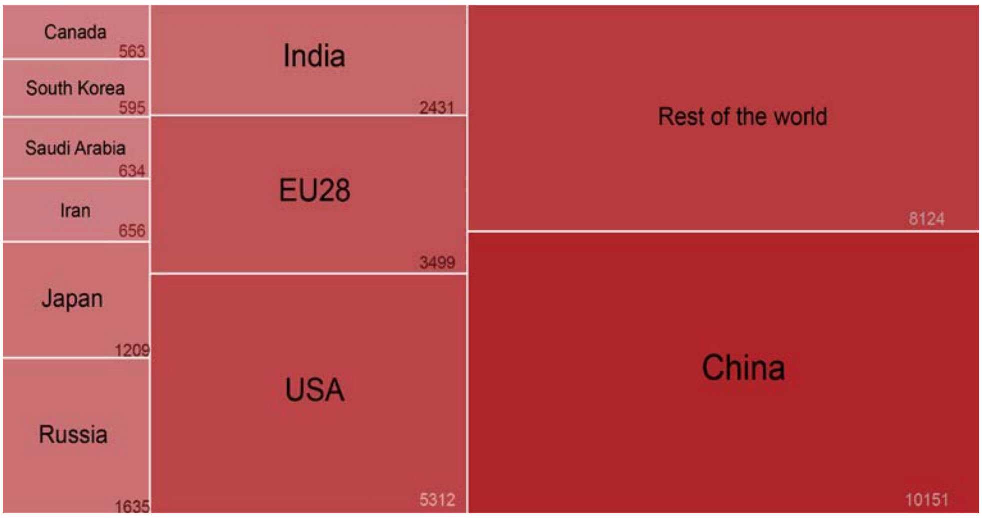
The 23rd session of the UN Climate Change Conference (COP23), presided over by Fiji, took place in Germany in November 2017. The EU and China are committed to the effective implementation of the Paris Climate Change Agreement. The Ministerial on Climate Action (MOCA) coalition, a joint group consisting of the EU, China and Canada, plays an important role following the US decision in June 2017 to pull out of the 2015 Paris Agreement. At the 20th Summit in July 2018, the EU and China confirmed their commitments under the 2015 Paris Agreement and agreed to step up their co-operation to enhance its implementation.

China, the world's largest emitter of GHG emissions, ranks 41st in terms of what has been done to tackle climate change.

In the Climate Change Performance Index 2018, published by GermanWatch, the New Climate Institute and the Climate Action Network, China, the world's largest emitter of GHG emissions (see below Figure 6), ranks 41st in terms of what has been done to tackle climate change, including development of renewable energy and achieving ambitious 2030 targets. In 2017 China's wind and solar power capacity reached 168.5 GW and 130.06 GW respectively, and renewables were generating 5.3 % of China's electricity supply.

While China is tackling air pollution, it became the world's largest user of energy-efficient vehicles in 2015. In 2016, China produced 517 000 new energy vehicles (battery electric cars, plug-in hybrids, and fuel-cell cars), and is planning to increase annual output to 2 million by 2020.

Figure 6:
Global CO2 emissions in 2016, territorial, in Mt



Source: © European Parliament, DG Expo ,Policy Dept, AS/GM, based on data from Global Carbon Atlas, December 2017

6 Human rights and civil liberties

The human rights situation in China is deteriorating under Xi's leadership.

The **human rights situation in China has been steadily deteriorating** under the rule of President Xi Jinping. There is a strong contradiction between the official Chinese declarations and the worsening human rights situation in the country.

In his letter to the opening of the Beijing Forum on Human Rights in December 2017, President Xi Jinping noted that 'there is always room for improvement when it comes to human rights protection', and that 'China has embarked on a path for human rights development suited to its reality through combining the universality of human rights with China's specific conditions'. While China is opening up to the world and assuming an increasingly assertive role, it is tightening internal control despite the fact that Beijing is currently **a member of the UN Human Rights Council** (until the end of 2019).

The Chinese government launched an unprecedented attack on human rights defenders in 2014.

Human rights defenders and other civil society activists are increasingly harassed, arbitrarily arrested and tortured in the country. 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 (including the cases of the Hong Kong book publishers), 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 Chinese leadership invested unprecedented resources into **mass surveillance and establishing large databases**, especially in Xinjiang region under the so-called 'Physicals for All' programme.

New laws restrict freedoms in the name of state security.

The clampdown includes new restrictive legislation on security, anti-terrorism and NGOs. A new national security law was passed in July 2015, defining security in broad and vague terms, included state control of the 'ideological sphere'. 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. The law introduces uncertainty for 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.

China's first counter-terrorism law contains a vague definition of terrorism.

China remains the world's leading executioner, with at least 2 000 capital punishments carried out by firing squad or lethal injection annually.

Despite a gradually decreasing number of cases, China remains the world's leading executioner, with at least 2000 **capital punishments** carried out by firing squad or lethal injection annually, accounting for over half of all executions globally. The exact numbers remain a state secret and there is no transparency with regard to court procedures, while about 10-15 percent of cases are estimated to be overturned by the Supreme People's Court. In 2011 the government reduced the number of offences punishable by death, although China maintains the death penalty for a number of non-violent offences, such as drug trafficking and economic crimes. In December 2017, a public trial and sentencing took place in a stadium with a large audience in Lufeng city (Guangdong province) that ended by 10 immediate death sentences, prompting some public debate on social media.

The foreign NGOs management law will curtail and control the activities of international NGOs.

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. It is estimated that there may be between 6 000 and 10 000 foreign NGOs operating in China; many of them so far registering as businesses. There are 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 more controlled environment for charitable organisations operating in China, but also more incentives for domestic donations.

Tensions between the authorities and ethnic minorities have increased.

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 urges China to meet its international obligations on human rights.

The EP has also noted, through several resolutions, the deterioration in the situation of human rights and freedoms. For many years EP has attempting to highlight the issue of **Tibet** and Uighurs to keep them on the international agenda.

The EU regularly issue statements urging China to abide by its international obligations, including respect for the Universal Declaration of Human Rights. One of the 28 EU Member States blocked the initiative of an EU statement criticising the crackdown on activists and dissidents in China that was due to be submitted to the United Nations Human Rights Council on 15 June 2017.

The EU Delegation in Beijing, on the occasion of the International Human Rights Day on 10 December 2017, specifically underlined the issue of arrests, detention and conviction of human rights defenders and lawyers and the freedom of religion and belief, including in Xinjiang and Tibet. It also pointed to the death in detention of 2010 Nobel Peace Prize Laureate Liu Xiaobo and the recent conviction of human rights lawyer Jiang Tianyong.

At the 36th round of the EU-China Human Rights Dialogue in July 2018, EU raised the deteriorating situation of civil and political rights in China.

At the 36th round of the EU-China Human Rights Dialogue in July 2018, the EU recalled that China, twenty years after having signed the International Covenant on Civil and Political Rights, has still not ratified it. The **EU also raised the deteriorating situation of civil and political rights in China**, which has been accompanied by the detention and conviction of a significant number of Chinese human rights defenders.

The EU supports civil society activities through the European Instrument for Democracy and Human Rights (EIDHR). The 3rd EU-China **Legal Affairs Dialogue**, scheduled to take place in autumn 2018, also addresses issues related to the rule of law.

7 Economy and trade

7.1 Economic update

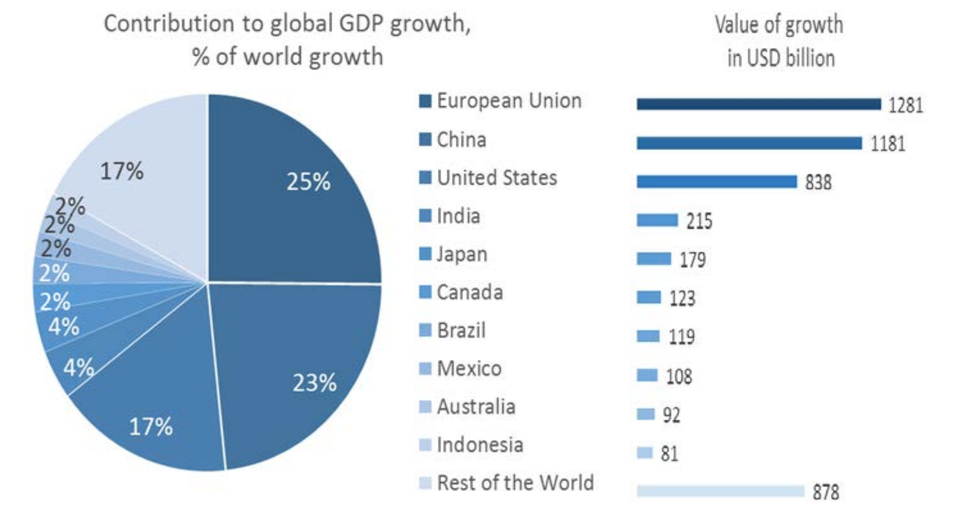
China is the world's third largest economy in terms of GDP after the US and the EU.

As Asia's largest economy, and the second (third, if the EU is taken into account) largest in the world, China plays a significant role, contributing around 23 % to global growth in 2018 (IMF). Despite a recent slowdown, China's growth is outpacing most other economies. Growth in China is estimated by the World Bank to have reached 6.8 % in 2017 but China continues to face vulnerabilities associated with high corporate indebtedness, particularly in sectors with overcapacity and deteriorating profitability.

Figure 7:
Top 10 economies contribution to global (nominal) GDP growth in 2018 (IMF forecast)

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

Contribution to global GDP growth, % of world growth   Value of growth in USD billion

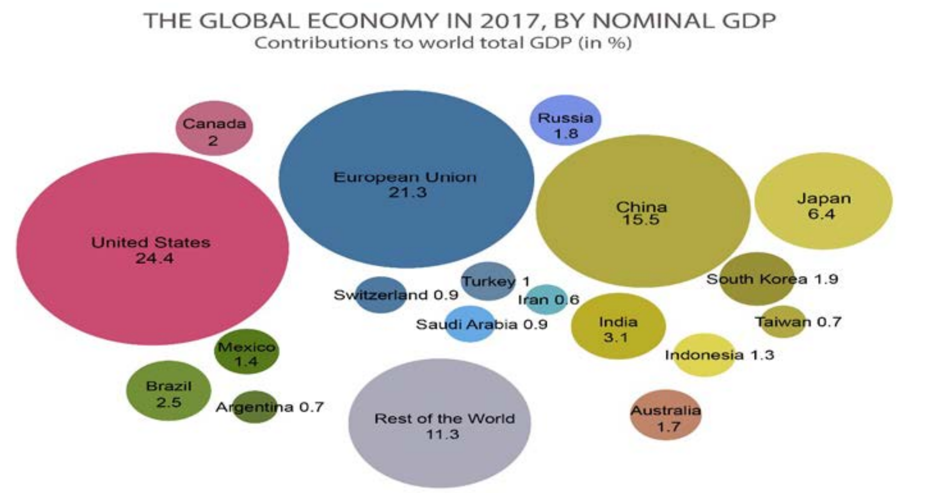


Source: European Parliament, DG EXPO Policy Dept., 2017, AS/GM, based on data from IMF, World Economic Outlook, October 2017

China's transition, or so-called rebalancing, is estimated to be positive overall for the global economy, but is likely to continue to produce some spill-over effects — that vary by country and by region.

The three top economies account for around 65 % of the world economy. The added value created by China's gross domestic product was estimated to be 15.5 % of the world's nominal GDP in 2017. Its contribution to global (nominal) GDP growth in 2018 is estimated at around USD 1.181 billion, compared to the EU's share of USD 1.281 billion. According to government figures, China's economy grew 6.9 % in 2017. The government's GDP growth target for 2018, at 6.5 %, reflects an acknowledgment of the continuing economic slowdown—whilst the emphasis is on higher-quality, more efficient growth. China's transition, or so-called rebalancing, is estimated to be positive overall for the global economy, but is likely to continue to produce some spill-over effects — through trade, commodity prices, investment and financial markets — that vary by country and by region.

Figure 8:
The global economy by GDP (2017, contributions in % of total)



Sources: © European Parliament, DG Expo Policy Dept., 2018, AS/GM, based on data from IMF, World Economic Outlook, October 2017

China's growth is forecast to moderate to 6.4 % in 2018 from 6.8 % in 2017.

According to the World Bank (WB), the global economy is projected to generate up to 3.1 % growth rate through 2018. Growth in China is forecast to moderate to 6.6 % in 2018 from 6.8 % in 2017, when the IMF and the WB raised their forecasts for China's growth, due to the economy's resilience. The outlook assumes that China addresses vulnerabilities, such as high and rapidly rising debt level and 'adjusted' corporate balance sheets (notably SOEs). Another key assumption is the absence of significant disruptions to trade and investment, hence the impact of the ongoing tensions with the US is to be considered.

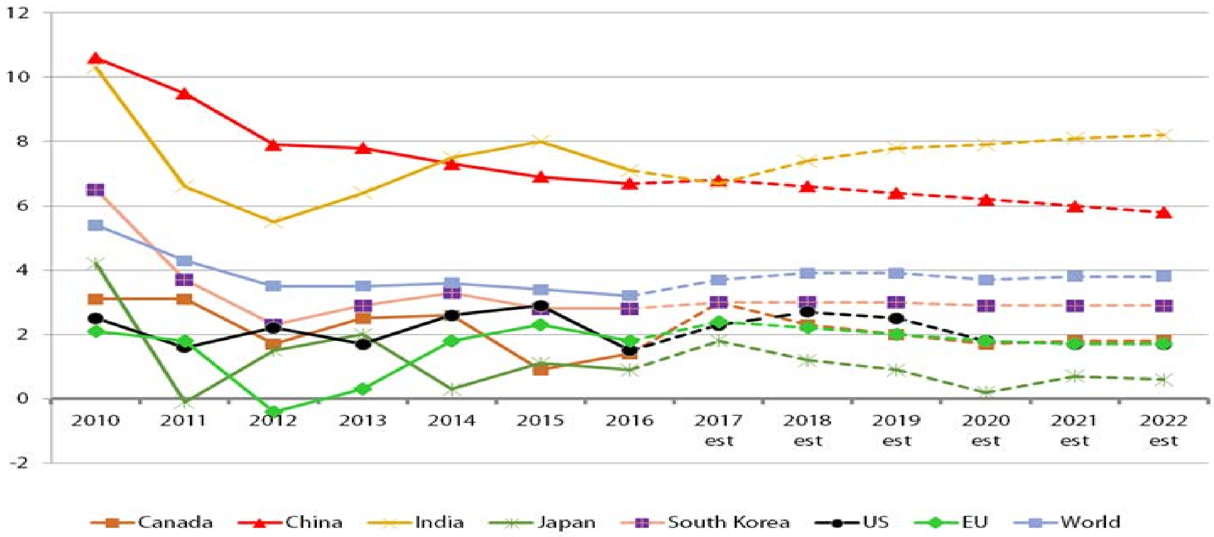
China is 'rebalancing' from investment to consumption and from manufacturing to services.

China is navigating a crucial but complex transformation towards more sustainable growth by 'rebalancing' from investment to consumption and from manufacturing to services. In 2017, growth continued to be led by strong domestic consumption, estimated to represent around 59 % of China's GDP growth in 2017. Total retail sales of consumer goods reached over 10 % growth in 2017 from 2016, while online sales surged by 32.2 % in 2017.

China's car industry began to transition in 2017 from high-growth, as 2017, for example, sales of passenger cars amounted to 24.7 million, in comparison to over 28 million cars sold in China in 2016.

China is expected to grow more slowly, by 6.2 % in the medium term, but its growth continues to outpace most other economies. A comparison of economic outlook projections of selected economies with China is given below (Figure 9):

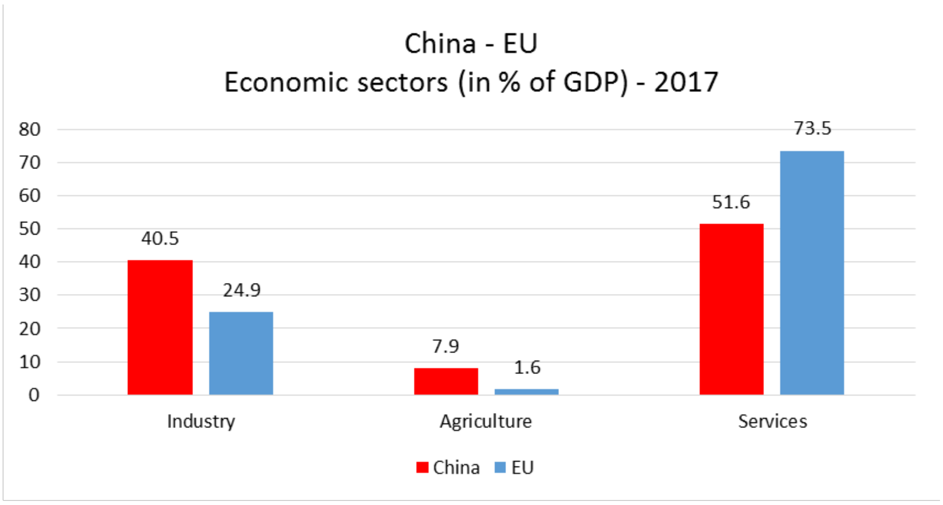
Figure 9: Real GDP growth (annual percentage change), 2010- 2022 (est.) of China and selected economies



Source: IMF DataMapper (POLDEP October 2017); World Economic Outlook Update, January 2018

According to the National Bureau of Statistics (NBS) data, **China's service sector accounted for 51.6 % of GDP** in 2017.The value added of agriculture (primary industry) and that of industry accounted, respectively, for 7.9 % and 40.5 % of GDP in 2017.

Figure 10:
China' and-EU's economic sectors (in % of GDP), 2017



Source: Statistical Communique, 28.2.2018; Eurostat

Potential spill-over effect of the 'rebalancing'

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

A study estimates that a spill-over effect of the 'rebalancing' as an average annual slowdown of GDP in China of one percentage 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 the countries in the world. The IMF study estimates that **China's move up the value chain,** i.e. production of higher added value 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 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.

7.2 Development plans and economic reforms

A 'collective study session' on economic policy priorities for 2018 focussed on Xi's thought on the socialist economy with Chinese characteristics for a new era, a balanced and sustainable 'high-quality development' concept.

On 8 December 2017, the 25-member Politburo of the Chinese Communist Party (CCP) held a 'collective study session' on economic policy priorities for 2018. China's annual Central Economic Work Conference took place on 18-20 December 2017, with an emphasis on Xi's thought on the socialist economy with Chinese characteristic for a new era, a balanced and sustainable 'high-quality development' concept, which covers slower, but more efficient economic growth along the '**new normal**'.

The Party's economic agenda for 2018 includes aims such as deepening supply-side reform; invigorating market participants; poverty reduction; climate change; promoting balanced trade, including the implementation of a pre-established national treatment system nationwide; and the grand-scale vision for global connectivity, including the Belt and Road Initiative.

7.2.1 The 13th five year development plan of China

Reforms under the 13th five-year plan for 2016-2020 are centred on rebalancing the economy.

In response to the country's economic slowdown, the **13th five-year Plan for National Economic and Social Development of China for 2016-2020** (the 13th Five-Year Plan), endorsed by the NPC in March 2016, translates the economic and social reform agenda into a set of concrete actions.

China is aiming at attaining a 'New Normal' featuring lower, but more service and technology-oriented economic growth.

The **economic and social reform process,** aimed at achieving greater efficiency, through the **'new normal'**, is characterised by increasingly more service and technology-oriented economic growth. According to the Plan, China aims to double its GDP and per capita income of both urban and rural residents from the 2010 level by 2020.

The reforms have gradually revealed their 'Chinese characteristics', as market forces have been given less prominence than expected.

According to the 13th FYP, Chinese government plans to continue the promotion of private-sector participation as well as to **strike a balance between the role of the government and that of the market**, 'letting the market play the decisive role in allocating resources'. However, the reforms have gradually revealed their 'Chinese characteristics', as market forces have been given less prominence than expected — a quite different approach from 'Western supply side economics'.

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.

China's 13th Five-Year Plan includes aims to implement the 'Made in China 2025' initiative, with an objective of **becoming a global manufacturing powerhouse**. In both, the industrial upgrading and the listed new strategic industries, the developments focus on utilising advanced technologies to enhance the value-added and competitiveness of the manufacturing industry.

The 13th Five-Year Plan **further encourages technological R&D activities** and includes targets to raise the share of R&D expenses in GDP to 2.5 % by 2020. In 2017 Chinese spending on R&D amounted to 2.1 % of total GDP, as compared to 2.8 % for the US, 2.9 % for Germany and 3.3 % for Japan.

7.2.2 'Made in China 2025'

The 'Made in China 2025' strategy of 2015— a master plans for China's economic transformation and upgrading its manufacturing industry.

The **'Made in China 2025'** (Plan) of 2015, a master plan for China's economic transformation and upgrading its manufacturing industry, has seen steady progress. The Plan has explicit targets for 10 industries, including advanced information technology, automated machine tools and robotics, aerospace and aviation equipment, maritime engineering equipment and high-tech vessels, advanced rail equipment, energy-saving vehicles and new energy vehicles (NEVs), electrical equipment, agricultural machinery and equipment, new materials, biopharmaceuticals and high-performance medical devices.

The 'Made in China 2025' seeks to replace foreign products with domestic products in the Chinese market,

In these industries, the Plan seeks to replace foreign products with domestic products in the Chinese market, and includes a 'semi-official' targets for the domestic market shares that would 'realise guarantees of self-sufficiency. The Plan also specifies **10 key policy tools** (such as forced technology transfers in exchange for market access, standards, subsidies, financial policy, SOEs and public-private partnerships) to be used in their pursuit.

An updated version of the 'Made in China 2025' roadmap, released in January 2018, includes targets for the country to become the world's leading

An updated roadmap of the 'Made in China 2025' of January 2018 guides the country to become the world's leading manufacturer of telecommunication, railway, and electrical power equipment by 2025.

manufacturer of telecommunication, railway, and electrical power equipment by 2025; and second or third in industries such as robotics, high-end automation, and new energy vehicles by 2025. According to the vice-minister for industry and information technology, Xin Guobin, China has already become one of the world's largest producers of more than 220 types of product. The government's intervention and government financial and other support for 'Made in China 2025' is estimated to exceed USD 1.5 billion. The Advanced Manufacturing Fund (a RMB 20 billion or around EUR 2.7 billion fund) was set up in June 2016 to facilitate the modernisation of manufacturing in China.

Figure 11: China's production/assembly in 2015 as of % of world production, and 2016 and 2017 production

Chinese production or assembly	***as % of world production in 2015***	**2016 production (estimate) In million units**	**2017 production (estimate) In million units**
Cars	*28*	28	29
Computers	*80*	290	307
Mobile phones	*90*	2 058	1 890
Refrigerators	*50*	85	85
Air conditioners	*80*	143	179
Colour TV sets	*60*	158	159

Source: EU Chamber of Commerce in China, 'China Manufacturing 2025: Putting Industrial Policy Ahead of Market Forces, 2017; Statistical Communiqué, National Bureau of Statistics of China, 28.02.2017; Statistical Communiqué, National Bureau of Statistics of China, 28.02.2018

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

China has continued to reform its SOEs but is keeping public ownership as the mainstay of the economy.

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 process of reforming SOEs has reduced the number of centrally administered SOEs to 98 from 117, and is **creating 'national champions'** that can push down the profit margins of global competitors as they continue to benefit from state funding. One of the examples in 2017 includes a merger of two of China's top bullet-train manufacturers, the China South Locomotive and Rolling Stock Corporation and the China CNR Corporation, which held global market shares of 30 % and 18 % respectively. The new CRRC Corporation Ltd would have by far the largest global market share.

The process of reforming SOEs has reduced the number of central SOEs to 98 from 117 and is creating 'national champions'.

In 2017, centrally administered SOEs had set up more than 700 new 'mixed-ownership' companies. According to China's State Council, there are currently 150 000 SOEs at central and local government levels. Fortune's 2016 list of the world's 500 largest companies includes 103 Chinese firms, of which 28 appear to have financial links to the Chinese government.

The reform of SOEs is prioritising steel, coal and power businesses,

The State-Owned Assets Supervision and Administration Commission (SASAC) is attempting to deepen the reform of SOEs, prioritising the restructuring of steel, coal and power businesses, and other sectors, including petroleum, gas, including petroleum, gas, railways, telecommunications, civil aviation and military-related industries.

railways, telecommunications, civil aviation and military-related industries, to conduct 'mixed ownership' reforms, thus many SOEs function as if they were 'private' enterprises. In 2017, the SOEs supervised by the SASAC made a total of RMB 1.4 trillion (about USD 216.8 billion) in profit, up 15.2 % from 2016.

Sectors of strategic importance remain dominated by large SOEs.

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 and financial services; telecommunications, education, health care and defence industries).

7.2.4 The 13th five year plan for Trade in Service Development

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.

The **13th Five-Year Plan for Trade in Service Development** (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 aims to strengthen export capacity, including the development of new types of services, such as cross-border e-commerce, and service outsourcing, while seeking to use free trade agreements (FTA) to strengthen China's position in the service market in specific countries.

According to the Plan, the growth of **China's trade in services faces challenges, such as increased international competition, trade protectionism and reconstruction of international rules on trade in services.** China has a Memorandum of Understanding on trade in service cooperation (including e-commerce) with several countries and regions.

China's Fiscal and Monetary Policy

China has, with other G20 partners, committed to refrain from competitive devaluations and not target exchange rates for competitive purposes.

China has committed to continue a market-oriented exchange rate reform that allows for two-way flexibility. At the G20 finance ministers meeting under the Chinese Presidency in July 2016 China, with other G20 partners, committed to refrain from competitive devaluations and not target exchange rates for competitive purposes.

The yuan - renminbi (**CNY**, **but often called 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, effective 1 January 2018, limiting individuals' withdrawals to RMB 100 000 (about USD 15 530) annually from outside China.

Cross-border accounts must be approved by the State Administration of Foreign Exchange.

On 5 January 2018, the People's Bank of China issued a notice on 'Further improving RMB cross border settlement policy and expediting the convenience of Investment and Trade', as part of efforts to facilitate overseas investment and trade. Holding of cross-border accounts requires an approval of the State Administration of Foreign Exchange.

On 1 October 2016, within the IMF Special Drawing Rights (SDR) currency basket, RMB became a freely usable currency along with the US dollar (0.58252), euro

(0.38617), Japanese yen (11.900) and pound sterling (0.085946), as a currency with the third (1.0174) biggest weight in the basket.

In 2016 China indicated that it was advancing the implementation of the OECD/G20 Base Erosion and Profit Shifting (BEPS) Action plan.

In 2016, when taking over the G20 presidency, China indicated that it was advancing the implementation of the OECD/G20 Base Erosion and Profit Shifting (BEPS) Action plan. The Chinese authorities decided not to conduct exchanges of the BEPS country-by-country reports of tax year 2016 in State Administration of Taxation (SAT) Announcement No. 46, issued on 19 December 2017. Although not a member of the OECD, China has been the key partner of the OECD since 2007.

Tax reform is an on-going priority.

China also clarified the 'beneficial owner' definition to determine non-resident eligibility for tax treaty benefits.

The value added tax (VAT) and corporate income tax (CIT) amount to around 50 % of China's total tax revenues. Tax reform is an on-going priority for the Chinese authorities, and as a result of the implementation of the VAT reform on services, taxes have been reduced by an estimated RMB 2 trillion (USD 308 billion) in the last five years. In 2017, the value-added tax (VAT) structure was further streamlined. China is, notably in the process of reforming its tax identification regime for legal persons. On 3 February 2018, the (SAT) announced clarification on the Beneficial Ownership in Double Taxation Agreements to clarify the 'beneficial owner' definition to determine non-resident eligibility for tax treaty benefits on China-sourced dividends, interests and royalties, effective as of 1 April 2018.

7.2.5 The Employment First Strategy

The government is implementing the 'Employment First Strategy' and is working to develop vocational education and training and improve social protection.

China's economic growth phase of 'New Normal' includes the government's '**Employment First Strategy**' and more active employment policies. It also aims to develop vocational education and training and improve the social protection system.

At the end of 2017, the total number of employed people in China was 776.4 million: 424.6 million in urban areas and 351.8 million in rural areas. The total number of migrant workers in 2017 was 286.5 million, up by 1.7 % from 2016. The registered urban unemployment rate remains about 3.9 %.

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.

7.3 China's global commercial strategy

Whilst China has been active in all spheres of the multilateral trading system, it is supplementing it particularly with a comprehensive Free Trade Agreement strategy at regional, sub-regional and bilateral levels.

Whilst China has been active in all spheres of the multilateral trading system, since its accession to the WTO in 2001, it is supplementing it particularly with a comprehensive Free Trade Agreement (FTA) strategy at regional, sub-regional and bilateral levels of trade and investment liberalisation and facilitation as well as cooperation arrangements. In 2017, China's free trade agreements (FTAs) extended far beyond its close neighbourhood, such as Southeast Asian Nations (ASEAN), reaching out to Latin American, Central Asian and European countries. China also signed FTAs with Georgia and Maldives in 2017. China also has an 'economic cooperation framework agreement' with Taiwan, which is the equivalent of an FTA (see List of China's FTAs in Annex 3).

China is the top trading partner of over 120 countries/regions, which represent over 80 % of global GDP.

7.3.1 World Trade Organisation

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

China's accession protocol to the WTO in December 2001 took into account the legal and economic particularities of China's transition economy. These specific arrangements have enabled WTO members, e.g. 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.

A number of China's WTO commitments to open and liberalise the Chinese economy, have still not been met.

In turn, China's WTO accession required the country to make bold reforms and liberalise important parts of its economy. Yet, **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 reforms addressing excess industrial capacity remain to be completed. In 2017, trade-restrictive measures stabilised in the largest economies and declined in the rest of the world.

China played an active part in the Doha Development Agenda (DDA) negotiations.

China participated actively in the Doha Development Agenda (DDA) negotiations. At the WTO Mini-ministerial Conference that was held in March 2018 China reiterated its support to the multilateral trading system and towards joint efforts to ensure the smooth operation of the WTO functions and continue negotiations of the left-over topics of the DDA.

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, and 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.

China' accession to the WTO Agreement on Government Procurement would be a matter of significance to the world economy.

China applied for accession to the WTO Plurilateral Agreement on Government Procurement (GPA) on 28 December 2007, but remains an observer and continues to negotiate its accession thereto. China's GPA accession, on mutually agreeable and appropriate terms, would be a matter of significance to the WTO and for the world economy.

7.3.2 China and selected free trade agreements

China's trilateral FTA negotiations with Japan and South Korea continued in 2018.

Trade negotiations between **China, Japan and the Republic of Korea** resumed from 22 to 23 March 2018, nearly a year after the 12th round on 13 April 2017 in Tokyo. The three parties exchanged views on issues, such as trade in goods, trade in services (telecommunications and financial services) and investment. The Trilateral Investment Agreement came into force in May 2014. The three countries are also part of a broader effort to clinch a 16-country regional trade deal, the Regional Comprehensive Economic Partnership.

The China-South Korea FTA was signed in 2015.

China and the Republic of Korea signed a bilateral FTA in June 2015. The FTA governs around USD 300 billion in trade in goods and 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 next phase of the bilateral pact was launched in March 2018, by the first round of negotiations on services and investment that should build on existing commitments.

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

The **Regional Comprehensive Economic Partnership** (RCEP) is seen as China's alternative response to the Trans Pacific Partnership agreement (now called **the Comprehensive and Progressive Agreement for Trans-Pacific Partnership**, the CPTPP). The 16-party RCEP FTA negotiations were launched by the 10 ASEAN countries and the existing FTA partners of ASEAN — Australia, China, India, Japan, Republic of Korea and New Zealand in the margins of the East Asia Summit in November 2012. The Ministerial Conference of RCEP was held on 12 November 2017 to prepare the meeting of RCEP Leaders that took place on 14 November 2017, when the Outline of the RCEP Agreement (as of November 2017) was annexed to the Joint Statement of the 16 participating countries.

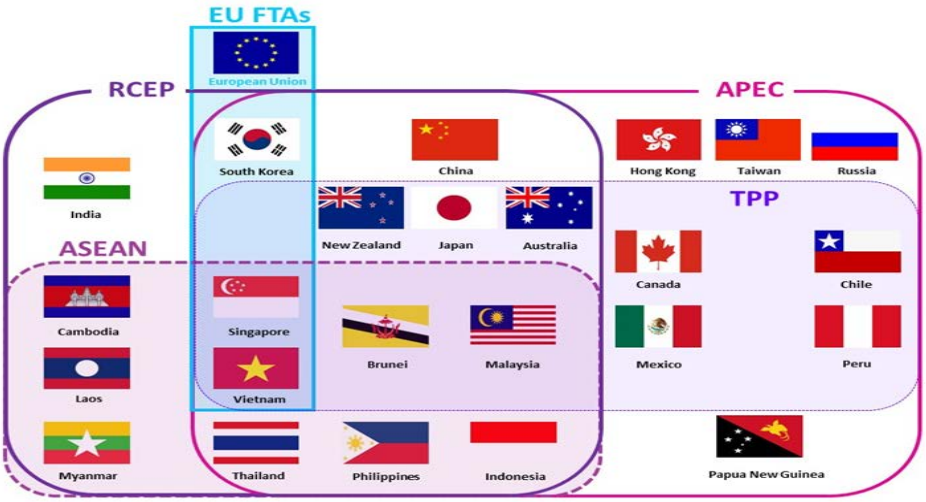
The Chinese foreign minister had called for joint efforts to conclude the RCEP negotiations by 2017, and stated that 'Either the RCEP or TPP or other regional arrangements is a possible path to the broader Free Trade Area of the Asia-Pacific' (FTAAP). The 21st round of the RCEP negotiations was held on 5-9 February 2018 in Indonesia. The 5th RCEP Ministerial meeting was held on 30 June to 1 July 2018 in Tokyo.

The RCEP is not expected to be a 'new generation' trade agreement and is expected to consist of some WTO-plus commitments.

It remains to be seen whether the final RCEP, will be a 'new generation' trade agreement, but it is expected to consist of some WTO-plus commitments. Differences between the CPTPP and the RCEP, will likely concern the inclusion of provisions such as state-owned-enterprises, environment and government procurement. Provisions on investment and dispute settlement appear to be part of the RCEP agreement, but the extent and the depth of the penalisation commitment remains to be seen.

Since the US withdrew its participation in January 2017, the CPTPP free-trade bloc includes Japan, Vietnam, Malaysia, Singapore and Brunei, Australia, New Zealand, Peru, Chile, Canada and Mexico. The CPTPP agreement was concluded in Japan on 23 January 2018 and signed in Chile on 8 March 2018. The CPTPP provides that 'at least six or at least 50 percent of the signatory countries must ratify for the deal to entry into force.

Figure 12: Participation in Regional Comprehensive Economic Partnership (RCEP) and the former Trans-Pacific Partnership (TPP-11), which is now called 'the Comprehensive and Progressive Agreement for Trans-Pacific Partnership'



Sources: http://www.postwesternworld.com/images/2015/08/RCEP.png; http://atlantacir.org/wp-content/uploads/2017/01/Chart-2.jpg

7.4 Trade policy issues

7.4.1 Overview

Although China became the world's largest exporter in 2010, it remains relatively closed to exports from other countries.

China's, the world's largest exporter since 2010, trade surplus continued to narrow in 2017, declining 14.2 % from the previous year, while the country's overall exports increased 11 %, according to government data. In 2017, China's foreign trade volume, rose 14.2 % (from 2016) to RMB 27.79 trillion (around USD 4.28 trillion). China remains relatively closed to imports from other countries, ranking 121st out of 136 countries for domestic market access. China has announced that it will adjust duties and import taxes on a number of import and export items in 2018, such as machine components, energy materials, and raw materials for advanced medicine.

The Global Enabling Trade Report 2016 ranks China in 61st position, behind the best performing countries in its neighbourhood.

In the Global Enabling Trade Report 2016, co-published by the World Economic Forum and the Global Alliance for Trade Facilitation, China is ranked in 61st place (out of 136 countries) in the index that measures domestic and foreign market access; border administration; transport and digital infrastructure; transport services; and operating environment. China is behind the best countries in its neighbourhood — Singapore (first), Hong Kong (third) and Japan (16th). The country performs best in the transport infrastructure category, where it ranks 12th globally.

Trade tensions have jumped to the top of the list of risks facing China in 2018.

7.4.2 Overcapacity

China, with other G20 partners, agreed to reduce steel excess capacity at the G20 meeting in November 2017.

China, with other Group-20 countries, recognises that structural problems, including **excess capacity in steel and other industries, exacerbated by a weak global economic recovery and depressed market demand**, has a negative impact on trade, workers and economic growth.

The first Ministerial meeting of the **G20/OECD Global Forum on Steel Excess Capacity (GFSEC)**, established on 16 December 2016, resulting from the

G20 Leaders' Summit in July 2016, was hosted by the German G20 Presidency on 30 November 2017. The 33 economies in the Global Forum represent over 90 % of global steel production capacity. Ministers agreed on a report, including a roadmap with six guiding principles to reduce excess steel capacity. The report notes that the GFSEC members' combined capacity to produce crude steel stood at 2 031.4 million Mmt in 2016, of which China's capacity was estimated to 1 073.3 Mmt.

China has taken steps to cut excess production capacity.

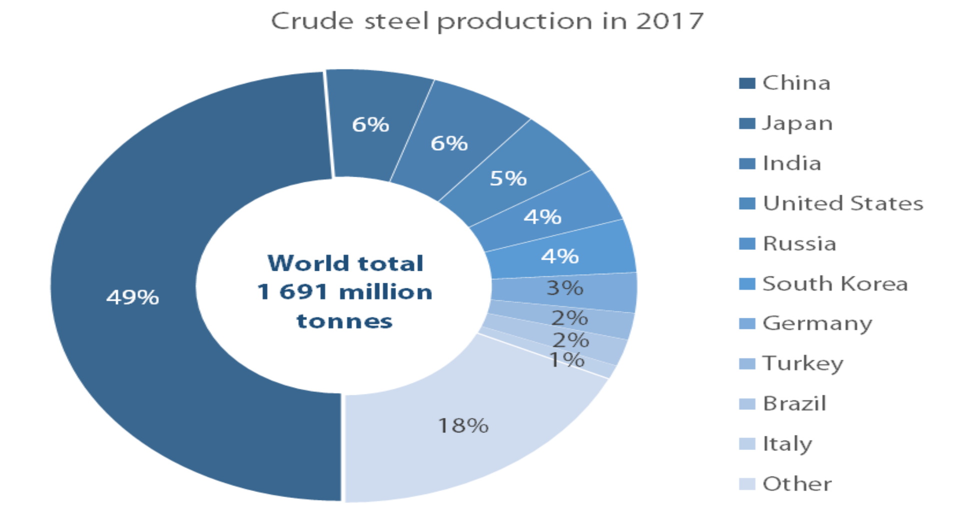
China's supply-side structural reforms started in 2016 when the State Council's **Guidance for the Iron and Steel Industry to Reduce Excess Capacity and Resolve Difficulties for Future Development** set targets to reduce 100 to 150 million tons of domestic crude steel capacity in five years starting from 2016. They involve a reduction in capacity of between 9 % and 13 % to 977-1027 Mmt and the resettling of 500 000 workers — around 15 % of the total. In November 2016, the Ministry of Industry and Information Technology (MIIT) issued the Iron and Steel Industry Adjustment and Upgrade Plan (2016 – 2020) that set the same targets and raises the capacity utilisation rate to 80 % by 2020.

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.

China's problem of overcapacity is much broader and encompasses several other sectors besides steel. The problem of overcapacity in a number of heavy industries has its roots in the state support to state owned enterprises and in some trade-distorting practices. 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 glass and vessels (ship) industries**. According to the State Council**,** in 2017 China's production of steel and coal was reduced by 5.95 million tons and 27.03 million tons, respectively.

According to the World Steel Association's statistical yearbook 2017, the total production of crude steel in China increased slightly in 2017, to 831.7 Mmt, representing around 49 % of the total number of 66 countries' crude steel production (of a total of 1691.2 Mmt).

Figure 13:
Imports and Exports of Goods by Major Countries and Regions and the Growth Rates in 2017



Source: *World Steel Association*

7.5 Trade and investment

7.5.1 Trade

China is an integral part of the global value chain, and much of its exports are foreign-produced components delivered for final assembly in the country

According to the World Bank, 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. China is an **integral part of the global value chain**, and much of its exports are foreign-produced components delivered for final assembly in the country. However, the import content of Chinese investment spending fell from around 30 % in 2004 to 18 % in 2014 as China sourced intermediate goods domestically. The shift in global value chain puts many economies heavily involved in the 'Asia value chain' under competitive pressure.

In 2017, China's total external trade reached USD 4.10 trillion, and China's exports and imports increased by 7.9% and 15.9% respectively, resulting in a trade surplus of USD 422.5 billion. In 2017, China's trade surplus with US was USD 275.8 billion; with the EU USD 127.2 billion; with India USD 51.7 billion and with Japan USD 28.3 billion.

According to Chinese authorities, in 2017 the **main destinations for China's merchandise exports** remained the United States 19 %; the EU 16 %; Hong Kong 12 %;Japan 6 %; and the Republic of Korea 4.5 %.In this context, China's statistics indicate that the ASEAN region absorbs over 12 % of its exports.

In 2017, the main **sources of imports of goods to China** were the EU (13.0 %); the Republic of Korea (10 %); the United States (8.4 %); Japan (9 %); Taiwan (8.4 %); and the Russian Federation (2 %).

Figure 14: China's imports and exports of goods with top countries and regions and the growth rates in 2017

Country or region	Exports			Imports		
	RMB (100 million)	Increase over 2016 (%)	Proportion of the total%	RMB (100 million)	Increase over 2016 (%)	Proportion of the total%
EU 28	**25 199**	**12.6**	**16.4**	**16 543**	**20.2**	**13.3**
United States	29 103	14.5	19.0	10 430	17.3	8.4
ASEAN	18 902	11.9	12.3	15 942	22.8	12.8
Japan	9 301	8.9	6.1	11 204	16.3	9.0
Hong Kong	18 899	-0.4	12.3	495	-54.9	0.4
South Korea	6 965	12.6	4.5	12 013	14.4	9.6
Taiwan	2 979	12.2	1.9	10 512	14.5	8.4
Brazil	1 962	35.2	1.3	3 974	31.4	3.2
India	4 615	19.8	3.0	1 107	42.4	0.9
Russia	2 906	17.8	1.9	2 790	31	2.2
South Africa	1 004	18.4	0.7	1 649	12.1	1.3
Other, est.	31 610		20.6	38 030		30.5
Total, est.	153 445		100	124 689		100

Source: : Statistical Communiqué, National Bureau of Statistics of China, 28.02.2018

Figure 15:
China's main export Commodities (2016 and 2017)

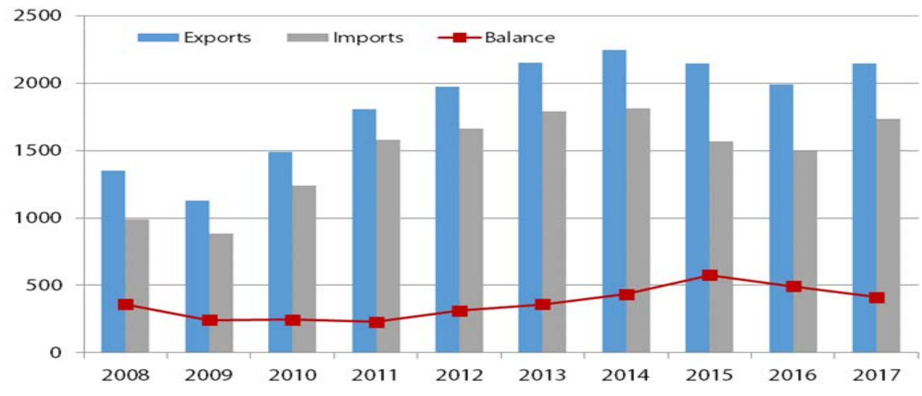
Commodities	2016 (in RMB 100 million)	2017 (in RMB 100 million)
Clothes and clothing accessories	10 413	10 656
Automatic data processing machines and components	9 068	10 710
Handheld mobiles and car telephones	7 643	8 503
Textile yarns and textile articles	6 925	7 441
Rolled steel	3 587	3 700
Furniture and parts	3 151	3 385
Footwear	3 113	3 269

Source: Statistical Communiqué, National Bureau of Statistics of China, 28.02.2018

In the first quarter of 2018, it is estimated that China's total imports grew by 31 %, while its exports grew 15 %.

Combined January-March 2018 data shows an increase of 24.4 % (year-on-year) as total import and export volume reached USD 563.5 billion. **China's trade surplus** rose 43.6 **%,** to USD 54.32 billion in the first quarter 2018; exports and imports rose 14.1 % and 18.9 %, respectively in comparison to the same period in 2017.

Figure 16:
China's trade in goods in USD billion

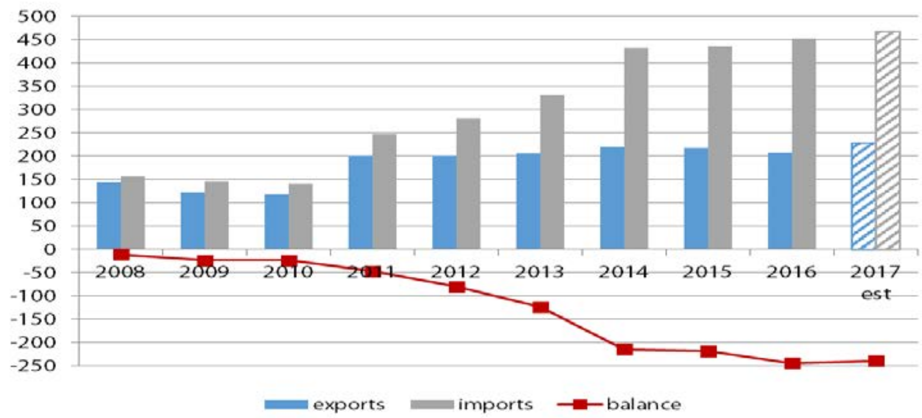


Source: World Bank and CNBC

China's commercial services imports accounted for over a quarter of total imports in 2017.

China's Imports of commercial services have surged since 2010 (USD 140.9 billion) to USD 449 billion in 2016. In 2017, total trade in services from China was up by around 7 %, amounting to USD 696 billion, of which exports were USD 228 billion and imports of USD 468 billion. According to the WTO, China was the 5th largest exporter of commercial services in 2017 (up from the 16th in 1995), reaching USD 226 billion. In 2017, exports of services were up by 10.6 %, while China's import of services increased by 5.1 % from 2016.

Figure 17:
China's exports and imports of services (in USD billion)



Source: World Bank - World Integrated Trade Solutions (WITS); 2017; Statistical Communiqué, National Bureau of Statistics of China, 28.02.2018 -(2017 data calculated by POLDEP, based on the Federal Reserve avg exchange rate for 2017 : 1 USD = 6.7569 RMB.

7.5.2 Investment

China has continued to seek to attract FDI by easing formalities and creating a number of incentive schemes.

China has continued to seek to attract FDI by opening up various industries to foreign investors. The revised 'Catalogue for the Guidance of Industries for Foreign Investment' came into force on 28 July 2017. It stipulates in which of over 400 industry sectors, foreign investment is 'encouraged', 'restricted' or 'prohibited'. The 2017 Catalogue reduces the number of restrictions or special administrative measures on foreign investment from 93 to 63. This reflects the government's efforts making the manufacturing sector more attractive to foreign capital, including the **'Made in China 2025**' strategy and the strategy of innovation-driven development. It encourages foreign investments in, among others, high and new technology, advanced manufacturing, energy conservation and modern service industries, such as e-commerce. The joint venture requirement with a Chinese party (who holds at least 50 % ownership) continues to apply for manufacturing automobiles, limiting them to maximum of two for the same type of passenger automobiles and commercial automobiles.

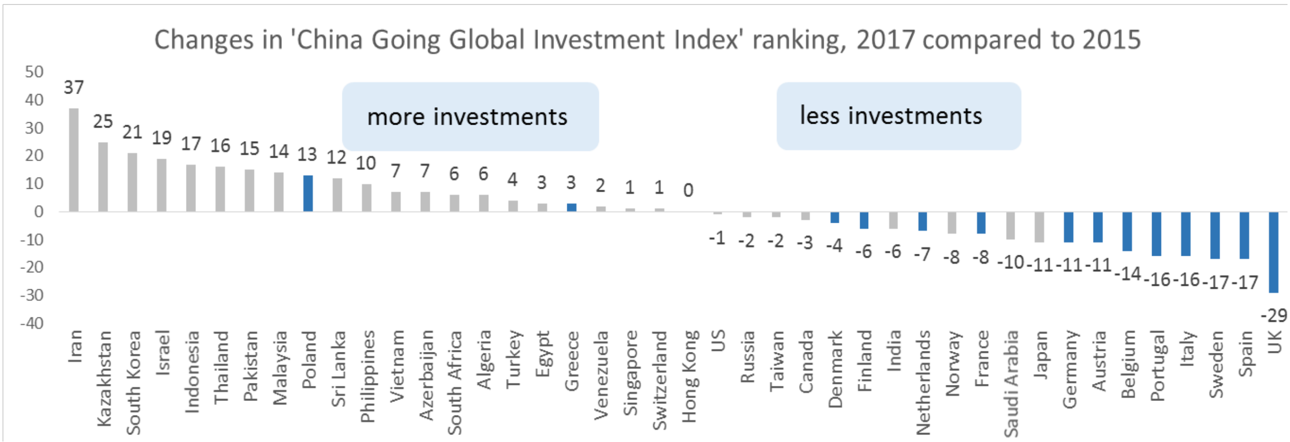
New guidelines on Chinese foreign investment policy aim to facilitate foreign investment in China.

China continued to seek to attract FDI, and in the Free Trade Zones across the country.

The government published the 'Special Administrative Measures of Pilot Free Trade Zone for Admittance of Foreign investments' (negative list), effective from 10 July 2017, to simplify the process for foreign investors in setting up their business in the 11 Free Trade Zones and lifting investment restrictions in a number of sectors in China. The list specifies 15 investment sectors and 40 industries in which foreign investment remain 'restricted' or 'prohibited' such as mining, leasing and financing, but removes 27 restrictions, allowing for more equal treatment to foreign and Chinese companies. The negative list model is expected to be adopted nationwide in January 2018.

The Economist Intelligence Unit's 'China going global investment index ' of 2017 (see below Figure 18) puts the US at the top of the index, which balances opportunities against risk for 67 countries.

Figure 18: Changes in Chinese ODI index, 2017 compared to 2015, selected countries



Source: 'China Going Global Investment Index 2017', Economist Intelligence Unit

Inward Investment to China

In 2017, the US remained the largest recipient of

According to UNCTAD, global flows of foreign direct investment (FDI) fell by 16 % in 2017 to an estimated USD 1.52 trillion, from a revised USD 1.81 trillion

FDI, with USD 311 billion in inflows, followed by China with record high inflows of an estimated USD 144 billion.

in 2016. In 2017, the US remained the largest recipient of FDI (USD 275 billion), followed by China with an estimated USD 136 billion. The top two economies were followed by Hong Kong, Singapore, and the Netherlands with estimated inflows USD 104 billion, USD 62 billion and USD 58 billion, respectively. FDI inflows to the EU declined from USD 500 billion in 2016 to an estimated USD 370 billion in 2017, representing a 26 % decline.

According to the Ministry of Commerce, FDI flows into China reached USD 136.3 billion, a record high, in 2017.

China's new rules, effective from March 2018, will restrict domestic companies' outbound overseas investments.

On 26 December 2017, the National Development and Reform Commission (NDRC) issued the 'Administrative Measures for Enterprise Outbound Investment' (Regulation No. 11), which came into force on 1 March 2018. The monitoring of outbound investments will no longer be subject to pre-transaction 'verification' and 'record-filling' or reporting procedures, even for overseas projects worth over USD 300 million. However, projects involving sensitive countries, regions or industries, continue to be subject to a verification procedure. Restrictions apply to domestic companies' outbound FDIs in certain sectors such as real estate, hotels, entertainment, and sports clubs, while indicating support for investments in natural resources and along the 'Belt and Road' corridors.

The new Negative List, effect on 28 July 2018, outlines prohibited and restricted industries for foreign investment.

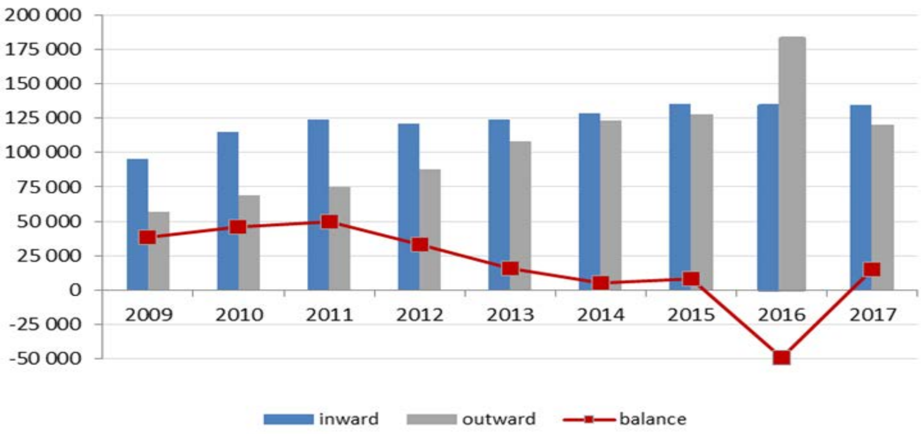
The NDRC and the Ministry of Commerce jointly released new national, negative list 'the Special Administrative Measures on Access to Foreign Investment 2018', effect on 28 July 2018. The new Negative List outlines prohibited and restricted industries for foreign investment and reduces the number of restrictive measures from 63 in the previous version to 48. The new free trade zone negative list, 'the Special Administrative Measures for Foreign Investment Access to Pilot Free Zones' reduce restrictive measures from 95 in the previous version to 45.

Chinese Outward Investment

According to UNCTAD World Investment Report, China was the 3rd largest source of outward FDI flows (USD 125 billion) in the world in 2017, behind the US (USD 342 billion) and Japan (USD 160 billion).

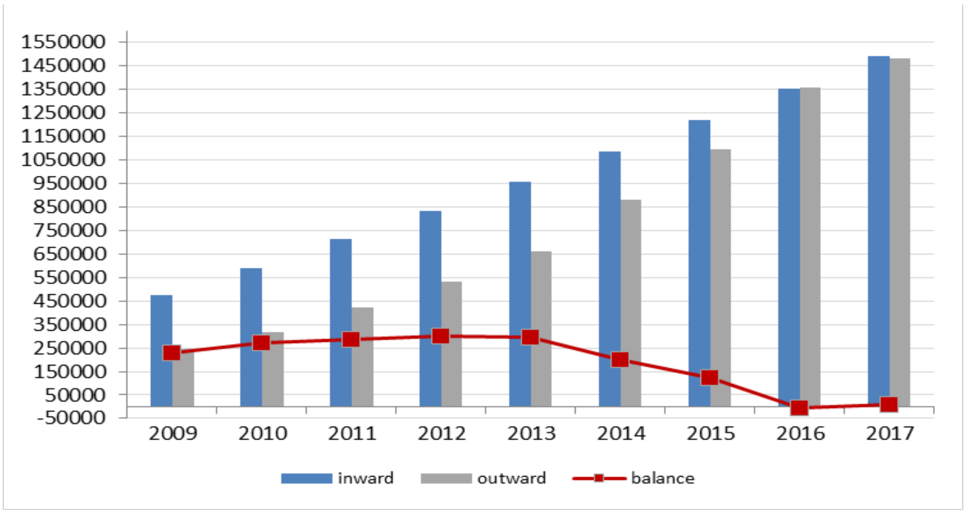
According to China's Ministry of Commerce, Chinese investors provided direct investment overseas in 2017, (excluding banking, securities and insurance) amounting to RMB 810.8 billion, (USD 120.1 billion), down by 29.4 % over 2016. Chinese investment in countries along the Belt and Road amounted to USD 14.4 billion in 2017.

Figure 19:
China FDI flows with world (in USD million)



Source: [*UNCTAD, World Investment Report 2018*]

Figure 20:
China FDI stocks with world (in USD million)



Source: *UNCTAD, World Investment Report 2018*

One of the key outcomes of China's G20 presidency was the G20 Guiding Principles for Global Investment Policymaking.

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). Although voluntary, they include a strong statement on **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.

7.6 Digital economy and cyber security

Cybersecurity is recognised as one of the world's most critical risks.

Cybersecurity is recognised as one of the world's most critical risks, requiring **international governance of cyberspace**. The World Economic Forum's Global Cyber Centre's recently established platform encourages collaboration on global cybersecurity challenges.

At the 2016 G20 Hangzhou Summit, China prioritized digital economy for the G20 Blueprint on Innovative Growth. The G20 Digital Economy Ministers' Declaration of 8 July 2017 set a roadmap for joint digital policies.

The 8th EU-China ICT Dialogue took place on 11 July 2017. The collaboration through initiatives such as EXCITING, which aims to explore the platforms for cooperation between China and the EU, could push towards new technologies, such as autonomous vehicles.

The Council conclusions on 'malicious cyber activities' of 16 April 2018 (a part of the EU's CFSP) stress the importance of a global, open, free, stable and secure cyberspace where human rights, fundamental freedoms and the rule of law fully apply for the social well-being, economic growth and prosperity. It will also assess the progress achieved under **the EU-China Cyber Taskforce**.

China boasts more internet users than the EU and US combined, and it's rapidly growing e-commerce sector, represents around 40 % of global e-commerce.

In 2017, China's digital economy accounted for 30.3 % of the country's total GDP, amounting to about USD 3.43 trillion. China boasts more internet users than the EU and US combined, and it's rapidly growing e-commerce sector, represents around 40 % of global e-commerce. It has dramatically changed the way Chinese enterprises conduct their business, as well as day-to-day life with the easier transfer of money for goods and services.

Recent legislation in these areas in digital economics and cyber-security includes China's 'Internet Plus' initiative of 2016, which is promoting the main strategy, 'Made in China 2025' integration plan (through e-commerce). China aims to have commercial use of 5G technology in use by 2019/2020, in some of its regions and the country also aims to become a world-leading cyber power by 2035.

China's Strategy on International Cooperation in Cyberspace

The Chinese Strategy on International Cooperation in Cyberspace was released on 1 March 2017, which sets out 4 basic principles for cooperation.

On 1 March 2017 the Chinese authorities released a Strategy on International Cooperation in Cyberspace, which sets out four basic principles for international cooperation and China's six strategic goals: safeguarding sovereignty and security; developing international rules; protecting the legitimate rights and interests of citizens; promoting fair internet governance, digital economy and building a platform for cyber culture exchange.

China's Cybersecurity Law, which came into effect on 1 June 2017, provides additional national security review requirements and standards for companies engaged in or seeking to engage in network and data operations in China. **Legitimate security concerns related to cyber security should be addressed in a proportionate way**, which does not create unnecessary market access barriers, or trade restrictions on imported ICT products and services or deviate from WTO commitments.

China's Cybersecurity Law requires companies operating in critical service sectors, to store data domestically in China.

China's Cybersecurity Law already imposes stringent requirements on the transfer of data as it requires companies and their partners operating in critical service sectors, such as public communication and information services, power, traffic, water, finance, public services, electronic governance and other critical information infrastructure, to store domestically in China 'personal information and other important data' that is 'gathered or produced during their operations within mainland China'. Moreover, network operators are required to provide 'technical support for public security organs and state security organs for lawful activities preserving national security and investigating crimes'. The Law has a greater significance, as it goes beyond 'data security' and includes the protection of 'individual privacy'.

Network operators collecting and using personal information are required to obtain the consent of the person whose data is gathered.

Network operators collecting and **using personal information** are required to 'obtain the consent of the person whose data is gathered'. In the absence of consent, personal information should not be provided to others, although there are exceptions - albeit on the condition that that individual is unidentifiable and cannot be recovered. Infringing the privacy of personal information, can lead to suspension of business activities or fines (of a maximum RMB 1 million).

The Cyberspace Administration of China published a list of rules in August, with effect from 1 October 2017 requiring 'real-name' registration on bulletin boards. The regulation released of 2 May 2017, requires online news service providers and entities with foreign investment to go through a security review.

As of 31 March 2018, new rules came into effect, with regards to Virtual Private Networks (VPNs) in China.

As of 31 March 2018, new rules on Virtual Private Networks (VPNs) require companies and consumers to only use VPNs that are government approved/licenced. As the Ministry of Industry and Information Technology (MIIT) has no jurisdiction over companies operating overseas, the new rules appear to be aimed at the 'local Data Center, Internet Service Providers, Content Delivery Networks and other services'. It remains to be seen how these new rules may affect multinational enterprises operating in China. For example, in 2017 Apple had removed 674 VPNs from its store in China, citing compliance with government regulations. In August 2017, the Cyberspace Administration of China (CAC) ordered five websites, including a top online shopping platform, to remove vendors that offered access to VPNs.

China's action plan on artificial intelligence aims to upgrade its economy.

China has a separate development strategy for artificial intelligence (AI), published in July 2017. In addition, China published its **action plan on artificial intelligence 2018-2020** in December 2017, to upgrade its economy with AI as a main driving force. The three-year new AI plan, for 'Internet plus Artificial Intelligence', is expected to have roughly the same impact on the industry as the 'Made in China 2025' initiative has had on the manufacturing sector. China aims for a market of USD 15 billion in 2018 in the field of artificial intelligence.

7.7 Belt and Road Initiative (BRI)

The Belt and Road Initiative (BRI) is building China-sponsored infrastructure and connectivity links.

The Belt and Road Initiative (BRI), the international collaboration project for China-sponsored infrastructure and connectivity links, invests an estimated USD 150 billion a year. The BRI is a conceptual framework for policies that aim to increase economic integration within Asia, between Europe and Asia, and through (northern) Africa and the Middle East; via a variety of economic activities. The 'BRI' is a part of Beijing's ambitious and refocused **'Go Global strategy'.** Besides the connectivity and infrastructure projects, the BRI also aims to strengthen China's energy security by diversifying supplies and helping its overcapacity through additional access to export markets.

The BRI initiative serves many goals, including reducing China's problem of overcapacity.

China's official media in December 2017 stated that 86 countries and international organizations had signed 100 cooperation agreements with China under the BRI. Projects include building the China-Pakistan Economic Corridor, the Mombasa-Nairobi railway, construction of the Belgrade-Stara Pazova section of the Hungary-Serbia railway, and ports such as Khalifa in the United Arab Emirates, Hambantota in Sri Lanka and Piraeus in Greece .

In 2017, China's non-financial direct investment in countries along the 'Belt and Road' was USD 14.4 billion. The total volume of the newly signed projects was USD 144.3 billion, up 14.5 % from 2016. Large projects included the Ethiopia-Djibouti railway, the China-Laos railway; and the Colombo port city of Sri Lanka.

In 2017, 62 mergers and acquisitions in the countries along the 'Belt and Road' amounted to USD 8.8 billion. The biggest project was the China National Petroleum Corporation and China Energy Company Limited's joint acquisition of 12 % of Abu Dhabi's National Oil Company in the United Arab Emirates.

Figure 21:
The 'Belt and Road' initiative:
'Road' refers to ancient maritime routes between China and Europe, while 'belt' describes the Silk Road's better-known trails overland (see map)'.

Source: The Economist, http://www.economist.com/news/china/21701505-chinas-foreign-policy-could-reshape-good-part-world-economy-our-bulldozers-our-rules

'Polar Silk Road' though the Arctic

In June 2017, China published, 'A Vision for Maritime Cooperation under the Belt and Road Initiative' which refers to a blue economic passage envisioned to 'lead up to Europe via the Arctic Ocean'.

In June 2017, China published, 'A Vision for Maritime Cooperation under the Belt and Road Initiative', which indicates that the Ocean cooperation would focus on building the China-Indian Ocean-Africa-Mediterranean and China-Oceania-South Pacific sea blue economic passages. It also refers to a blue economic passage intended to 'lead up to Europe via the Arctic Ocean'. It includes China's participation in Arctic affairs, such as scientific surveys of navigational routes, setting up land-based monitoring stations, research on climatic and environmental changes, as well as providing navigational forecasting services. It also 'encourages Chinese enterprises to take part in the commercial use of the Arctic route'.

In the first official Chinese Arctic policy white paper, issued on 26 January 2018, China defines itself as a 'Near-Arctic State'.

The first official Chinese Arctic policy white paper, issued on 26 January 2018, acknowledges that sovereignty over Arctic area belongs to Canada, Denmark, Finland, Iceland, Norway, Russia, Sweden and the US, respectively. **China defines itself as a 'Near-Arctic State'**, i.e. one of the continental States that are closest to the Arctic Circle. China's strategy promotes its **vision of a 'Polar Silk Road' through the Arctic**, and across the Japanese straits. The Chinese Arctic Strategy is assertive, stating for example that 'While pursuing its own interests, China will pay due regard to the interests of other countries and the broader international community ... '

The 'Polar Silk Road' is the third pillar of the flagship BRI, designed to connect China to Europe and beyond via the Arctic region.

The **'Polar Silk Road' is the third pillar of the flagship 'Belt and Road Initiative'** (see map below). Despite the fact that the Arctic region is rich in natural resources such as iron ore, coal and precious metals, opportunities offered in the transport sector have become more prominent than mining, due to high costs of exploiting natural reserves in the Arctic. Both, the Northern Sea

Route (over the Russian coast) and the North West Passage (throughout the Canadian archipelago) are of strategic importance. But the Northern Sea Route, which stretches roughly from Murmansk in the west to the Bering Strait in the east, has become the focal point of both Russia and China's Arctic strategies.

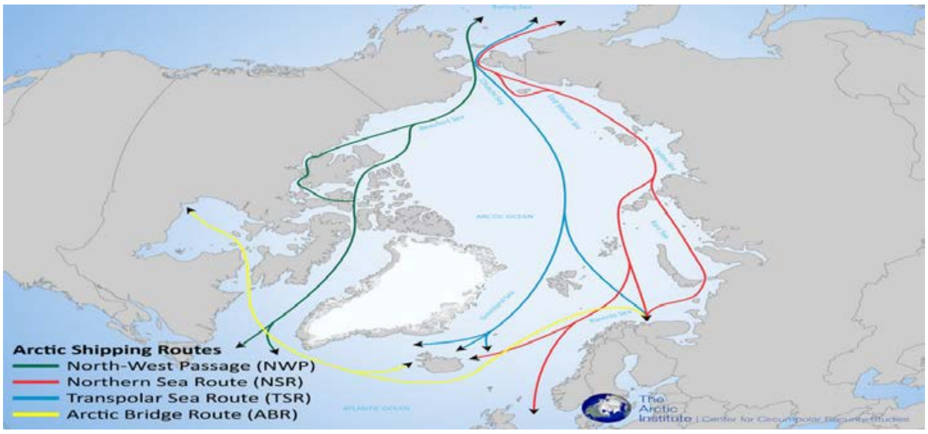
Since the Chinese president visited Russia in July 2017, the two countries have further enhanced cooperation on the 'Polar Silk Road'.

Since a visit by Chinese President Xi Jinping to Russia in July 2017, the two countries have further enhanced cooperation on the 'Polar Silk Road', as well as on the BRI, notably in the energy sector, cargo shipping and the development of a Northeast Arctic underwater fibre optic telecommunications cable (Arctic Connect). Russia issued new rules in 2017 stipulating that only Russian vessels, may ship energy resources through the Northern Sea Route. Russia considers the Northern Sea Route to be its internal waters, under Article 234 of the United Nations Convention on the Law of the Sea (UNCLOS).

References to UNCLOS in China's White Paper aim to back up China's rights to exploration and navigation in the Arctic.

Meanwhile, China has been conducting its own scientific research with the aim of learning more about environmental protection and navigation security in the Arctic. References to UNCLOS in China's White Paper aim to back up China's rights to exploration and navigation in the Arctic. China also intends to launch tests of the icebreaker capability for shipping operations of in the Arctic waters.

Figure 22:
Artic Shipping routes (Yale University)



Source: Polar trade routes (Yale University); the Global Construction Review, January 2018.

8 Foreign and security policy issues

8.1 Global and regional security

China has become more ambitious and assertive, seeking to 'regain its rightful place in the world'. And its foreign policy is also assuming a more confident, multi-dimensional stance.

Foreign policy has largely remained an instrument to underpin domestic issues, the role of the Communist Party and economic growth. Under President Xi's rule, China has become more ambitious and assertive, seeking to 'regain its rightful place in the world'. Its foreign policy is also assuming a more confident, multi-dimensional stance.

China has acknowledged the growing global responsibilities and obligations, which come with 'major country' status, including the chairmanship of the G20 in 2016. Following the 19th CPC Congress, China promotes a 'new type of international relations', based on 'win-win' cooperation and emphasising the central role of the United Nations, including the UN Security Council resolutions.

China is building regional security architecture, along the

China is building regional security architecture. The Sea Lanes of Communication (SLOCs), a term describing the primary maritime routes between ports, used for trade, logistics and naval forces, represents a major strategic plan of China -

Sea Lanes of Communication (SLOCs).

beyond piracy, as it includes access to Middle East natural resources, as well as its main trade partners in Europe and Africa. In 2017, China also formally opened its first overseas military base in Djibouti.

South China Sea Dispute

In a case filed by the Philippines against China, UNCLOS ruled against China in the South China Sea dispute.

The importance of the South China Sea dispute has recently come to the forefront, along with China's assertive behaviour in its maritime periphery. The UN Permanent Court of Arbitration for the UN Convention on the law of the Sea (UNCLOS) ruled on 12 July 2016 in a case filed by the Philippines against China that the specific portion of the South China Sea claimed by both China and the Philippines belongs to the Philippines alone. On 10 April 2018 President Xi Jinping and Philippine counterpart Rodrigo Duterte divulged closer relations between the two countries, as Beijing pledged USD 73 million in economic and infrastructure aid and new ideas for maritime security.

The EU supports the swift conclusion of an effective Code of Conduct between ASEAN and China on the Conduct of Parties in the South China Sea.

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. The Framework of the Code of Conduct in the South China Sea was adopted by the Foreign Ministers of ASEAN Member States and China in August 2017. A first draft of a Code of Conduct (COC) on the South China Sea was issued by ASEAN and China in 2017. China and the ASEAN consultations on the Code of Conduct in the South China Sea were scheduled for March 2018 have not taken place. There seem to be differences, such as on whether to limit the applicability of the code of conduct to the Spratly archipelago, or to also include the Paracels and Scarborough Shoal. Another aspect applying the UNCLOS is whether Southeast Asian states would have the right to exploit the oil, gas and fish resources off their coasts.

China established a new 'cooperation mechanism', with Philippines and the coastal states of the South China Sea in 2017.

In 2017, China pushed the coastal states of the South China Sea to establish a new 'cooperation mechanism'. The 2nd meeting of the China-Philippines bilateral consultation mechanism on 13 February 2018 stated some positive developments in the South China Sea, such as:

- ✓ access to fishermen within the disputed areas;
- ✓ measures taken to protect the environment and marine ecosystem in the South China Sea; and
- ✓ a commitment by China and all parties not to build on uninhabited features in accordance with the Declaration of Conduct on the South China Sea.

In May 2018, however, the Philippines warned China that 'it will go to war over natural resources in the South China Sea'.

Figure 23:
South China Sea: Chinese claims and disputed islands

Source: *Global Security, CSIS, 30.3.2018*

China-Japan: East China Sea dispute

China is involved in another dispute, in the East China Sea, which complicates its relations with Japan.

Ties between China and Japan have sparred over 40 years due to a territorial dispute over a set of small, uninhabited islands in the East China Sea, called 'Senkaku' by the Japanese and 'Diaoyu' by the Chinese. The two nations have, however, sought to improve ties more recently. Following rising tensions in 2017 between China and Japan over the contested islands, the US and Japanese leaders affirmed in the joint US-Japanese statement that Article V of the US-Japan Treaty of Mutual Cooperation and Security covered the 'Senkaku' Islands and that they would deepen cooperation to safeguard the peace and stability of the East China Sea. On 11 January 2018 the Japanese government lodged an official protest at the entry of a Chinese submarine into the 24-nautical-mile (44 km) contiguous zone east-northeast of Miyako Island near Japan's territorial waters, around the 'Senkaku' Islands in the East China Sea.

China in Central Asia

China is increasingly involved in Central Asia because of security concerns, which also relate to part of its own territory.

China has emerged as a significant player in Central Asia, aiming to gain access to energy resources and new export markets for Chinese goods and to enhance connectivity (and support for the 'Belt and Road' initiative). Security plays an increasingly important role in China's policy towards Central Asia. China is reportedly building a military base on the Tajik–Afghan border, given its concerns regarding possible Muslim radicalisation in the region, potential spill-over of radical elements in restive Xinjiang or negative influence over groups like the East Turkestan Islamic Movement (ETIM).

The Shanghai Cooperation Organisation

China considers the Shanghai Cooperation Organisation (SCO) as a primary instrument for consultations to reinforce Central Asian security.

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 'BRI'. In June 2016, the Council of the Heads of State of the SCO signed the Tashkent Declaration on the 15th Anniversary of the SCO; approved a 5-year action plan (2016-2020) on Implementation of the SCO Development Strategy Towards 2025, and adopted the Memorandums of the Obligations on the Entry of India and Pakistan to the SCO.

The 18th SCO summit in June 2018 recognised a special role of the SCO regional counter-terrorist agencies in jointly combating terrorism, separatism and extremism, and safeguarding regional security.

The Declaration of the 18th SCO summit on 10 June 2018 recognised a special role of the SCO regional counter-terrorist agencies in jointly combating the 'three evil forces' of terrorism, separatism and extremism, and safeguarding regional security. Particular emphasis was given to the 5-year Plan for the implementation of the 'Treaty on Long-term Good Neighbourliness, Friendship and Cooperation' of the SCO Member States. A joint communication of the Head of States of the SCO on 'Simplifying Trade Procedures' also highlights the importance of the joint efforts to support and strengthen the multilateral trade system based on the standards and principles of the WTO. The Kyrgyz Republic took over the Presidency until 2019.

In the margins of the 18th SCO summit on 9 June 2018, President Xi and his Russian counterpart agreed to promote greater development of China-Russia relations towards a comprehensive strategic partnership.

In 17 May 2018, China signed an economic and trade cooperation agreement with the Eurasian Economic Union (EAEU).

On 17 May 2018 China signed an economic and trade cooperation agreement with **the Eurasian Economic Union** (EAEU) (established in 2015 between Russia, Kazakhstan, Belarus, Armenia and Kyrgyzstan), which is expected to promote integration of China's BRI with the EAEU framework. The agreement covers 13 aspects such as customs cooperation, trade facilitation, intellectual property rights, sectoral cooperation and government procurement, e-commerce and competition.

8.2 China - ASEAN relations

The white paper entitled 'China's Policies on Asia-Pacific Security Cooperation' outlined priorities to improve the existing regional multilateral mechanisms and strengthen the framework for supporting peace, security and stability in the Asia-Pacific region.

The Philippines assumes the coordination of the Association of South-East Asian Nations (ASEAN)-China Dialogue Relations in August 2018 (while, on 1 November 2017, Singapore took over ASEAN's rotating chair for 2018).

The white paper entitled 'China's Policies on Asia-Pacific Security Cooperation', released in January 2017 by China's Foreign Ministry, outlined priorities to improve the existing regional multilateral mechanisms and strengthen the framework for supporting peace, security and stability in the Asia-Pacific region.

ASEAN and China continue to strengthen

China and ASEAN joint statement at the 20th ASEAN-China Summit on 13 November 2017 states that they continue strengthen their strategic partnership through implementation of the 2016-2020 Plan of Action in a wide range of political-security, economic, and socio-cultural areas. ASEAN Leaders and China also agreed continue to endeavour to resolving pending issues under the Framework Agreement on Comprehensive Economic Co-operation and their strategic partnership through the effective implementation of the 2016-2020 Plan of Action.

Certain Agreements (ACFTA), in order to ensure greater economic and trade cooperation, and to address with urgency the long-standing issue concerning iron and steel.

The 11th Joint Commission on China-ASEAN FTA (also known as CAFTA), signed in November 2002, was held on 13-15 March 2018. China was ASEAN's largest trading partner with total two-way trade reaching USD 515 billion, 13.8 % up from 2016. Chinese exports to ASEAN countries accounted for USD 279.1 billion, an increase of 9 % from 2016. While Chinese imports grew 20 % in 2017 from 2016, to USD 236 billion.

The joint Communique refers to China's support to explore synergies between ASEAN Connectivity 2025 plan and the Belt and Road Initiative.

The joint Communique refers to China's support for the Master Plan on ASEAN Connectivity (MPAC) 2025 and ongoing efforts to explore synergies between ASEAN's MPAC 2025, China's Belt and Road Initiative, including deepening the cooperation on infrastructure connectivity, through the Asian Infrastructure Investment Bank (AIIB) and the Silk Road Fund.

8.3 The Korean Peninsula

China considers the achievement of a stable, peaceful settlement and denuclearisation of the Korean Peninsula as an important goal, and continued to support the United Nations' (UN) constructive role and the UN Security Council's strong condemnation of the North Korea's nuclear weapons programme.

The North Korean leader's, unpredicted visit to Beijing from 26 to 28 March 2018, was intended to re-establish relations between North Korea and China.

The North Korean visits to China were also significant due to the North Korea-US Summit that took place in May 2018.

The summit between North Korean and South Korean Presidents covered the denuclearisation of the Korean peninsula.

The re-engagement between China and North Korea serves as a reminder of Beijing's influence when dealing with North-Korean-related issues.

The North Korean leader, Kim Jong-Un, made an unpredicted visit to Beijing from 26 to 28 March 2018, the first official visit to China since he became leader in 2011. Talks between the two leaders were intended to re-establish relations between North Korea and China, and also covered the denuclearisation of the Korean peninsula. Kim Jong-Un is assumed to have expressed his willingness to engage in talks with the international community as part of the process towards resolving tensions on the Korean peninsula. Beijing has continued to advocate for the resumption of the Six Party Talks, the multilateral framework aimed at denuclearising North Korea.

The diplomatic move was also viewed as an opportunity for North Korea to prepare its stance, notably on the denuclearisation of the Korean peninsula, for the summit with the South Korean President Moon Jae on 27 April 2018. The historic one-day summit in Panmunjom resulted to a joint 'Declaration for Peace, Prosperity and Unification of the Korean Peninsula' and marked the first time that North Korean Leader set foot in the South Korea, since the end of the 1950-53 Korean war. As a peace treaty was never signed, the two nations technically remain in a state of war.

The North Korean Leader made the 2nd surprise visit to meet Chinese president on 8 May 2018, ahead of the North Korea-US summit that took place on 12 June 2018 in Singapore. In the Joint Statement of the two Leaders recognised an establishment of new US-North Korea relations; joint efforts to build a lasting and stable peace regime on the Korean Peninsula and the South Korea 'committed to work toward complete denuclearization of the Korean Peninsula'. Following the summit, the US suspended military exercises with

South Korea, which was seen as a major success for North Korea and its allies, China and Russia.

Kim Jong-un met with Chinese President on 19 June 2018, during his third visit to China, in which discussions are expected to cover the outcome of the recent summit between North Korea and the US. The re-engagement between China and North Korea serves as a reminder of Beijing's influence when dealing with North-Korean-related issues. China is by far North Korea's most important trading partner and main source of food and energy. In 2016 North Korea's trade grew by about 5 %, with China accounting for around 93 % of North Korea's overall trade. China's largest imports from North Korea were coal and mineral fuel, which rose to USD 1.2 billion in 2016, up 12 % from the previous year. In the first three quarters of 2017, Chinese imports from North Korea actually fell by 16.7 %, though exports were up by 20.9 %. In January 2018, trade levels fell once more to their lowest levels since 2014, accounting for USD 216 million (down 52 % from 2017), as China has strived to keep implementing sanctions in line with the UN resolutions on North Korea. On 12 June 2018, following the US-North Korea summit, China suggested that sanctions relief could be considered for North Korea as Kim Jong Un had pledged to work toward complete denuclearisation of the Korean peninsula.

One major issue within China-US relations *vis-à-vis* the Korean Peninsula has been the deployment of the Terminal High Altitude Area Defence (THAAD) system. China's concerns are that a Japan-US-South Korea military alliance (a miniature Asian version of NATO) would be reinforced through THAAD's development.

8.4 China-US relations

The US-China relationship is strained by a number of underlying security and trade issues.

Despite the personal rapport displayed by President Trump and his Chinese counterpart, Xi Jinping at two bilateral summits (April and November 2017), the US-China relationship is strained by a number of underlying security and trade issues, highlighted by the suspension of a major bilateral economic dialogue.

On 18 December 2017, the US government released a revised National Security Strategy, in which China (alongside Russia) is labelled as a 'revisionist power'.

On 18 December 2017, the US government released a revised National Security Strategy (NSS), in which China (alongside Russia) is labelled as a 'revisionist power'. The NSS outlines geopolitical and economic issues facing the US in the international arena, stating notably that 'China seeks to displace the US in the Indo-Pacific region', and that 'China (and Russia) target their investments in the developing world to expand influence and gain competitive advantages against the US'.

Recent developments in bilateral China-US trade relations include increased tariffs on steel and aluminium and trade sanctions valued at USD 50 billion.

China's a record high trade surplus of USD 375.6 billion in 2017 with the US, increased tensions further. **Recent developments in bilateral China-US trade relations** (see Annex 1) include, President Trump's proclamation imposing additional tariffs on steel (25 %) and aluminium (10 %), based on Section 232 national security justifications on 8 March 2018; and the US' sanctions (including raising tariffs by 25 % on selected Chinese products valued at USD 50 billion), announced on 22 March 2018, against China over its technology transfer practices, industrial policies (such as the 'Made in China 2025' initiative), excess capacity, and restrictive cyber-security measures. On 19 June 2018 the US President requested to identify USD 200 billion worth of Chinese products for additional 10 % tariffs to address China's harmful trade policies and practices.

The '100-day action plan on trade' at the US-China Comprehensive Economic Dialogue in July 2017 resulted China to allow imports of US beef.

The '100-day action plan on trade' at the US-China Comprehensive Economic Dialogue in July 2017 resulted in measures to expand opportunities for US companies in China and made progress on issues, including credit rating and electronic payment services, commercial banking, and liquefied natural gas as well as market access. Moreover, for the first time since 2003, China allowed imports of US beef, on certain conditions, as from 16 July 2017.

On 12 December 2017, the trade ministers of the United States and Japan, with the EU trade commissioner, issued a joint statement on a 'Global Level Playing Field'.

On 12 December 2017, the trade ministers of the United States and Japan, with the EU trade commissioner, issued a joint statement at the WTO, in an apparent reference to China, expressing concerns over 'severe excess capacity in key sectors exacerbated by government-financed and supported capacity expansion, unfair competitive conditions caused by large market-distorting subsidies and state owned enterprises, forced technology transfer, and local content requirements and preferences'.

China is the largest holder of the US Treasury Securities, ahead of Japan and Ireland.

In May 2017 China regained its position as the largest holder of the US debt - or treasuries issued by the US Treasury Department, from the second largest holder which is Japan. As of April 2018 the US debt (totalling USD 6.17 trillion in treasury bills, notes, and bonds) owed by China amounted to USD 1.18 trillion (19 %), followed by Japan (17 %), Ireland (5 %), Brazil (5 %) and United Kingdom (4 %).

9 Multilateral cooperation

9.1 Asian Infrastructure Investment Bank

The Asian Infrastructure Investment Bank is seen as an alternative bank, in which China will play a dominant role in international lending, in pursuit of its geostrategic interests and accelerating its 'Belt and Road' initiative.

China is a founding member of the Asian Infrastructure Investment Bank (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 86 countries, including 16 EU Member States (and 14 G20 countries), have signed for membership of the AIIB. 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 share, and non-regional members. China's voting share (26.9 %) is substantially larger than the second-largest AIIB member, India, which holds (7.7 %). Russia is the third largest, with a 6.1 % voting share. The AIIB is seen as an alternative bank (e.g. to the World Bank and International Monetary Fund), 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 'Belt and Road' initiative (BRI)**. The AIIB has, however, formed partnerships with some key global institutions, including the World Bank, the European Bank for Reconstruction and Development and the European Investment Bank. The AIIB has, so far, invested around USD 4.3 billion in 25 projects, including energy, environment protection, urban development and transport sectors in China ('Beijing Air quality improvement and coal replacement project'), Pakistan (2), Oman (2), Bangladesh (3), India (6), Indonesia (3), Georgia (1), Philippines (1), Egypt (1), Tajikistan (2), Myanmar (1) and Azerbaijan (1). The AIIB has also invested in the International Finance Corporation Emerging Asia Fund.

9.2 Emerging market bloc of BRICS

In 2017 China held the rotating chair of the emerging-market bloc of BRICS.

China, which held the rotating chair of the emerging-market bloc of BRICS (Brazil, Russia, India, China and South Africa) in 2017, hosted the ninth BRICS Leaders' summit in September 2017, which reduced tensions in the Sino-Indian border dispute. The Xiamen Summit Declaration covers a large number of international security issues; provides a roadmap for boosting cooperation among developing countries; and upholds a fair and equitable international order based on the central role of the United Nations. The Leaders welcomed the first report on the implementation of Strategy for BRICS Economic Partnership. China continues to play a key role in the BRICS-backed New Development Bank (NDB), which opened in Shanghai in July 2015. In the margins of the BRICS summit in September 2017, the NDB and the BRICS Business Council signed a Memorandum of Understanding on Strategic Cooperation. South Africa, the rotating chair of the BRICS in 2018, has scheduled the annual BRICS Summit to take place on 25-27 July 2018.

9.3 China and Africa

China has become a strategic business and economic partner for Africa.

China has grown to be a **strategic business and economic partner of Africa**. Since 2000, China has emerged as Africa's **largest trading partner and a major source of investment finance** as well. According to the China Customs, in 2017 the total China-Africa trade amounted to USD 170 billion, up 14.1 % from 2016. China's exports to Africa reached USD 94.74 billion, up 2.7 %; and China's imports from Africa reached USD 75.26 billion, showing trade surplus of USD 19.48 billion, down 45.2 % from 2016. Over 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**. The Forum on China-Africa Cooperation summits, held at three-year intervals, is scheduled for September 2018 in Beijing. The China-Africa Industrial Capacity Cooperation Fund started operations in January 2016, with the USD 10 billion start-up capital from the Chinese government. After 18 months of formal operation, the fund only approved six projects with a total investment of USD 542 million.

The 10th Round of China-EU Consultations on African affairs was held on 23 February 2018.

On 23 February 2018, the 10th Round of China-EU Consultations on African affairs was held in Brussels.

Annex 1: US tariffs measures

The US measures under sections 232 on steel and aluminium

According to the two US presidential orders of 8 March 2018, issued on the grounds of national security under **Section 232** of the US Trade Expansion Act of 1962, the US imposes additional ad-valorem import tariffs on steel (25 %) and aluminium (10 %), worldwide, including China (besides those temporarily exempted[3]) as of 23 March 2018. These US' additional tariff measures on the EU's steel and aluminium imports were suspended until 1 May 2018, subject to 'a satisfactory long-term alternative means to address the threatened impairment to US national security'. This exemption was extended until 1 June 2018, from when the tariffs on imports from the EU were automatically applied. The Presidential Proclamations of 31 May 2018 adjusted tariffs on imports of steel and aluminium into the US effective worldwide (except otherwise provided, including quantitative limitations[4] and subject to 'a satisfactory alternative means to address the threat to the national security'). In the meantime high-level negotiations between Washington and China continues. On 19 May 2019, US Secretary of Treasury Steve Mnuchin meekly announced that US and China were 'putting the trade war on hold', while the talks in early June 2018 led by the US Commerce Secretary, Wilbur Ross ended in an impasse.

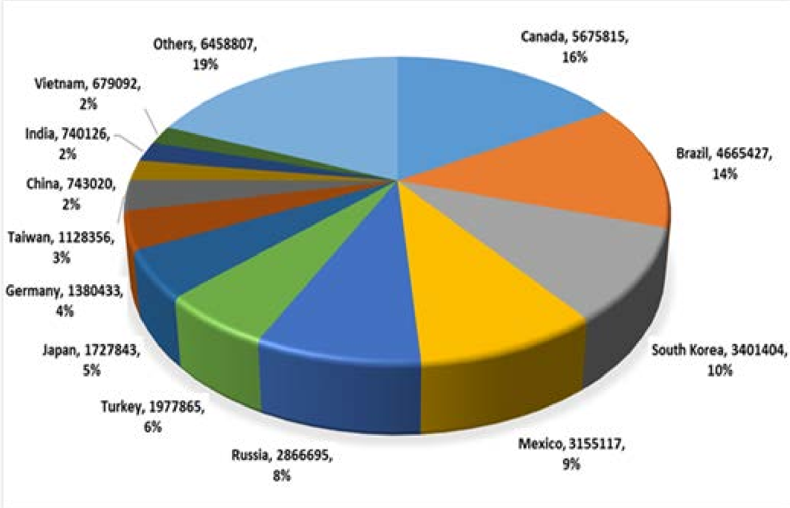
Both, the EU and China are pursuing so-called 're-balancing measures' under the provisions of the World Trade Organisation (WTO) General Agreement on Tariffs and Trade (GATT) 1994, and of the Agreement on Safeguards, since the US measures are considered to be safeguards 'in disguise'. On 9 April 2018 China has requested consultations under the WTO Dispute Settlement (case DS544) procedure with respect to US tariffs on steel and aluminium. On 29 March 2018 China notified the WTO of such 're-balancing measures' (disregarding certain conditions, such as a 30-days waiting period putting such measures into effect under WTO rules) in response to the US Section 232 tariff actions on certain imports of steel and aluminium products. China's list tentatively contains 128 products across 7 categories, with an estimated value of US exports to China of some USD 3 billion (2017).

On 18 May 2018 the EU notified the WTO Council for Trade in Goods of the proposed suspension of concessions and other obligations as from 20 June 2018 on the basis that the US failed to notify the WTO Committee on Safeguards under Article 12.1(c) on taking a decision to apply safeguard these tariff measures.

On 6 June 2018, the EU decided to exercise its rights to rebalancing on US products, corresponding the list of products notified to the WTO on 18 May 2018, the damage (worth in total EUR 6.4 billion, 2017) caused by the US measures on steel and aluminium products, corresponding EUR 2.8 billion of trade. The remaining rebalancing on trade valued at EUR 3.6 billion will take place at a later stage – within three years' time or after a positive finding in WTO dispute settlement if that should come sooner. The EU considers that 'Section 232 of the Trade Expansion Act of 1962, as amended (19 U.S.C. §1862), as repeatedly interpreted by the United States' administrative and judicial authorities in the above and other measures, is 'as such' inconsistent with the United States' obligations and rights set out in the WTO Agreement'. The launch of legal proceedings against the US in the WTO (case DS548 of 1 June) also leaves a possibility of initiating of safeguard action to protect the European market from disruptions caused by the diversion of steel from the US market. As regards aluminium, the Commission has put in place a surveillance system for imports of aluminium to monitor trade flows and be prepared in case action is required in that sector.

[3] Canada, Mexico, Australia, Argentina, South Korea, Brazil and the European Union.
[4] As of 1 June 2018 additional tariffs on steel apply to all countries of origin except Argentina (quota), Australia, Brazil (quota), and South Korea (quota), and on aluminium to all countries of origin except Argentina (quota) and Australia.

Figure 24: US steel imports in 2017 (in metric tons and percentage)



Source: Global Steel Trade Monitor, US Department of Commerce, March 2018; Statista

The China-targeted US' measures

On 22 March 2018 the US President signed a memorandum under **Section 301** of the US Trade Act 1974, announcing initial tariffs (of 25 %) effective within 15 days of the date of the memorandum on a list of Chinese goods imports (around 1 300 tariff lines) that are valued to some USD 50 billion in view of 'rebalancing' the US-China trade relationship. On 4 April 2018, the USTR issued a notice for the proposed action with the list of 'retaliation measures' for public comment with a deadline of 11 May 2018.

This follows the US investigation, announced in August 2017 on the basis of a Presidential memorandum of 14 August 2017, which examined whether China's laws, policies, practices, or actions may be unreasonable or discriminatory and could be harming American intellectual property rights, innovation, or technology development (under Section 301 of the 1974 Trade Act (19 U.S.C. § 2411)). The US' findings of the investigation (of 22 March 2018), concluded that China's market practices contribute to an unfair playing field as the Chinese government targets foreign technology, digests and absorbs it through joint ventures and other investment restrictions, discriminatory licensing requirements, state supported and led outward investment generating large-scale technology transfer, cyber theft and other means (notably, the way Chinese legislation on cybersecurity, IPR or competition is enforced). The US' findings refers to China's 'Made in China 2025' strategy, which expressly calls for China to raise 'self-sufficiency' to 40 % by 2020, and to 70 % by 2025, in core components and critical materials in a wide range of industries, including aerospace equipment and telecommunications equipment.

The US initiated consultations in the WTO (DS542) with China, under the WTO's Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs) on 26 March 2018. Such consultations are the first step in the WTO dispute settlement process. If the US and China are unable to reach a solution through consultations, the US may request the establishment of a WTO dispute settlement panel to review the matter. On 4 April 2018, China requested consultations (DS543) with the US concerning US' tariff measures on certain Chinese goods under Section 301-310 of the US Trade Act of 1974.

First, on 4 April 2018, the EU made the request (WT/DS542/3) to join as a 'third party' as stated in the WTO rules on the US dispute settlement consultations (DS542), due to a 'substantial trade interest' in the matter. Also Japan, Ukraine, Saudi Arabia and Chinese Taipei have joined the US consultations in the WTO on China. Subsequently, on 6 June 2018, the EU requested its own WTO consultations (DS549) concerning certain

Chinese measures, which the EU alleges as inconsistent with China's obligations under the WTO's Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs).

The US made requests to China such as cutting tariffs on a list of products, identified as benefiting from Chinese industrial policies. The draft list went through the notice and comment process, including a public hearing of the US' Section 301 Committee on 15 May 2018, leaving interested parties to file until 23 April 2018. The increase in duties can only apply on the basis of the finalised list, which is expected to be issued in June 2018.

Moreover, President Trump has directed the USTR to determine if an additional USD 100 billion worth of tariffs would be appropriate under Section 301 for Chinese goods imports. Any additional tariffs would be subject to a similar review and public comment period. In addition to the tariff announcements on 6 April 2018, the US has initiated a WTO dispute against China for its unfair practices, including the forced transfer of US' technology and theft of US intellectual property.

On 17 and 18 May 2018, the US and China engaged in consultations regarding trade and issued a joint statement. The third round of trade consultations on 2 and 3 June 2018 between China and the US focused on reducing the US' trade deficit by facilitating the supply of agricultural and energy products to meet China's growing consumption needs. The US runs a trade deficit with China of USD 375 billion on trade in goods, and estimates according to one study that the cost of counterfeit goods, pirated software and theft of trade secrets could be as high as USD 600 billion.

On 29 May 2018 the US announced investigation on automobiles under Section 232, (e.g. the US has a 2.5 % tariff on Chinese cars, while China currently maintains a 25 % tariff on US' cars). On 19 June 2018 the US President requested to identify USD 200 billion worth of Chinese products for additional 10 % tariffs to address China's harmful trade policies and practices. The US is also expected to announce by 30 June 2018 specific investment restrictions and enhanced export controls for Chinese persons and entities related to the acquisition of industrially significant technology, which would be implemented shortly thereafter.

The Trump administration barred Chinese telecom giant Zhongxing Telecommunications Equipment Corporation (ZTE) from purchasing parts from US companies in April 2018. Following the ban, President Trump abruptly tweeted on 13 May 2018 that he wanted to help get ZTE 'get back into business' as part of broader trade negotiations with Beijing. Under the new agreement of 7 June 2018, ZTE was obliged to pay USD 1 billion and place an additional USD 400 million in suspended penalty money in escrow before the company would be removed from the Denied Persons List. These penalties are addition to the USD 892 million that ZTE already paid for allegedly violating US sanctions by dealing with North Korea and Iran under the March 2017 settlement agreement. The US Commerce Department pronounced further action in 2018, 'because the company tried to mislead regulators and did not discipline the employees involved'. ZTE is also required to retain a team of special compliance coordinators selected by and answerable to Bureau of Industry and Security for a period of 10 years. This new settlement agreement sets another record, and brings the total penalties assessed on ZTE to USD 2.29 billion. The US Senate, however, approved a defence bill, the National Defence Authorization Act, on 18 June 2018 that would likely reinstate a ban on US companies selling parts to ZTE, and could ban US government agencies from buying or leasing telecom equipment and services from ZTE and another Chinese telecom firm, Huawei.

Rather than individual countries (i.e. the US) taking unilateral measures or other actions to manage trade flows, the EU supports the rules-based multilateral WTO system that addresses the root cause of the problems in these two sectors, i.e. global overcapacity largely caused by non-market-based production, notably Chinese.

Annex 2: China: Key economic and social indicators

Key Economic Indicators
China ranked 27th (out of 137 economies) in the Global Competitiveness Index (2017-2018) a move up from 28th the previous year. China's position is ahead of several EU Member States such as Estonia (29), Czech Republic (31), Spain (34), Malta (37) and Poland (39), while Taiwan is in 15th place.
China ranked 26th in the ranking of emerging economies (out of 103 economies) with a score of 4.09 in 'The Inclusive Growth and Development Report 2018'. China also performed well in terms of growth and development (9th). Its Gini coefficient has increased from less than 30 in the early 1980s to 51 in 2018.
China ranked 78th (out of 190 economies) overall in the World Bank's Ease of Doing Business report 2018 with a score of 65.29. China performed well in terms of enforcing contracts (5th) but particularly weak in terms of starting a business (93rd). For receiving electricity, the country has a high cost (356 % of income per capita).
China ranked 77th (out of 180 countries) with a score of 41 in the Corruption Perceptions Index 2017.
In the 2018 Financial Secrecy Index, established by the Tax Justice Network, **China ranked 28th** (out of 112 countries). China accounts for less than 1 per cent of the global market for offshore financial services, making it a small player compared with other secrecy jurisdictions.
China remains **'not free'** as it **ranked 110th** (out of 180 countries) in the Heritage Foundation's 2018 Index of Economic Freedom, with an overall score of 57.8. Its overall score has increased by 0.4 points, with higher scores for government integrity and judicial effectiveness more than balancing declines in fiscal health, labor freedom, and property rights. China is ranked 24th among 43 countries in the Asia–Pacific region, and its overall score is below the regional and world averages.
In the World Bank's Digital Adoption Index of 2016, **China scored 0.62 out of 1**, lower than Germany and the United States (0.78), but higher than Bulgaria and Cyprus (0.59). China scored highest in people indicator (0.77), with mobile access at home (97 %) and internet access at home (54 %).
In the 2016 OECD FDI Regulatory Restrictiveness Index, which measures statutory restrictions on foreign direct investment across 22 economic sectors in 62 countries worldwide, **China ranked as the 4th** most closed economy (out of 62 economies), with a score of 0.327 (scale of 0-1) - significantly higher than the OECD average of 0.067.
Key Social Indicators
China ranked 90th (out of 188 countries) with a score of 0.738 in the UN Human Development Index 2016. China's HDI value is higher compared to the East Asian and Pacific countries' average (0.720).
China ranked 130th (out of 159 countries) with a score of 6.01 in the 2017 Human Freedom Index (HFI). China ranked 136th in terms of personal freedom (a score of 5.62); and of economic freedom 112th, (a score of 6.4).
Labour Market
According to the Statistica: The Statistics Portal the number of unemployed persons was at 3.9 % of the labour force population in December 2017, a decrease from 4.02 % from the previous year.
According to the World Bank Data, **female participation in the labour market was 61 %** (% of female population ages 15+) in 2017.
Also according to World Bank Data, the GDP per person employed (constant 2011 PPP USD) in China in 2016 was 27,196.

Annex 3: China: Free Trade Agreements

Signed and in effect (date of entry into force)	Under negotiation	Under consideration
China - **Australia** FTA (20 December 2015)	China - **Israel** FTA	China - **Bengal** FTA Joint Feasibility Study
China - **Chile** FTA (1 October 2006)	China - **Japan - Korea** FTA	China - **Canada** FTA Joint Feasibility Study
China - **Costa Rica** FTA (1 August 2011)	China - **Maldives** FTA (signed but not yet in effect: 7 December 2017)	China - **Columbia** FTA Joint Feasibility Study
China - **Georgia** FTA (1 January 2018)	China - **Mauritius** FTA	
China - **Iceland** FTA (2 July 2014)	China - **Moldova** FTA	China - **Fiji** FTA Joint Feasibility Study
China - Republic of **Korea** (20 December 2015)	China - **Norway** FTA	China - **Mongol** FTA Joint Feasibility Study
China - **New Zealand** FTA (1 October 2008)	China - **Sri Lanka** FTA	China - **Nepal** FTA Joint Feasibility Study
China - **Pakistan** FTA (1 July 2007)		China - **Palestine** FTA Joint Feasibility Study
China - **Peru** FTA (1 March 2010)	China - **Eurasia**n Economic Union FTA (1 October 2017)	China - **Panama** FTA Joint Feasibility Study
China - **Switzerland** FTA (1 July 2014)	China - **GCC** (Gulf Cooperation Council) FTA	China - **Papua New Guinea** FTA Joint Feasibility Study
China - **Thailand** FTA (October 2003)	Regional Comprehensive Economic Partnership (RCEP)	China - **Peru Upgrade** FTA Joint Feasibility Study
	China - **Southern Africa**n Customs Union FTA	China - **Switzerland Upgrade** FTA Joint Feasibility Study
China - **Hong Kong** Closer Economic Partnership Arrangement (1 January 2004)		
China - **Macao** Closer Economic Partnership Arrangement (1 January 2004)		
China - **Singapore** FTA (1 January 2009)		
China - **Taipei** Economic Cooperation Framework Agreement (12 September 2010) **Asia** Pacific Trade Agreement (APTA) (17 June 1976)		
China - **ASEAN** Comprehensive Economic Cooperation Agreement (1 July 2005)		

Annex 4: China's Social Credit System. A new tool for stricter controls ?

The Social Credit System (SCS) is an initiative proposed by the Chinese government with a view to developing a national social credit rating system by 2020. On 14 June 2014, the Chinese government released a planning outline for the construction of a social credit system (2014-2020). This outline refers to the SCS as a 'necessary condition to deepen international cooperation and exchange, establishing international brands and reputations, reducing foreign-related transaction costs, and improving the country's soft power and international influence ... .'

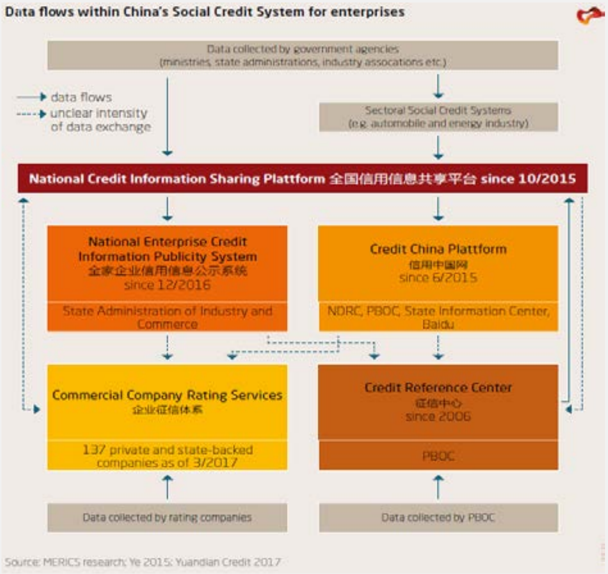
Under the proposed SCS, individuals will be rated on a 'range of areas', which leaves room for interpretation of how broadly people will be assessed. Areas for assessment include activities such as administrative affairs (e.g. blacklist systems for legal violations concerning taxation and housing), commercial activities (e.g. e-commerce, recruitment and government procurement activities) and measures regarding an individual's ability to comply with legal requirements, and their social behaviour. The SCS is intended to incorporate central and local government data, data from industry associations and data from commercial rating services into a nationwide database platform overseen by the central government. The data will include the economic domain as well as the social, environmental and political fields. The introduction of the Social Credit System has been fast-tracked: the report indicates that these new rules would come into effect nationwide by mid-2018, when it was announced that a total of 33.99 million credit codes were issued to newly registered businesses.

The fast-tracked implementation of the SCS system seems already to have taken effect for establishing the **creditworthiness** of individuals. The Financial Times reported in October 2017 that the big e-commerce companies are obliged to share their data with central authorities, such as the People's Bank of China (PBoC). The PBoC shares the data with state-owned banks to create a data base establishing the creditworthiness of individuals. The rating of individuals' creditworthiness is to be assessed by companies operating on the Chinese market, as well as other actors, such as NGOs. Under the SCS system, social behaviour is part of the assessment, and for example, people deemed to have 'bad' credit ratings are listed, as 'untrustworthy' as far as the government is concerned. These lists will restrict these individuals' access to public resources or certain industries, while the credit-worthy could e.g. enjoy more convenient services when applying for administrative approval. Setting up a mechanism for information-sharing between different institutions, such as the Memorandum of Cooperation between the Ministry of Civil Affairs and the Supreme Court, assume the collection of information on 'bad credit', which Chinese courts nationwide can access. The key lies in the implementation practices, such as reward and punishment systems.

Monitoring appears only the first step, and the ultimate aim is to steer the behaviour of all market participants by rewarding desirable practices and punishing undesirable ones. For instance, if a company diligently complies with environmental regulations and is even ahead of its obligations in reducing emissions, it can get a tax reduction or more preferential access to state (backed) credit. Merics, in its study 'China's social credit system' of May 2017, lists as examples of punishments: unfavourable conditions for a new loan, higher taxes than for compliant competitors, reduced opportunities to participate in publicly-funded projects and even, in severe cases, shutting down a company's e-commerce accounts or even denying travel tickets for top managers. Potential rewards include lower taxes or good credit conditions.

The SCS has the potential to further reinforce the role of the state in the management of the economy and, consequently, also to reduce the space for the free flow of market forces. The SCS system could be used in a protectionist way to promote its 'indigenous' companies, products and services, to the detriment of foreign business and even professionals in China (e.g. through rewards if a company's data processing operations are located inside China or if they use 'indigenous' components, or through punishment if a company hires foreign nationals beyond a given threshold).

The SCS could be used to restrict the possibilities of foreign business to benefit from the announced liberalisation of investments that is meant to come with the negative lists that will replace China's investment catalogues (e.g. if only companies with good ratings can actually invest in areas not excluded by the negative lists, i.e. on unrestricted sectors). According to the [Merics study](#) (China Monitor of May 2017), some of the recently established free trade zones may serve as testing grounds for linking investment opportunities and social credit ratings.



Source : Merics, China Monitor May 2017

The SCS system appears to be in line with its broad industrial policy strategy set out in 'Made in China 2025' and with China's efforts to strengthen the government's control over cyberspace. In particular, the guidelines and measures related to the security of cross-border data transfers entail a strong preference for data localisation and for using domestic ICT equipment. Alongside the SCS initiative, which also refers to strengthening quality supervision by e-commerce enterprises by implementing identification rules, and requires users to apply real-name registration for using live-streaming, which came into force 1 December 2017. A new platform traces fake names used on the internet back to their original domain — a further means for the Chinese government to track the actual people posting information without them being able to hide behind anonymity. China also released the final version of the national standard on personal information protection in January 2018. Unless the information is de-identified, prior notice and consent from individuals to the transfer or sharing of their data is required, as is also required by China's Cybersecurity Law. Moreover, the certification requirement in China for virtual private networks (VPN) restricts the processing of data to technology approved by the Chinese government and may provide access to a huge pool of information, which could be used to feed the SCS. It is essential to push for transparency over the system and the way in which it is implemented: the regulations enforced, and the punishments and rewards handed down.

Annex 5: Basic data

People and geography

Population		1 378 665 000	*Source:* World Bank (2016)
Capital city	Beijing	21 240 000	*Source:* UN (2016)
Other major cities	Shanghai	24 484 000	*Source:* UN (2016)
	Chongqing	13 744 000	
	Guangdong	13 070 000	
	Tianjin	11 558 000	
	Shenzhen	10 828 000	
Surface area		9 562 911 km^2	*Source:* World Bank (2017)
Life expectancy at birth	women men	77.7 74.6	*Source:* World Bank (2015)
Literacy rate		95.1 %	*Source:* World Bank (2010)

Rankings

Human development index	Score: 'High' Ranking: 90/188	*Source:* Human Development Index, United Nations Development Programme, 2016.
Press freedom index	Score: 77.66/100 Ranking: 176/180	*Source:* World Press Freedom Index, Reporters Without Borders, 2017 *(0 being the best possible score and 100 the worst)*
Freedom in the world	Score: 'Not free' Rankings: political rights: 7/7 civil liberties: 6/7	*Source:* Freedom in the world, Freedom House, 2018. *(1 represents the most free and 7 the least.)*
Ease of doing business	Score: 65.29/100 Ranking: 78/190	*Source:* Ease of Doing Business, The World Bank Doing Business index, 2018.
Corruption perceptions index	Score: 41/100 Ranking: 77/180	*Source:* Corruption Perceptions Index, Transparency International, 2017. *(0 represents the highest level of corruption, 100 the lowest)*
Global terrorism index	Score: 5.543/10 Ranking: 31/163	*Source:* Global Terrorism Index, Institute for Economics & Peace, 2017. *(0 represents the lowest impact of terrorism, 10 the highest)*

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