China's geoeconomic strategy and its implications for Europe

A view from Barcelona

Patricia García-Durán and Marc Ibáñez Díaz (eds.)

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INTRODUCTION

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Associate Professor of International Economic Organisation, University of Barcelona

Marc Ibáñez Díaz
Economist and political scientist

China has become an essential actor on the global economic scene, including for local economies like Barcelona's. In 2021, 2–3% of Catalan and Spanish exports went to China. While this may seem a small figure, it conceals China's real impact on our economy, since global value chains mean that many Spanish products are exported to China via third countries. In terms of value added, China accounted for over 5% of the value exported by Spanish companies in 2016, the most recent year for which there is data. China's impact on local infrastructure is no less significant. In 2021, it was the origin or destination for 40% of containers unloaded and 15% of containers loaded at the port of Barcelona.

However, China's role in international trade causes tensions. Its state capitalism, with its public companies, subsidies and forced transfers of intellectual property, entails a model that distorts the world economy. Without breaking any of the rules of the world's trading system, China breaches its spirit.

During the pandemic, the Asian giant has both closed off from the rest of the world and become a more assertive actor. Lithuania and Australia have recently been subjected to commercial reprisals for making decisions against Chinese political interests. Meanwhile, tensions between China and the United States (US) persist despite the Phase One agreement reached at the end of 2019. Talk of greater economic interdependence has given way to debate about the benefits of decoupling, especially when it comes to products that are essential to national security such as rare earths. In the United States a new episode of great power competition is already openly discussed, and the debate has only grown in prominence since the Russian invasion of Ukraine and China's pro-Russian neutrality.

In this context, the European Union's (EU) strategy of trying to open up a third way of rapprochement with China through the investment agreement signed at the end of 2020 – which former German Chancellor Angela Merkel defended – seems to have been unsuccessful. But even if that agreement had materialised, it would have been insufficient to face all the challenges China presents, according to the European Parliament (2021/2037(INI). The recent restrictions on Lithuanian products mean Europe has also become a target of Chinese coercion. This monograph, funded by the Barcelona Metropolitan Area (AMB), seeks to understand

The opinions expressed in this article are the sole responsibility of the authors and do not necessarily reflect or represent the position of the organisations in which they work.

this complex state of international economic relations, which has such potential to impact Europe's economy and, by extension, Barcelona's. As the vice president of the AMB, Ernest Maragall, pointed out, this monograph aims to help reduce the uncertainty in which institutions make decisions, and thus has a foresight function.

Talk of greater economic interdependence between China and the United States has given way to debate about the benefits of decoupling.

The monograph is structured into two sections. The first deals with China's economic and trade strategy and the second with the EU's response. The theses of the authors of this monograph were presented at a seminar held in Barcelona on October 6th 2022. The subsequent debate revealed the existence, even in Europe, of the two opposing visions of how to approach the relationship with China that are so prevalent in American debates. The doves, on the one hand, who lean towards the liberal school of international relations, defend cooperation with China and emphasise the absolute gains from its participation in the international economy. The hawks, meanwhile, who are closer to the realist school, argue that cooperation should not naïvely disregard China's objectives of global supremacy. For this group, cooperation must show relative gains – integrating China into the international system has not worked, and its aim is not cooperation but the overhaul of the international system. Both sides agree that a level playing field with China does not exist – and on the need to establish one.

Arancha González Laya, current Dean of the Paris School of International Affairs at Sciences Po, and former Minister of Foreign Affairs of the Spanish government, made the seminar's opening remarks. She began by stating that rather than deglobalising, the world is fragmenting. In our present situation commercial growth comes from services (mainly digital) and the great powers are competing to be pioneers in developing new technologies and setting standards for them. In this setting, Xi Jinping gives China a new type of leadership – more nationalist than Mao, more ideological than Deng Xiaoping and more controlling than his predecessor, Hu Jintao. Europe needs a trade relationship with China that involves a balance between openness, autonomy and sovereignty. In order to define this relationship, we must reflect on what challenge China poses, how much we want to depend on it, and, finally, what position the EU should adopt in the face of China–US decoupling. To find this balance, the EU has decisions to make about its instruments (it must be able to defend itself), its degree of dependency (it must diversify its sources), its ability to set standards (perhaps by allying with third parties), its degree of cooperation with China (a systemic actor) as well as with other actors, and it should increase its resilience (new public–private partnerships for investments in new technologies). In other words, the separation between trade and geopolitics is being redefined.

1. The Chinese economic model and its effects on Barcelona: impacted by the pandemic?

Alicia García Herrero, Chief Economist for Asia Pacific at Natixis and Senior Fellow at Bruegel, begins the first section of the monograph with a chapter on China's macroeconomic situation and its geopolitical aspirations. Her analysis shows that the government's anti-COVID-19 policy has affected Chinese growth and it will be unable, in the long run, to sustain its exponential growth. Nevertheless, China will

continue to harbour aspirations of global hegemony. Despite its anti-Western rhetoric over the Russo-Ukrainian war, Chinese companies are scrupulously complying with Western sanctions. The Chinese government backs Russia, but stops short of offering it material support. The author suggests that China will take advantage of the present opportunity to strengthen the role of the renminbi and to implement its payment system – another step towards achieving global supremacy.

Óscar Guinea, Senior Economist at ECIPE, discusses the dual circulation strategy promoted by the Chinese government since 2020. This strategy is based on internal and external circulation. With internal circulation, China seeks to develop its domestic economy and make domestic consumption the engine of the economy, thus providing greater insulation from the global economy – particularly the West, and any possible sanctions it may apply. To do this, China must substitute imports of high-tech materials with its own production, which requires a strong industrial policy like "Made in China 2025". Through external circulation, China looks to continue maintaining its global export position, but with products of increasingly high added value. To date, foreign demand has been a major part of China's growth engine. The government aims to maintain its position as the world's leading exporter, without it being the main driver of the economy.

In his contribution, Guinea uses the example of medical technology products to show how Chinese industrial policy discriminates against foreign companies. This specific example helps us understand how national, provincial and local governments assist the country's companies to gain capacity and become globally competitive in specific sectors handpicked by the authorities. In this particular case, the central government has used subsidies and large-scale public tenders to develop the sector domestically without offering equal competition to foreign companies. But this is not always a successful strategy. China may have achieved its goals when it comes to medical technology products and solar panels, but this has not been the case in sectors like aircraft construction and semiconductors, where it has spent years trying to break Western dominance. Now, developed countries (particularly the EU) are giving China a taste of its own medicine, deploying instruments that limit Chinese companies' access to developed economies. In Guinea's view, the EU's relatively small degree of dependence on China allows it to advocate for maintaining cooperation.

Enrique Fanjul, partner at Iberglobal, presents the main means of developing China's external circulation, the Silk Road. He introduces it as a Chinese tool for increasing its interdependence with other countries and extending its influence, while taking a leadership position in the Global South. Originally, the project was set to reproduce a large Eurasian connections corridor, but it has gradually expanded to other sectors, including healthcare and digital technologies. For the time being, the Silk Road seems to have lost momentum as its development slowed due to the pandemic, China's economic slump, and the economic difficulties making recipient countries wary of taking on more debt. Fanjul sees the slowdown as temporary, because the Silk Road remains an essential component of China's long-term foreign policy. Other developed countries, meanwhile, are presenting their alternatives to the Silk Road, such as the European Union's Global Gateway and the G7's Partnership for Global Infrastructure and Investment.

In order to define the EU China relationship, we must reflect on what challenge the Asian giant poses, how much we want to depend on it, and, finally, what position the EU should adopt in the face of Sino-American decoupling.

The Silk Road seems to have lost momentum due to the pandemic, China's economic slump, and recipient countries economic difficulties.

At the seminar, these contributions were enriched by that of Marin Orriols, Director of the Business Internationalisation Area of the Barcelona Chamber of Commerce, who analysed the relationship between China and Barcelona's local economy. First, he explained that the difficulties European companies face when operating in China are paralleled by the issues Chinese companies face doing business in Barcelona. Some of these difficulties oblige Chinese companies to buy existing factories and distribution chains rather than creating them. On the other hand, he pointed out that China's pandemic restrictions against foreign travel are currently having a significant impact on Barcelona's local economy, especially at the luxury end. Nevertheless, he added, Barcelona retains features that favour good relations with China, and gave the example of its universities and business schools. Finally, he mentioned the need to continue cooperating economically with the Asian giant.

2. Europe in relation to China's geoeconomic strategy and the uncertainty of the conflict in Ukraine

The authors in the second section of the monograph agree that no level playing field exists with China, and discuss the EU's various responses. All three recognise that Europe is seeking to reform the World Trade Organization (WTO) in order to correct its deficiencies and revise the international trade rules against unfair competition. The WTO's 12th Ministerial Conference in June 2022 was the starting point for that reform, thanks to the EU's efforts. But a multilateral deal will take time. To achieve short-term results, this multilateral response must be complemented by bilateral relations with the US and China, as well as new trade instruments that allow the EU's values and interests to be better defended.

Clàudia Canals, Director of Avançsa and Luís Pinheiro de Matos, economist at CaixaBank Research, present the transatlantic response: the EU–US Trade and Technology Council (TTC). Albeit not explicitly, this initiative is the product of China's more than likely leadership in the technologies of the fourth industrial revolution. Canals and Pinheiro de Matos show that Europe depends more on China in the technology sector than on Russia for energy, although US China-dependence exceeds even Europe's. A hard decoupling from China is thus unfeasible in the short term. Given this, the TTC appears to be an endeavour to define technological standards that preserve transatlantic values, promote green technologies and strengthen global supply chains. The authors consider this tool to be more pragmatic than previous failed cooperation attempts like the Transatlantic Trade and Investment Partnership (TTIP), although caution must be exercised when assessing its potential successes.

Xavier Fernández Pons, Associate Professor of International Public Law at the University of Barcelona, focuses on the European Union's unilateral response. Thus far, it has relied on trade defence instruments against unfair competition (anti-dumping and anti-subsidy) that are acceptable under WTO rules. But these mechanisms do not allow it to tackle coercive pressures deployed by third country governments like

China's. A recent example are the Chinese trade restrictions against Lithuania in retaliation for allowing Taiwan to open an office in the country under its own name (an attack on the "One China" policy and, therefore, on China's political interests). In such situations, the European Commission's proposed anti-coercion instrument would allow the EU to act as a federal state and deploy trade countermeasures.

Finally, Pepe Álvarez, General Secretary of the UGT and Vice President of the European Trade Union Confederation (ETUC), who also participated in the seminar, expressed the need to maintain a bilateral relationship with China. Unions recognise that the economic opportunities the Chinese economy offers can attract many European companies, which can bring benefits to Europe's economy and workers. But European companies do not enjoy the same access to the China's market as their Chinese counterparts. And China is an opaque country ruled by a dictatorship that does not respect labour rights and which also exports low social, environmental and labour standards to the rest of the world. The existence of unions is essential to democracy, Álvarez said, and in China there are no free unions. Here, EU trade policy can play its part, as the proposal to ban the sale of products made with forced labour on the single market recently showed. It follows that a lack of European collaboration with China could in fact bring much worse outcomes for workers' rights.

US dependence on China in the technology sector exceeds Europe's. A hard decoupling from China is thus unfeasible in the short term.

3. Final thoughts

China's economic ascendancy and more assertive global stance is creating tensions. The contributions in this monograph make clear that relations with the Asian giant pose four main problems to the international economic and political order. First, China considers its economic, social and political model superior to the West's and seeks both recognition and supremacy in the international system. Second, its model discriminates against foreign companies by tilting the playing field. Third, the fourth industrial revolution is underway and China wants to lead it in both standards and technology. Fourth, globalisation also brings dependencies, as the US–China trade war, the pandemic and the war in Ukraine have made abundantly clear.

The EU has been negatively affected by all these events. When it comes to trade, the EU is major global actor, but being a global power requires a multidimensional approach. Trade is one dimension – the others are foreign, security and defence policies. With Europe's defence outsourced to the US (Borrell, 2022), transatlantic alignment may seem the most logical choice. But while this is one potential strategy, it must be recognised that in the new world of great power competition European interests do not always align with the US. Europe and the US may agree on the economic and social model that needs defending, but it must be borne in mind that the US also defends its global hegemonic position.

As this new phase begins, Europe is not entering it naively. First, it has shed some of its naivety about the challenge China poses, and has already taken certain measures to limit its influence, such as investment review mechanisms. Second, the EU is approving new trade policy instruments that will allow it to better defend itself against coercive and

anti-competitive pressure (Erixon, 2022). Third, it is aware that is has the capacity to define global standards and has fostered the creation of the TTC. Finally, the pandemic and the Russo-Ukrainian war have crystallised the problems generated by dependence on a single supplier and the need to diversify. The war has produced conditions that have highlighted Europe's vulnerabilities, but which favour the necessary strengthening of foreign policy. The EU continues to define China as a "partner, economic competitor and systemic rival" (JOIN(2019) 5 final). Parliament has given its view on the foundations of this strategy and, according to the press, the Council is negotiating a new, more assertive strategy towards China (Foy, 2022).

The EU is major trade global actor, but being a global power requires a multidimensional approach. Trade is one dimension – the others are foreign, security and defence policies.

We thus find ourselves in an international setting in which the main powers (USA, China, Russia and the EU) are defining their instruments of competition and taking positions so as to be able to defend themselves. The contributions in this monograph have shown that decoupling would not only be bad for our economy, but that it is not even possible in the short term. For this reason, China should still be considered a significant economic actor for Barcelona's economy. However, this does not mean we should stop fighting for a level playing field. Only common rules that ensure fair competition will allow the different international players to interact with confidence.

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THE CHINESE ECONOMIC MODEL AND ITS EFFECTS ON BARCELONA: IMPACTED BY THE PANDEMIC?

- THE GEOECONOMIC IMPACT OF CHINA'S COVID POLICY AND WHY IT MATTERS TO THE EUROPEAN UNION

  Alicia García-Herrero

- EXPORTING DISTORTIONS: CHINESE INDUSTRIAL POLICY AND THE EUROPEAN RESPONSE

  Óscar Guinea

- THE NEW SILK ROAD: FROM EURASIAN CORRIDOR TO GLOBAL CHINESE FOREIGN POLICY INITIATIVE

  Enrique Fanjul

Alicia García-Herrero
Senior Research Fellow, Bruegel ; Chief Economist of Asia Pacific, Natixis

The COVID pandemic hit China in January 2020. Since then, like the rest of the world, the Chinese economy has gone through huge up and downs. The difference is that China appeared to have recovered from COVID earlier than anybody else, ending 2020 with positive GDP growth (2.3%), while deep recessions were being suffered globally. In fact, China was dubbed "first in, first out".

The problems began in the second half of 2021, as China's recovery turned out to be less spectacular than many expected, and only worsened in the first half of this year, as it continued with draconian lockdowns and closed borders while the rest of the world finalised its opening up. In fact, China might end 2022 with below 3% GDP growth, well below the levels in Southeast Asia and less than half India's rate.

Strict mobility restrictions are not the only problem China is facing. For one thing, the geopolitical landscape is increasingly tense. The Biden administration, which many had expected to change tack on China, has essentially continued with the containment measures implemented under Trump, following years of engagement. As if this were not enough, Russia's invasion of Ukraine last February 24th brings China's rather close relationship with Russia into play, even though it has officially remained neutral with regard to the ongoing military conflict.

In this paper, I will first review the impact of the pandemic on the Chinese economy and its geopolitical implications. Then, I will analyse how the war in Ukraine has complicated matters further and what to expect in the future on the geopolitical front. Finally, I look into China's medium-term growth, which will suffer structural deceleration.

1. The impact of the COVID pandemic on the Chinese economy

In January 2020 the Chinese city of Wuhan was the first to declare a full-scale lockdown in response to the virus later named COVID-19. Soon after Wuhan, China deployed large-scale lockdown measures across the country, which lead to a sharp reduction in people's mobility nationwide with massive economic impact. Vehicle navigation data suggests that national inter-city mobility fell by 66% in February 2020 compared to

Strict mobility restrictions are not the only problem China is facing.

the 2019 average. That said, mobility soon recovered, as the outbreak was successfully contained rather quickly and tight border controls were imposed as the rest of the world was hit by the pandemic. The reduction in people's mobility moderated in March, falling only 10% and even turning positive in April (+26%). Since then, mobility had been relatively stable until the novel Delta variant stepped in and led mobility in China to slow from the second half of 2021.

Worse than that, in the first few months of 2022, China introduced more widespread lockdowns in response to Omicron, a much milder but more contagious variant of COVID-19. Drastic mobility restrictions were imposed on cities that in total accounted for 40% of China's gross domestic product, including Shanghai, the renowned international financial centre. In addition, half of China's highways were not functioning and ports were operating inefficiently as a result of large mobility restrictions[1].

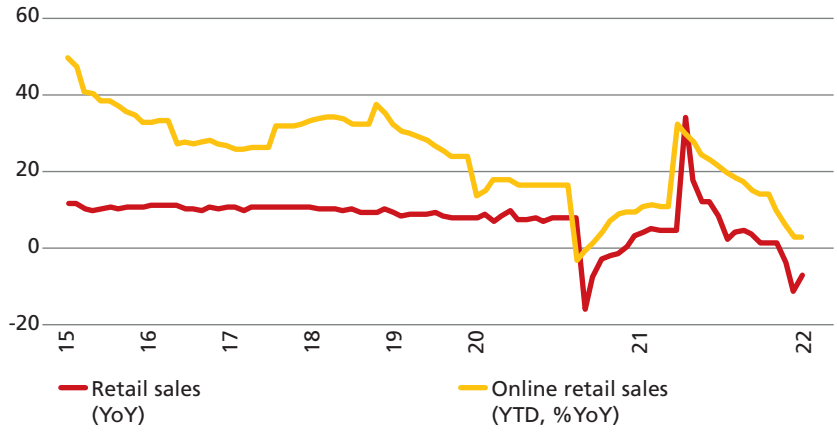
The sharp fall in people's mobility took a toll on household consumption but also disrupted manufacturing production, with a slight recovery since June as some of the most severe lockdowns were lifted. Still, sentiment has remained at a record low throughout 2022 as the Chinese economy has been coping with another massive shock since the second half of 2021, namely the demise of the real estate sector. This started with the collapse of China's largest real estate developer, Evergrande, followed by several others and which extended, in the second half of 2022, to mortgage boycotts by Chinese households who had not received the housing units they had paid for, as developers left them incomplete. The only bright spot has been the strength of external demand throughout 2021 and the first half of 2022, although this has slowed more recently as the world moves into synchronised deceleration.

Moving ahead, two important questions remain, first and foremost whether zero-COVID policies will be ended. The Party Congress, which confirmed President Xi in an unusual third term, has offered no clues in this regard but the very negative market reaction to the conclusion of the congress and the continuing poor economic data might lead to some targeted re-opening. In any event, this decision – like many others in China today – is highly political and hinges on President Xi's conviction that China's response to COVID should be different than that of the United States. This will be explored in more detail in the next section. The second key question is the handling of the real estate crisis, which has so far been rather ineffective and mainly based on setting up fiscal resources – especially by local governments already cash-strapped by COVID-related expenses – to support developers and help them finalise the millions of housing units which remain under construction.

Given China's size and how much it has contributed to the global economy over the last decades, this is extremely important for the global economy and could not come at a worse time. China's lower economic growth is bound to affect the rest of the world via two key channels. First, China is the largest importer of most commodities, so commodity importers are bound to see their exports fall. Secondly, it has become the centre of global value chains, so any renewed lockdown in important cities for the production/assembly of manufactured goods, as well as ports and railways, will create bottlenecks in other parts of the world, feeding supply-related inflationary pressures.

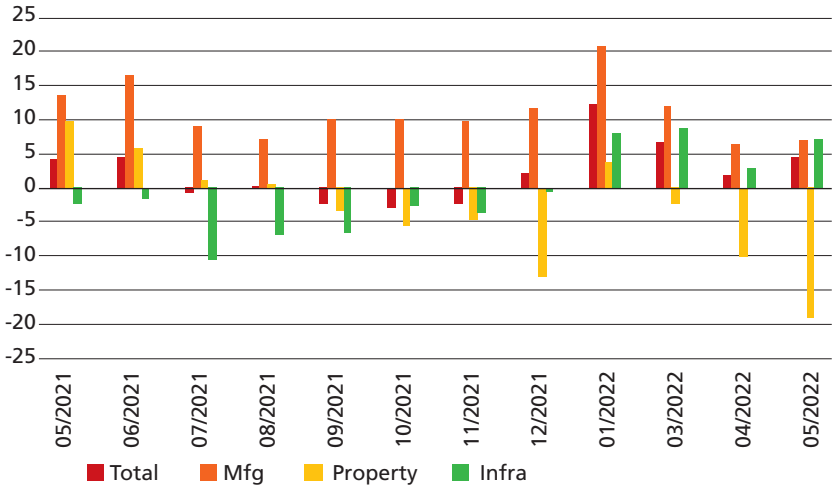
1. For a full account of China's economic future after the October 2022 Party Congress, see: https://jamestown.org/program/the-economic-outlook-for-xis-third-term-mounting-challenges-dwindling-fiscal-and-monetary-options/

Figure 1. China: Retail Sales and Online Retail Sales



Source: NBS, Natixis.

Figure 2. Retail sales (YOY)



Source: Natixis, AACC.

Figure 3. China's International Air Passengers (million persons)

N.B. Data as of February 2022.
Source: Natixis, Civil Aviation Administration of China, CEIC.

2. Geopolitical consequences of the pandemic

Trust between China and the rest of the world, especially the West, is at a record low. Beyond the economic impact, anti-Chinese sentiment has been growing in many parts of the world.

The fact that China's leadership, and especially President Xi, has remained fully committed to "dynamic zero-COVID" policies has political as well as economic consequences. The sharp decline in imports China has experienced is not only due to lack of demand (in fact imports have grown much less than retail sales), but rather the push for self-reliance. As such, Chinese exports grew 10% year-on-year in the third quarter, while imports rose by only 0.6%, per the data from China Customs. All in all, the substitution of foreign inputs for domestic ones is in full swing and is bound to continue with or without zero-COVID restrictions.

The lack of people-to-people exchanges also related to the closed borders clearly adds to the decoupling push stemming from the pandemic, as trust between China and the rest of the world, especially the West, is at a record low. Curbs on Chinese citizens traveling abroad have wreaked havoc on the economies of several countries that were major tourist destinations for Chinese travellers before the pandemic, particularly Thailand and others in Southeast Asia, but also Hong Kong. Beyond the economic impact, anti-Chinese sentiment has been growing in many parts as the lack of exchange continues, and the same is true for Chinese citizens' attitudes towards foreigners.

Without physical exchanges, Chinese overseas investment has also plummeted and we see no signs of recovery yet. This has led to increased scrutiny of Chinese companies' potential acquisitions by target countries. In other words, the pandemic has clearly increased the speed of bifurcation between China and the United States but, also more generally, as China has been closed to the rest of the world as whole and not only the United States. In fact, the recent position paper from the EU Chamber of Commerce in Beijing is probably the most negative of the past few decades[2].

The lack of mutual understanding between China and the rest of the world is also clearly shown in the much more reduced number of high-level summits between the United States and China but clearly also between China and the EU (European Union) or even its member states. The most recent high-level economic dialogue between the EU and China took place digitally, on April 1st 2022, and was a "dialogue of the deaf", according to the High Commissioner, Josep Borrell. In addition, although China and the EU in principle concluded the long-disputed Comprehensive Agreement on Investment in 2020, the deal has not yet taken effect due to the European sanctions.

The increasing perception of a growing political and social divide between the West and China obviously does not bode well for future scientific or business collaboration between China and the broader international community, although it is difficult to measure the immediate impact of this on the global economy.

3. Economic impact of the war in Ukraine on China

The war in Ukraine and the unprecedented sanctions imposed on Russia by Western allies in response to Russia's invasion are having a very large negative impact on the global economy well beyond Russia and Ukraine.

2. https://www.europeanchamber.com.cn/en/publications-position-paper

The European economy is being hit hard not only due to its dependence on Russian energy.

While the direct impact of the Ukraine crisis on the Chinese economy has been much more muted, it has still been negative. As the largest importer of oil and gas in the world, the huge jump in energy prices is bad news for China, not least because China's carbon reduction goals (as outlined in its Five-Year Plan) require additional gas imports to transition away from coal. However, China has swiftly reacted to this additional headwind buffeting its economic outlook by lifting annual carbon emission targets at the Two Sessions of the National People's Congress and the Chinese People's Political Consultative Conference in early March 2022. In addition, China – as well India and other emerging economies – has stepped up purchases of cheaper oil from Russia due to the wedge created by Europe's reluctance to buy oil from Russia.

In other words, although China should, in principle, oppose events that increase energy prices, its implicit support for Russia seems to indicate that other objectives, namely weaking the United States global hegemony, are more important. This has been further demonstrated by China's accommodating position on OPEC's recent cut in production, even if that means higher oil prices.

Although China should, in principle, oppose events that increase energy prices, its implicit support for Russia seems to indicate that other objectives, namely weaking the United States global hegemony, are more important.

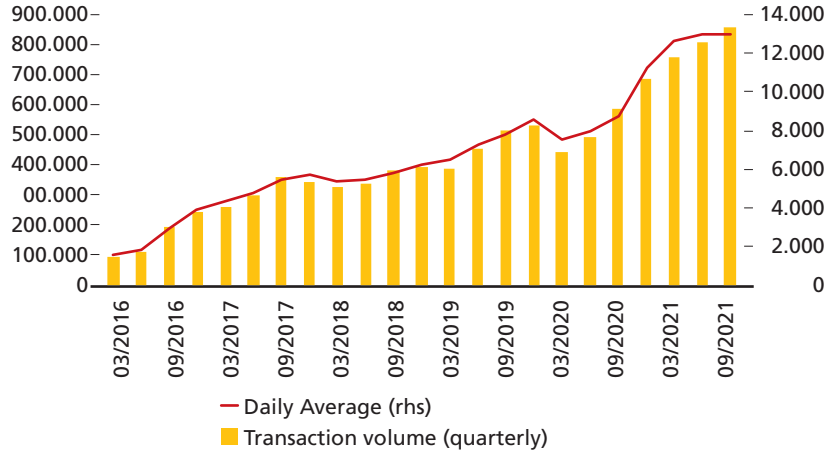
The other immediate downward pressure on the Chinese economy is the slew of Western sanctions imposed on Russia. Chinese banks do not seem to be financing operations with Russia, although evidence remains scarce and Chinese energy companies – including Sinopec – are shelving their projects with Russian counterparts. Still, the impact of such withdrawal from Russia has so far been quite moderate for China, since Russia is ten times smaller. China does not even need to fully cut its ties with Russia, but just avoid hard currency payments and some targeted entities such as the Russian central bank and the ministry of finance. Indeed, China remains the largest exporter of goods to Russia, especially those that are subject to export controls, like semiconductors, and which Russia desperately needs in order to maintain its industrial – as well as military – capacity. This also means that there is a latent risk of China ending up being subject to secondary sanctions, especially as far as exports of dual-use semiconductors are concerned.

Another silver-lining for China from the war in Ukraine is fostering the international role of the renminbi (RMB) as Russia – as well as other sanctioned countries such as North Korea and Iran – steps up its use of the RMB through China's international payment system (CIPS). This is also increasingly the case for Saudi Arabia as well, whose largest export destination is China, and even for India when it comes to coal imports.

All in all, China's rhetoric regarding the war in Ukraine has been anti-US and anti-NATO, while being quite accommodating towards Russia and opposing Western sanctions against the nation. At the same, by complying with Western sanctions, China has so far abided with the letter of the law – or at least no proof exists of the opposite – even if not its spirit[3].In other words, China is using any space available to support Russia and to create a united front against the West with its Global Security Initiative and the expansion of the Shanghai Cooperation Organisation and the BRICS.

3. For more details on the steps China could take to help Russia financially, see: https://www.bruegel.org/blog-post/can-china-bail-out-putin

Figure 4. RMB Cross-border Interbank Payment System (transaction volume)



Source: Natixis, PBoC.

All in all, while the war in Ukraine constitutes a negative shock to the Chinese economy, beyond high commodity prices the direct impact remains limited. The problem is that it is happening at a time when China is beset by a severe Omicron COVID-19 wave on top of a cyclical deceleration and negative market sentiment stemming from a regulatory crackdown. Though China seems keen to abide by the letter of the law and comply with sanctions, the country also seems willing to take risks to maintain its strategic relationship with Russia. This is clearly a razor's edge for China, as it could be caught in the fire not only of Western sanctions, but also of potentially negative decisions by Western companies operating in China. Still, China looks favourably upon Russia's attack on the West, as its ultimate objective is to change the global order towards Chinese dominance. Fully aware of this challenge, the United States is putting renewed pressure on China, most recently with a very broad semiconductor ban that will make it harder for China to move up the technological ladder.

All in all, the growing differences between the Western narrative and that of China – let alone Russia – are clear signs that, following the invasion of Ukraine, the world is more than ever like a chess board on which Biden and Xi are pursuing global hegemony.

4. China's long-term growth prospects

At first sight, China's difficult economic situation may appear temporary, since it is mainly explained by COVID restrictions, real estate woes and, to a lesser extent, the war in Ukraine. However, the reality is that the Chinese economy is also decelerating structurally.

To gauge China's potential growth rate in the future, a straightforward and common way is to make a forecast based on standard convergence theory. Convergence theory is based on the assumption that poorer countries grow relatively faster than richer countries and in the long run growth rates will all converge. Following a similar methodology to Gordon (2014) and implementing a convergence-style estimate for

labour productivity by taking the changes in the population growth pattern given by UN population forecasts, the estimated average real GDP growth rate for the period between 2021 and 2025 should be 4.9% and 3.6% from 2026 to 2030, descending to 2.4% from 2030 to 2035 (Table 1). This rather low medium-term growth rate should surprise no one. Many studies have already made use of this framework, and many have pointed to a slowing growth trajectory for China[4].

Table 1

	Output	Labour productivity
2021-2025	4.9	4.9
2026-2030	3.6	3.8
2031-2035	2.4	3.0

No matter how low this growth rate may look, the reality is that most risks are on the downside. First, is the further worsening demographics, as one key scarring effect of the pandemic. The second is an even lower return on assets, as the state's role in the economy becomes more and more pervasive with continual crackdowns on the private sector and, in particular, China's innovative tech sector. Finally, both climate change and COVID-related harm to human capital and Chinese people's openness to the rest of the world are worrisome issues which make lower potential growth increasingly likely. Finally, both United States–China strategic competition and China's own increasingly totalitarian drive, blessed at the recently concluded Party Congress, are two additional worrying signs for China's potential growth.

At first sight, China's difficult economic situation may appear temporary, (COVID-19, real estate woes and, to a lesser extent, the war in Ukraine). However, the reality is that the Chinese economy is also decelerating structurally.

5. Conclusions

China's growth has been coming down for both cyclical and structural reasons. The cyclical reasons in 2020 are a redoubling of COVID restrictions while the rest of the world was lifting them, the troubles in China's real estate sector and the war in Ukraine. China's response to the pandemic, like Russia's invasion of Ukraine, is best understood not through an economic prism but rather a geopolitical one. On COVID, the recent mobility restrictions have created havoc for consumption as well as investor sentiment but are framed in President Xi's mantra that China's response to COVID is superior to that of the West. In the same vein, China's narrative favouring Russia's invasion of Ukraine by blaming the US and NATO does not make much economic sense, as Europe is a far bigger market for China than Russia. Still, supporting Russia serves a much more important objective – feeding anti-Western sentiment across the world in a heated system rivalry for world hegemony between the US and China.

This is why Russia's invasion of Ukraine has clearly worsened the world's already shaky geopolitical situation, feeding an even more intense confrontation between the US and China, already heated due to the pandemic.

The result of all this is a world moving in two blocs, with the EU, the United Kingdom, Australia, Japan and South Korea more aligned with the United States than ever. At the same time, and supported

4. See IMF (2020) and World Bank (2019).

by Russia, China is extending its alliances in the Global South with the New Development Paradigm and the Global Security Initiative, as well as expanding the BRICS. The world has clearly become a great power competition between the United States and China. Against this background, China's power – so far mainly economic – seems likely to suffer much worse growth prospects for a few years to come.

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The effects of China's industrial policy are felt beyond its borders. On the one hand, foreign companies see their trade with China reduced, while at the same time those same companies must compete in other markets with Chinese businesses that have benefited or are benefiting from its industrial policy, which tilts the playing field. So, what begins with a gradual erosion of market share in China becomes a decline in market share in other countries. In other words, market distortions that begin in China do not stay in China.

This paper focuses on Chinese industrial policy and its repercussions for the global economy. It studies the case of medical technology goods to show how Chinese industrial policy moves from the general – strategic plans and general lines – to the specific – increased market share for Chinese companies in the medical technology sector. Deciphering the Asian giant's industrial policy "playbook" in this sector allows us not only to understand how its industrial policy applies in a given industry, but also to untangle the process by which economic policy acts as a lever to position Chinese companies at the technological vanguard in other sectors.

1. Chinese industrial policy: plans, policies, successes and failures

China's industrial policy is shaped by several different plans, strategies and documents. The general lines are set out in "Made in China 2025", which was published by the government in 2015 and aims to transform Chinese companies into leading global high added-value manufacturers. More recently, the "dual circulation" policy aims to reduce China's dependence on the rest of the world and to this end promotes domestic consumption of domestic products rather than those of foreign manufacturers (García-Herrero, 2022).

These strategies are complemented by sectoral measures and plans at state and provincial levels that give concrete content to the general strategic lines mentioned above. The measures include concessional loans, government procurement that favours domestic industry and research and development (R&D) incentives in the form of public funding, tax breaks and subsidies for R&D spending.

China's "dual circulation" policy aims to reduce Chinese dependence on the rest of the world and to this end promotes domestic consumption of domestic products rather than those of foreign manufacturers.

The success of China's economy and its industrial policy in certain sectors is unquestionable. For example, the country has become one of the world's leading exporters of active pharmaceutical ingredients (APIs). Indeed, Chinese companies' market share of European Union (EU) of EU imports of APIs grew from 5% (by value) and 12% (by volume) in 2010 to 7% and 22%, respectively, in 2019. Public procurement policies have played a part in this success, such as "China 4+7", which supported the generic medicines industry (Burton, 2019). Solar panels are another well-known example, where Chinese producers increased their share of global exports from 4% in 2002 to 42% in 2019. In its 11th Five-Year Plan (2006–2010), the government granted Chinese solar companies subsidies and favourable access to credit, while at the same time strengthening control over the raw materials that are essential to producing the panels (Erixon et al., 2021). More recently, the growth in Chinese machinery and equipment exports saw them contribute 17% of the global total in the sector in 2019, partly thanks to government subsidies (Szamosszegi, 2009).

And yet, all that glitters is not gold. For example, despite years of state support, Chinese companies continue to lag behind in the semiconductor industry and have failed to break the dominance of Airbus and Boeing in the aeronautics sector. Meanwhile, provincial governments have at times sought to foster their own industrial champions to pursue national goals, resulting in excess capacity and undermining national industrial policy objectives. Barwick et al. (2019) show how subsidies to the Chinese shipbuilding industry between 2006 and 2015 led to the entry and expansion of inefficient companies, while bringing in only mediocre profits.

Nevertheless, the gestation of industrial policy – be it the "Made in China 2025" initiative or the sectoral plans – and its successes and failures are part of a process by which the government uses public policies to shape the market so that Chinese companies can prosper. The following section presents the government's industrial policy "playbook" in the medical technology sector.

2. Case study: Chinese industrial policy and the medical technology sector

In 2014, President Xi Jinping declared the need to accelerate the localisation of high-end medical devices, reduce production costs, and promote the continuous development of domestic companies (Chinese Central Government, 2014). In April 2021, the Five-Year Plan (2021–2025) set a medical technology goal of having at least six Chinese businesses in the top 50 global medical device companies. With only four Chinese companies currently in the top 100, and none in the top 50 (Chinese Department of Equipment Industry, 2021), this is an ambitious goal.

In the past, most medical devices produced in China were low-cost high-volume items, while international manufacturers supplied high-end devices to Chinese hospitals. In recent years, this commercial pattern has changed radically. The change is in part a natural reflection of Chinese companies' improved capacity for innovation and their ability to serve a market whose demand has increased substantially as a result of the COVID-19 pandemic. Between 2019 and 2020, the number of Chinese medical technology

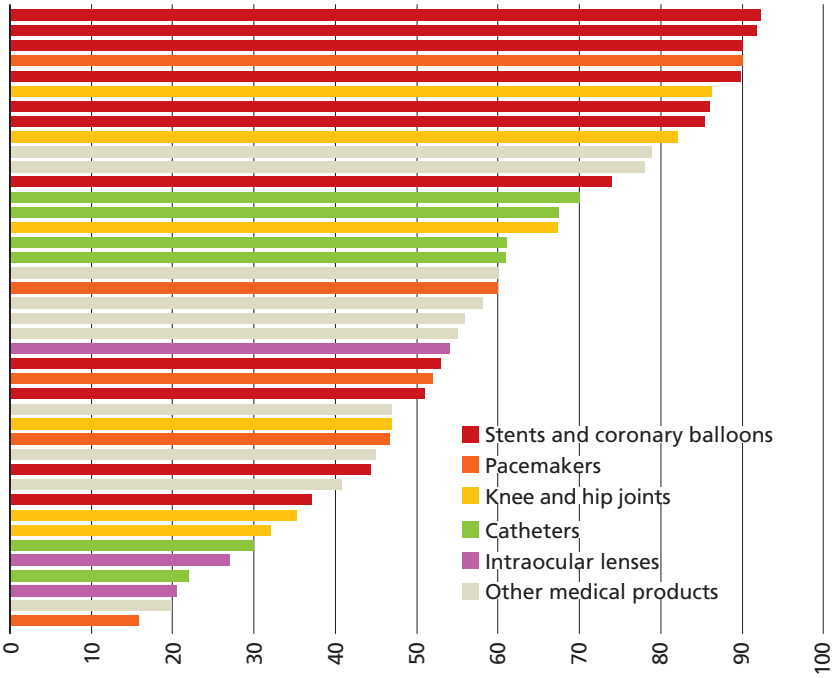
manufacturers grew by 46% and exports of these products increased by 33% (China Department of Comprehensive and Planning Finance, 2020).

But Chinese medical equipment exports grew much more strongly than those of European companies. This increase was not only down to higher sales of personal protective equipment like medical gowns, masks and gloves due to the COVID-19 pandemic. Exports of relatively sophisticated medical devices such as electrodiagnostic, radiation and dental devices rose too. China's medical technology trade balance – the difference between exports and imports of these products – rose from a deficit of €1.3 billion in 2019 to a surplus of €5.2 billion in 2020 (Erixon et al., 2021).

One of the key industrial policy tools has been the centralisation of public tenders as a way to encourage domestic production of "Made in China" medical technology. Following the example of the pharmaceutical sector, both the central and provincial governments have used public procurement to shape the medical technology market. Former Premier Li Keqiang summed this process up: China should centralise public procurement in order to concentrate industry (Zhou Chencheng, 2020).

In the gestation of industrial policy and its successes and failures are part of a process by which the government uses public policies to shape the market so that Chinese companies can prosper.

Figure 1. Falling prices in medical technology tenders in China 2019–2021



Source: Erixon *et al*. 2022a

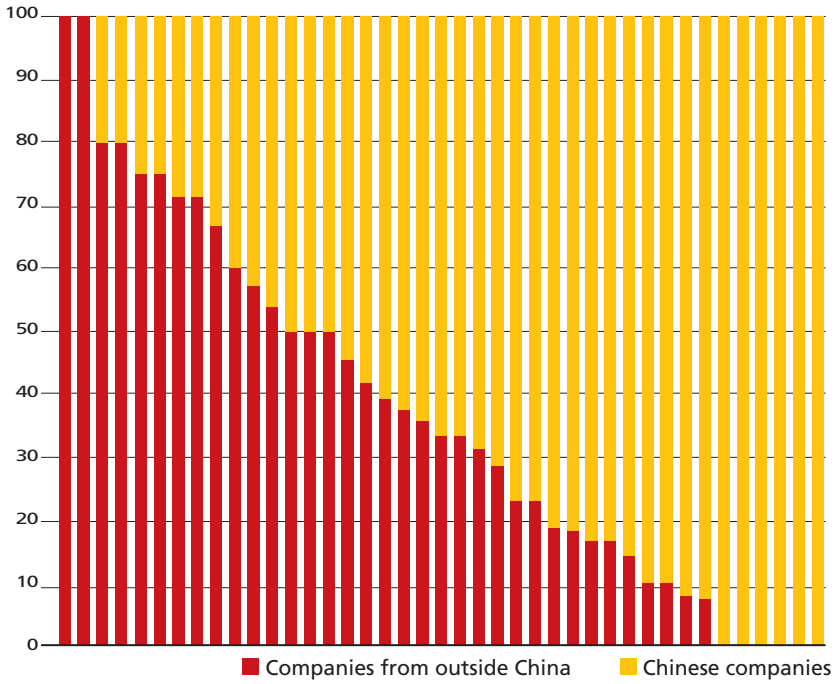
Centralised public procurement of medical supplies – which in several cases involves a single tender for groups of cities or provinces that are home to tens of millions of people – seeks to create a monopsony, which is similar to a monopoly, except that the purchaser receives most of the profit from each transaction. A monopsonic market usually contains few suppliers because the buyer tends to reduce the sellers' margins, leading the number of companies to fall. Meanwhile, the buyer – in this case the Chinese government

– has so much power over the market that they can introduce other objectives besides securing a lower price. With the Chinese medical technology market, centralised state procurement reinforces the industrial policy that promotes domestic production.

One of the key industrial policy tools has been the centralisation of public tenders as a way to encourage domestic production of "Made in China" medical technology.

The effects of centralising public procurement of medical technology and making the market a monopsony are becoming clear. In recent years, medical device tender prices have fallen up to 90% (Figure 1), partly thanks to public subsidies, and an increasing number of Chinese companies have won these tenders (Figure 2). At the same time, the market is becoming consolidated, and the number of medical technology companies per million inhabitants accessing public contracts is much lower in China than in Europe (Erixon et al., 2022a). In general terms, this is the Chinese industrial policy "playbook" in the medical technology sector. The end result is a more concentrated market in which both size and economies of scale prevail when it comes to achieving cost reductions, and where Chinese companies supply a growing proportion of the national market.

Figure 2. Percentage of Chinese and non-Chinese companies winning medical technology tenders 2019–2021



Source: Erixon *et al.* 2022a

Table 1. Chinese and European exports of medical technology to Africa, Asia and Latin America and the Caribbean (2019 and 2020, in billions of euros and as a year-on-year percentage)

	Africa			Asia			Latin America and the Caribbean		
	2019	2020	%	2019	2020	%	2019	2020	%
European Union	2.5	2.6	5%	19.9	19.6	-2%	3.0	2.9	-5%
China	0.7	0.8	26%	5.8	7.5	29%	1.1	1.6	46%

Source: Erixon *et al.* 2021

Chinese industrial policy directly affects Western companies. One example is the impact on the European medical technology industry, which directly employs over 650,000 people in the sector's 33,000 companies (95% of which are SMEs). These companies are the leading exporters of medical technology to China, accounting for 34% of all Chinese imports of these products in 2020. Nevertheless, between 2019 and 2020 purchases of European medical technology decreased. The drop in Chinese imports was most notable in products for which the government organised centralised public procurement. At the same time, as Table 1 shows, Chinese exports of these products showed positive growth between 2015 and 2020. The figures not only show that foreign production was replaced by domestic production, but also that Chinese companies gained market share abroad.

European governments are well aware that China's industrial policy distorts prices and competition in China, in third countries, and in the EU.

3. Europe's response to Chinese industrial policy

European governments are well aware that China's industrial policy distorts prices and competition in China, in third countries, and in the EU. In response to this industrial policy and the distortions it provokes in the European economy, the EU is preparing two regulations that aim both to dissuade China from using industrial policy and to tackle its negative effects: an international public procurement instrument and a foreign subsidy instrument.

The international public procurement instrument will allow the EU to restrict access to its public tender market to companies from countries where European companies face restrictive or discriminatory measures when accessing public procurement. To do this, the regulation adjusts the rating scores for the proposals for a tender, or excludes offers from countries subject to the public procurement[1] instrument. This measure, which is applied to public contracts worth over €5 million, could restrict Chinese companies' access to the EU public procurement market, which is estimated to be worth over €2 trillion. The European Union could use this new tool to negotiate with the Chinese government to change the public policies that discriminate against European companies in the Chinese public procurement market.

The foreign subsidy instrument, meanwhile, aims to tackle the distortions foreign subsidies create in the single market. To this end, the European Commission may impose corrective measures on foreign companies that benefit from public subsidies in mergers and acquisitions, public procurement and the sale of goods and services by foreign subsidiaries in the EU that distort the functioning of the internal market. The measures may include blocking investments or obliging subsidies to be repaid. Once this instrument is approved, the EU will be able to investigate these subsidies and respond to the tension between the EU's relatively strict rules on state aid and the growing competition in the internal market from companies from outside the EU that benefit from state subsidies, as is the case of certain Chinese companies.

In parallel, the EU has deployed a more active industrial policy. For example, it has relaxed competition rules to allow certain state subsidies in Important Projects of Common European Interest (PCEI) in sectors like microelectronics and electric batteries, and has proposed a regulation

1. A more detailed analysis of the international public procurement instrument and the international subsidy instrument, as well as other trade defence measures currently under consideration by the EU, can be found in Erixon *et al*. (2022b).

to support the production of semiconductors in the EU. Europe's industrial policy approach is not so different from China's "dual circulation" strategy, insofar as the EU also seeks to reduce its foreign dependency. In the case of China, its dependence is limited (Guinea, 2022). The EU has, meanwhile, abandoned the competitiveness agenda, relying on a European industrial policy that prioritises the interests of dominant companies over entrepreneurship and economic dynamism.

China's industrial policy creates market distortions whose effects reverberate beyond its borders.

4. Conclusion

China's industrial policy creates market distortions whose effects reverberate beyond its borders. Both because of its size and the government's active role in the country's economic development, Chinese industrial policies have a direct effect not only on the Chinese market but also on third countries and on the EU itself – and by extension on foreign companies, including European ones. From the EU point of view, the measures described in this article are intended to achieve fairer competition between the EU and China, in addition to tackling distortions in China's industrial policy in the single market. However, these policies treat the symptoms of the problem, rather than the root: the only way to counter China's ability to attract business and investment is to implement policies that improve the competitiveness of Europe's economy and companies.

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THE NEW SILK ROAD: FROM EURASIAN CORRIDOR TO GLOBAL CHINESE FOREIGN POLICY INITIATIVE

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The New Silk Road, launched by Chinese President Xi Jinping in 2013, has had a variety of English names – "One Belt, One Road", the "Belt and Road Initiative" and now "the BRI". Initially, it was conceived as the development of a great Eurasian corridor that would help China extend its economic influence towards Central Asia, Europe, Southeast and South Asia, and some parts of Africa. Two routes were planned for the corridor: one, over land, more or less follows the old Silk Road from China to Europe via Central Asia and the Middle East; the other is a sea route from China to the Mediterranean, passing through South Asia and East Africa.

China had other complementary motivations, as well as opening up a Eurasian corridor. On the one hand, the New Silk Road offered a new means of export for its vast excess capacity in sectors like steel and cement. At the same time, China also sought to promote the development of its inland areas, which were more economically backward than the coastal regions.

The New Silk Road thus prompted great expectations. China planned to incentivise and promote the execution of projects by contributing abundant financing in the form of both investments and credits (which as of 2022 total nearly $1 trillion).

But over time the BRI (the term we will use in this article, interchangeably with the Silk Road) has taken on global scope. In a geographical sense, it now stretches across large swathes of the planet, especially countries of the so-called Global South. Indeed, 147 countries have established collaboration agreements of various kinds with the BRI (Nedopil, 2022b), with 18 European Union member states having signed agreements of one kind or another in support of the initiative.

More recently, new extensions of the Silk Road have been spoken of, such as the Polar Silk Road (to develop maritime connection routes in the Arctic) and the Digital Silk Road.

The BRI has acquired dimensions that extend beyond the merely economic, as it has become a key part of Chinese foreign policy.

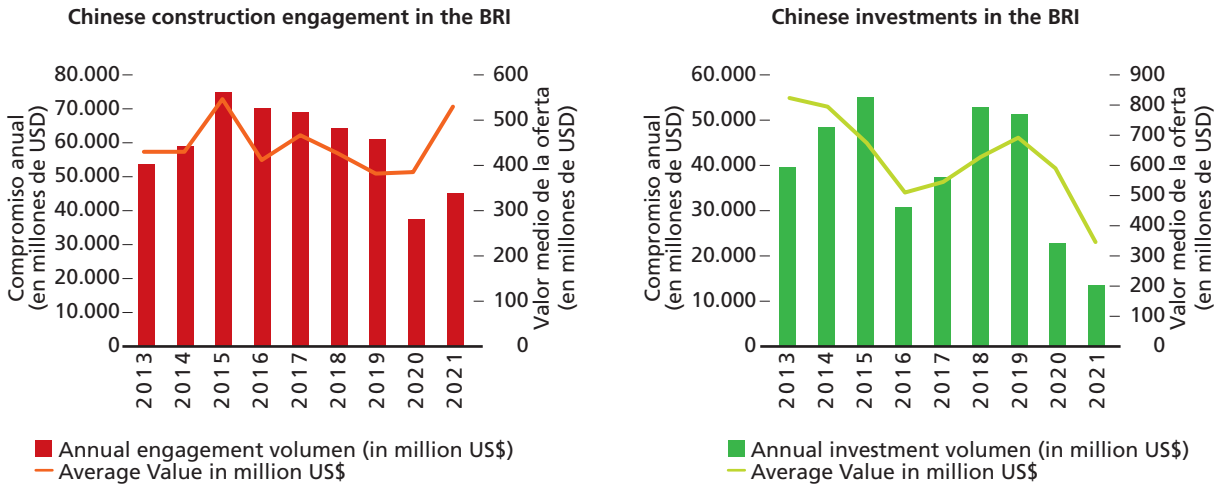
Having acquired dimensions that extend beyond the merely economic, the BRI has become a key part of Chinese foreign policy. Amid China's growing tensions with the United States (US) and other Western countries, the initiative is a way to seek allies among other countries, especially in the Global South. It is a tool for improving economic ties with other countries, creating interdependence, spreading its influence and taking a leadership role. Looking ahead, the BRI is likely to undergo significant changes, both for Chinese domestic reasons and due to the launch of competing initiatives by advanced countries, such as the European Union's Global Gateway and the Partnership for Global Infrastructure promoted by the US within the G7 framework.

1. Has the BRI lost momentum?

In recent years, the BRI has lost momentum. Figure 1 clearly shows this, using data from a study by Fudan University in Shanghai, the most recent work examining its progress (Nedopil, 2022a). The author identifies two types of BRI project: construction and investment. Although they are not precisely defined, it may be deduced that the construction projects are for exporting goods and services, and involve the construction or refurbishment of ports, railways, power plants and so on. These are not investments, and as such do not involve the acquisition of ownership rights over assets. On the other hand, there are investment projects, in which property rights to assets are acquired.

Figure 1. Evolution of BRI project

Deal size of chinese engagement in the BRI: left, for construction projects, right investments (Source: Green Finance & Development Center, FISF Fudan University, based on AEI)

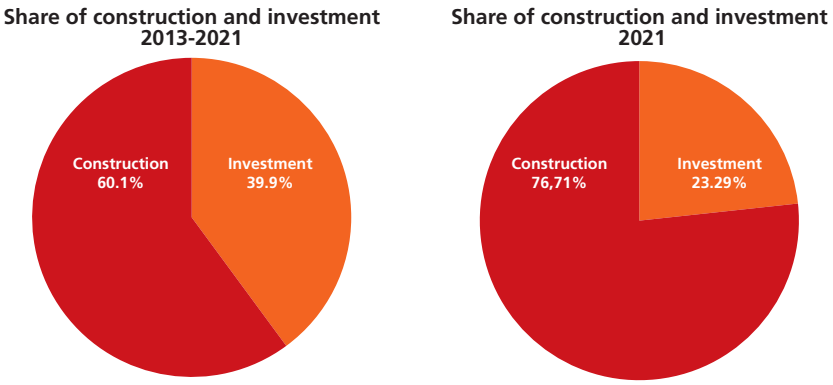


Source: Nedopil, 2022-A

According to studies published by Fudan University, as of 2022 the BRI has committed $932 billion: $561 billion to construction contracts, and $371 billion to investments.

In Figure 1, the downward trend in construction projects since 2015 is clear, with the exception of a moderate rebound in 2021. As for investments, a sharply downward trend is visible since 2018.

Figure 2. Distribution by type



The global economic slowdown has affected multiple countries where projects were planned, especially developing countries.

It is worth nothing that, globally, in 2021 foreign investment flows rose by 64% (according to UNCTAD), while Chinese investments in the BRI framework decreased by 40.8%.

Compared to 2019, the year before the COVID-19 pandemic, the funds dedicated to BRI projects in 2021 fell by around $53 billion (48%).

What factors explain this slowdown? First, the impact of COVID-19 and China's strict measures to fight it. China's zero-COVID policy has severely disrupted travel to and from the country. Unsurprisingly, this has affected international operations, which normally require a certain degree of personal contact.

Second, the pandemic and the zero-COVID policy caused a slowdown in the Chinese economy. The slump has been especially pronounced since the first half of 2022, when resurging infections led the authorities to adopt strict lockdown measures and quarantines, halting productive activity, disrupting maritime transport, and so on.

Third, the global economic slowdown has affected multiple countries where projects were planned, especially developing countries, whose lower foreign exchange earnings have made meeting their external debt commitments more difficult. This has led to a more prudent attitude among Chinese companies and banks when it comes to granting loans to finance projects. It has also led to a more prudent attitude among beneficiary countries when taking on new debt commitments.

The loans associated with the BRI projects have led to China's first foreign debt crisis, as a series of debtors are unable to meet the repayment commitments. China has been forced to carry out a major renegotiation of its loans. In total, $52 billion of loans from Chinese financial institutions to projects in BRI countries had to be renegotiated in 2020 and 2021, according data from the Rhodium Group. That is more than triple the $16 billion renegotiated in the previous two years. The renegotiations involve loan cancellations, deferred payment schedules and interest rate reductions.

Chinese involvement in BRI projects shows strong regional variations. Asian countries continue to receive the largest share of investment (around 35% in 2021).

Finally, at the time of writing, the potential impact on the BRI must be mentioned of the war in Ukraine. In the short term, rail connections between China and Europe have been affected. According to some sources (Umbach, 2022), about half of the rail routes between China and Europe pass through Russia. While there were 40 cargo routes in 2017 there are 78 today. In 2021, $75 billion-worth of Chinese goods were transported (up from $8 billion in 2016), with 336,000 containers reaching 183 cities in 23 European countries. The number of trains rose from practically zero in 2011 to 15,000 in 2021.

But while rail transport showed strong growth, it still represents a small share of Chinese freight transport. And it is impossible, at the present time, to forecast how the disruptions to rail connections between China and Europe will evolve in the future. It will depend, among other factors, on the evolution of the war, the sanctions against Russia and how China's image deteriorates due to its stance of implicit support for Russia.

2. Geographical and sectoral trends

Chinese involvement in BRI projects shows strong regional variations. Asian countries continue to receive the largest share of investment (around 35% in 2021), although projects in Africa and the Middle East have recorded strong growth, rising from 8% in 2020 to around 38% in 2021. On the other hand, investments in European countries decreased by 84% compared to the first six months of 2020.

Iraq was the site of the largest volume of construction contracts in 2021, with around $10.5 billion, followed by Serbia (about $6.8 billion), Indonesia (about $2.4 bn), Tanzania, Egypt, the Russian Federation and Singapore.

In terms of investments, Indonesia and Zimbabwe were the main recipient countries in 2021, followed by Vietnam and Chile. Meanwhile, investments in Laos, Sri Lanka and Singapore fell.

By sector, energy stands out. In 2021, total participation in this sector reached $22.3 billion, a significant reduction compared to previous years ($26.1 billion in 2020 and almost $44.8 billion in 2019).

3. Criticism and controversy

The BRI has attracted controversy since soon after its launch. One criticism, mentioned above, is that it is a means of exporting excess Chinese industrial capacity in certain sectors.

Over time, criticism of the initiative has grown. A notable example is the study published in 2020 by the European Union Chamber of Commerce in China, eloquently titled *The Road Less Travelled: European Involvement in China's Belt and Road Initiative* (European Union Chamber of Commerce in China, 2020).

Based on the opinions of companies that belong to the European Union Chamber of Commerce, the report highlights the marginal role European

companies play in the initiative. "Only 20 of 132 survey respondents report having bid on a BRI-related project. Most cite the lack of transparent bidding and procurement processes as a major barrier to participation, with only two having found projects through publicly available information. Of those that have participated, most have done so after being pulled in by business partners or local governments. All but a scant few have played niche roles, like providing certain technology or experience in the recipient country, which, given the scale of the BRI, saw most respondents refer to their level of involvement as "crumbs from the table"

BRI has attracted controversy since soon after its launch. Over time, criticism of the initiative has grown.

Among the other negative aspects mentioned are:

- Chinese lending conditions, which frequently lack transparency, and which may include very onerous conditions for recipient countries if they cannot meet their obligations;
- The lack of transparency in the project award processes, which in many cases do not follow the procedures that are standard in international markets;
- The lack of quality of some of the projects, which have been little studied and started up without adequate feasibility studies. There have also been accusations of corruption and political interference in the award processes, which have distorted their technical requirements.

Recently, criticism of BRI projects has increased notably. One example is the strong presence of the relationship with China in the Kenyan presidential elections of summer 2022. The two main candidates, former Vice President William Ruto and former Prime Minister Raila Odinga, both stated their intention to adopt a more firm stance towards China, which owns a substantial part of Kenya's external debt (around 30%). Vice President William Ruto, who went on to win the election, ran on a strongly anti-China platform, vowing to deport Chinese nationals doing jobs he said should be reserved for Kenyans. He also pledged to make government contracts with China public.

The flagship BRI project in Kenya has been the development of the Standard Gauge Railway (SGR) connecting Mombasa, the country's largest port city, with the capital Nairobi. The Export-Import Bank of China financed 90% of the SGR project with a $5 billion loan, while the Kenyan government provided the other 10%. A Chinese construction company, the China Road and Bridge Corporation, was responsible for implementing the project. In autumn 2022, the Kenyan government announced its intention to request a renegotiation of the credit in order to extend the repayment period.

4. Spanish companies in the BRI

Spanish companies have had almost no involvement in developing projects, something that aligns with the more general scant participation of non-Chinese companies.

In principle, a number of factors could have favoured Spanish companies' involvement.

First, Spanish companies have competitive advantages in engineering and construction, as shown by their experience building large-scale

infrastructure, with the Panama Canal and the Mecca high-speed railway good examples.

Second, Spain and China have maintained good political relations.

Third, while China has vast amounts of financing available, New Silk Road projects required significant contributions from other sources, which Spain could provide.

Spanish companies have had almost no involvement in developing projects, in line with the general scant participation of non-Chinese companies.

However, from the start there was notable scepticism in the business world, not only in Spain but around the world, about the chances of participating in BRI projects due to the dominant position of Chinese companies in them.

That dominance seems to be confirmed by the first published estimates. In January 2018, a study was published by the US-based Reconnecting Asia project, which keeps a database of BRI projects (Center for Strategic & International Studies, 2018). At the time, 89% of participating companies were Chinese, 7.6% were local companies and only 3.4% were foreign (companies that are neither Chinese nor from the countries where the projects are carried out).

By comparison, it should be noted that in the projects financed by multilateral development banks 29% of companies are Chinese, 40.8% are local and 30.2% are foreign.

At any rate, the result is that no known projects under the BRI banner include the participation of Spanish companies. There have, however, been cases of Spanish and Chinese companies collaborating on projects in third countries. In 2015, Técnicas Reunidas entered into an agreement with the Chinese company Sinopec and the Korean company Hanwha Construction for a refinery project in Kuwait. In 2018, ACS and the China Three Gorges Corporation were awarded a contract to build a dam in the Democratic Republic of the Congo. In 2019, Telefónica awarded Huawei a significant chunk of its 4G network in Brazil. To promote the cooperation, an agreement was signed during Chinese President Xi Jinping's 2018 visit to Spain.

5. Future prospects

What are the future prospects for the BRI? In the short term, a key determining factor is China's pandemic policy. As long as its borders remain semi-closed and international travel highly restricted, Chinese investment abroad will be severely limited, as will the financing of projects through loans.

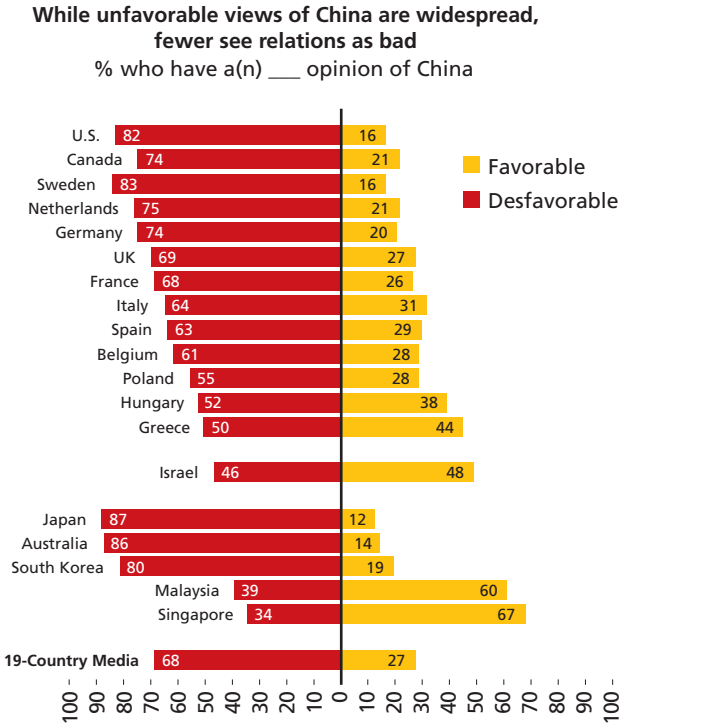
As for the longer-term future, several factors will affect the BRI for good and bad. It is difficult, if not impossible, to anticipate at present what the consequences of these different conditions may be.

On the one hand, the international community's opinion of China has deteriorated sharply and in a very short period of time, especially among developing countries and certain Asian states. Figure 3 shows the results

of a Pew Research Center survey conducted in 2022 on the perception of China in 19 countries around the world. The results are clearly negative. In the 19 countries as a whole, 68% of those surveyed said they viewed China unfavourably, with 27% holding favourable views. In Spain, 63% expressed unfavourable opinions.

Opinions in the so-called Global South were less negative, although, as mentioned, misgivings have risen about Chinese credits and investments.

Figure 3. Perceptions of China



Note: Those who did not answer not shown. Source: Spring 2022 Global Attitudes Survey. Q5b.
"Negative Views of China Tied to Critical Views of Its Policies on Human Rights"
PEW RESEARCH CENTER

In 2022, China's strategy in Europe suffered a blow when Estonia and Latvia announced their withdrawal from the 16+1 cooperation forum China had established with a number of European countries. This followed the withdrawal of Lithuania the previous year. The Estonian foreign minister said China's refusal to condemn Russia's invasion of Ukraine "was definitely a factor" in the decision. Estonia and Latvia mentioned the importance of China upholding the "rules-based international order", which Russia had violated with its invasion of Ukraine, even as China continued its "no limits" partnership with Russia.

Nevertheless, even as they withdrew Estonia and Latvia made clear that they remained open to cooperation with China. However, both countries preferred to use the platform provided by the European Union as the basis for their relations with China, and to strengthen their ties with the United States, especially on security, given the threat posed by Russia and China's implicit support for the invasion of Ukraine.

As well as widening the BRI's scope, China is launching new projects to strengthen its international influence. In recent months it has launched the so-called Global Development Initiative, which is economic in nature, and the Global Security Initiative (GSI), on international security. These are recent proposals, and it remains to be seen how they coordinate and overlap with the BRI – especially when it comes to the GSI. Either way, they are another reflection of China's desire to play a key role in the international order.

The BRI will have to "compete" with the various reactions of Western countries, which are offering their own alternatives. At the recent G7 summit, the launch of the Partnership for Global Infrastructure was announced, which seeks to mobilise $600 billion for infrastructure projects. Meanwhile, the European Union has launched the Global Gateway, with the aim of mobilising €300 billion by 2027 in projects relating to digital infrastructure, energy, transport, health and education. To a large extent, these initiatives are responses to the BRI, and seek to counteract Chinese influence in the international community.

The New Silk Road, already losing steam over recent years, faces a series of uncertainties: from the slowdown of the Chinese economy to the problems many debtor countries face meeting their debt commitments and the launch of alternatives by advanced democratic countries and China itself. All of this in a geopolitical context that has become highly complex, and in which unease about and clashes with the Asian giant have increased sharply. How these factors affect the Silk Road remains to be seen.

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EUROPE FACING CHINA'S GEOECONOMIC STRATEGY AND THE UNCERTAINTY CAUSED BY THE UKRAINE CONFLICT

THE TRADE AND TECHNOLOGY COUNCIL: THE NEW WINDOW FOR EUROPEAN UNION–UNITED STATES COLLABORATION

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The Trade and Technology Council (TTC) was created in 2021 to be a forum for the United States and European Union (EU) to discuss and agree a common trade and technology agenda that aligns with their shared democratic values. To a degree, this forum also marks a new approach to transatlantic relations, with regulatory coordination used as a tool for economic integration, rather than a brake on achieving it. However, despite an ostensibly more pragmatic approach than prior attempts, the first few months – along with the history of transatlantic trade relations – invite caution when assessing the TTC's potential successes.

1. The what and wherefore

The TTC was announced at an EU–United States meeting in Brussels in June 2021, and by the end of summer 2022, two meetings had been held. The formal inauguration was at the first meeting, in Pittsburgh in September 2021. By the second, in Paris in May 2022, transatlantic relations had acquired renewed relevance following Russia's invasion of Ukraine at the end of February. The third meeting, to be held in the United States, may have taken place by the time this paper is published.

Specifically, the TTC aims (1) to increase trade and investment between the two powers, (2) to strengthen the technological and industrial leadership of the transatlantic region, and (3) to promote innovation while protecting and promoting emerging and key technologies. Implementation is via ten working groups that tackle issues such as setting technology standards, promoting green technologies, strengthening global supply chains[1], data governance, regulating technology platforms and the use of technology and its security and human rights implications (see Figure 1 for a complete list of the ten working groups).

The initial agreement establishing the TTC does not explicitly mention China. But, for the United States in particular, limiting the Asian giant's geoeconomic influence is among the forum's indirect objectives. China has

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1. Or global value chains.

The Trade and Technology Council (TTC) was created in 2021 to be a forum for the United States and European Union (EU) to discuss and agree a common trade and technology agenda that aligns with their shared democratic values.

become a very significant actor on the international stage, and one whose economic, social and political values differ greatly from those advocated by the United States and Europe. Trade and technology restrictions are classic ways to curb a country's economic emergence, as they directly affect economic development. Meanwhile, with the fourth industrial revolution well underway, limiting the use of (and potential leadership in) advanced technologies like artificial intelligence (AI) seems like the most effective route. By way of illustration, and staying with AI, Chinese companies do not yet lead in total number of patents, but they have made huge progress in recent years. Chinese universities and public research centres, meanwhile, are also well-placed in this field of research (see Figures 2 and 3).

The emergence of this new dialogue platform comes after years of growing questioning of the international liberal order established after World War II, and numerous disagreements between the United States and various major actors on the international stage, especially China. In 2018, for example, under Donald Trump's presidency, the United States stepped up the policy of decoupling from China with several clashes in the trade and technology spheres that led to considerable rises in tariffs between the two countries and major technology restrictions. In early 2020, the two economies signed the Phase One deal in order to calm the conflict. But while the agreement managed to bring a halt to the tariff escalation, its goals have not been reached.

The United States and EU have also had major disagreements in recent years. The conclusion without a deal of the negotiations over the Transatlantic Trade and Investment Partnership (TTIP), and the tariff increases that occurred under Trump due to the commercial dispute between Boeing and Airbus (now resolved), are two important examples. However, despite the discrepancies, both regions have unceasingly sought ways to collaborate in various fields (economic, political, social, environmental, etc.). The TTC is the latest attempt, this time with a technology and trade focus.

Thus far trade cooperation has been more fluid than on other occasions, as it has focused on the unified response over trade sanctions against Russia following the invasion of Ukraine. The need to build more diversified global value chains that depend less on China has also been discussed, as have key production inputs (the notorious chips, for example). At the technological level, the two parties to the TTC have reaffirmed the importance of working together to ensure AI development complies with the OECD's AI Principles.

The first two meetings have shown a clear improvement in transatlantic relations; those to come will reveal whether the new forum can provide some long-term joint lines of action.

2. What unites us and what divides us

The fourth industrial revolution and the current geopolitical setting mean that of all the crucial items of discussion in the TTC, the technological are particularly important. We focus on several of these to give a general picture of where the EU and US appear to agree, and where it is likely to be more difficult to find common ground.

What unites us ...

There is EU–United States agreement over the need to increase the robustness of global value chains through greater autonomy in the production of certain products, like semiconductors and chips. The pandemic led many economies to recognise the importance of certain products (including chips) to the proper functioning of many global supply chains in various sectors. Hence, both the United States and EU have announced programmes to strengthen local chip production (the CHIPS for America Act and FABS Act, in the case of the United States, and the European Chip Law, for the EU). The two regions start from very different points in the semiconductor sector, with the United States the more advanced. The planned investments differ too. But this is undoubtedly a technological area where cooperation between the powers can be extensive and understanding relatively simple.

A problem that unites us in the semiconductor field is that both regions depend on China for certain rare earth elements that are vital to various high-tech devices.

Another problem that unites us in the semiconductor field is that both regions depend on China for certain rare earth elements (like scandium or yttrium) that are vital to various high-tech devices (including chips). That China remains the country with the largest share of these chemical elements poses a clear obstacle to EU and United States desires to diversify their global value chains away from China, as the meeting in Paris explicitly mentioned.

Green technologies are another potential avenue of cooperation. This has undoubtedly become more urgent since the Russia–Ukraine conflict broke out, given the EU's pressing need to reduce its dependence on fossil fuels, many of which come from Russia (Canals et al., 2022).

Finally, both regions are equally concerned about the impact of the misuse of certain technologies in areas like protecting human rights and international law, as well as the spread of fake news, which can undermine democratic movements. Despite the shared nature of these concerns, the legal discrepancies around issues such as freedom of expression and data privacy are likely to prove sticking points.

... and what divides us

Among the more complex areas of agreement is transatlantic data transfer, due to the privacy issues mentioned above. The various legal frameworks on the how citizens' data may be used has been a recurrent obstacle in recent years. Indeed, the European Court of Justice (ECJ) has twice invalidated agreements established between the EU and United States over data transfer (2015 and 2020)[2]. In March 2022, the regions reached a new agreement. According to the press release, the United States is committed to strengthening the protection of personal data, as well as the civil liberties that govern United States intelligence activities. The final configuration of the legal text remains to be seen, along with any future judicial decisions in this regard[3].

Competition involving large technology companies is another difficult area to agree on. The EU currently applies antitrust regulation more forcefully than the United States. The Biden administration has been more open to dialogue over the regulation of technology companies, as

2. The Schrems I ruling invalidated the Safe Harbor Agreement in 2015, while the Schrems II ruling invalidated the Privacy Shield.
3. As this paper was concluded (October 7th 2022), President Biden signed an executive order introducing new guarantees that address the points mentioned in the ECJ's decision. Among others, this new decision would make it possible to limit US intelligence services' access to European data and would strengthen the legal guarantees around the monitoring and resolution of disputes over the protection of personal data.

shown by the promotion of a global minimum tax (particularly aimed at large multinational companies, including big tech). But the truth is that the United States, as the home of most of the big technology companies (see section 3), has a national vision and interests that differ from Europe's. In this area, the EU is preparing legislation (the Digital Markets Law) that seeks to regulate digital platforms towards more competitive practices.

Finally, and more generally, the United States approaches this collaboration with the EU as a way to limit China's power, as well as to maintain its world hegemonic status. To do this, it takes a notably offensive stance towards the Asian power. The EU meanwhile proposes this collaboration as a way to create a prosperous internal market that is more autonomous and better aligned with the humanist, social and democratic values that are its DNA (Torreblanca and Jorge Ricart, 2022). The European position has thus tended to be more defensive than offensive.

Fairly recently, however, a shift has been notable in the EU's typically more moderate approach (Otero-Iglesias, 2020). So, for example, with the roll-out of 5G technology, which depends on technology provided by various Chinese companies, the EU has published a series of recommendations to minimise security risks from providers that belong to "hostile states" (European Commission, 2020). Although the document does not directly point the finger at China or Huawei, the Chinese technology giant, it goes without saying that they fit this risk profile (European Court of Auditors, 2022).

3. Technological decoupling from China: the EU vs. the United States

The two regions' excessive dependence on Chinese rare earths was made explicit at the second TTC meeting, within the framework of working group 3 (secure supply chains), and appears in the Joint Statement from the meeting (TTC, 2022).

However, in a markedly globalised world in which China plays a central role in the mesh of global manufacturing value chains (even beyond the area of rare earths highlighted at the Paris meeting), securing greater autonomy from the Asian giant (or decoupling, as it is known in the United States) will not be easy for the United States or Europe, especially when it comes to technology.

European disengagement from China seems the more difficult challenge, since the Old Continent is facing the next industrial revolution without great technological champions (see the Figure 4) and with significant dependence on Chinese technology for the deployment of its 5G network. The United States, by contrast, has seven of the ten largest technology companies, including all of the top six[4].

Even so, decoupling from China is a complicated challenge for both regions, as our analysis based on the OECD's international input–output tables shows (TiVA, Trade in Value Added). The tables allow us to adequately assess the origin of the goods and services consumed in a

4. In terms of market capitalisation.

given country (whether for domestic production or consumption or for export), since they trace the "comings and goings" of the intermediate inputs throughout the entire production process. So, for example, if a good is imported from a certain country, but most of that good has been produced in a third country, data like gross imports do not reflect the importance of the third country, but TiVA tables do.

In the case that concerns us here, we analyse final EU and United States demand and, using the TiVA data, calculate the significance of the value added by China in said final demand, paying particular attention to the technological sectors. What we see is that 2% of final EU and United States demand originates in China. This is slightly below the weight of the EU and the United States in each other's final demand (approximately 2.5% of the EU's final demand originates in the United States, and vice versa). Hence, China has become the second-largest trading partner for the EU and the United States in recent years.[5] This was not always the case: at the end of the 1990s, before China entered the World Trade Organization, Chinese value added in the final demand of the two was below 0.5%, with the most prominent sector being textiles, especially in the United States (see Tables 1 and 2).

Greater autonomy from the Asian giant (or decoupling) will not be easy for the United States or Europe, especially when it comes to technology.

Studying the figures sector by sector reveals significant differences in the evolution of China's integration with the EU and the United States since the end of the 1990s. It is not only that European and United States dependence on the Chinese textile sector stands out, its integration is also among the fastest. This should come as no surprise, since it is linked to the end of the Multi Fibre Agreement, which gave extensive protection to the textile sectors of advanced countries and harmed emerging and less developed economies, which had a clear competitive advantage in the sector due to abundant cheap labour.[6]

Another noteworthy aspect, and one that fits with the topic that concerns us here, is the fact that China has also become a strategic partner in technological sectors like electronics, electrical equipment and machinery. Notably, China's "electronic footprint" is currently larger than Russia's "energy footprint" in the European economy, accounting for 18% of European final demand in this sector, compared to Russia's 16% of the European energy sector (see the detail in Table 1). Similarly, in sectors like machinery and electrical equipment, while the level of relative penetration in European final demand is lower, Chinese value added still already exceeds that of other historically much more important trading partners, like the United States, United Kingdom and Japan. In other sectors of high technological complexity, like transport, China's importance has also evolved relatively quickly over the last decade. For example, China currently dominates the production of battery cells, which are essential for electric car production.

The data shows that China has an even larger "electronic footprint" in the United States than in the EU. Thus, Chinese value added amounts to 20% of final demand in the computer and electronics sector and 19% for electrical equipment. What is more, over the last decade, the integration of Chinese products into United States demand in other technologically advanced sectors, such as machinery and transport equipment, has accelerated substantially (see details in Table 2).

5. According to OECD TiVA data, although not in terms of gross trade flows, where China's importance to the United States is greater. It should also be borne in mind that, due to its complexity, TiVA data is updated slowly, and the last year referenced is 2018.
6. At the Uruguay Round of 1994, agreement was reached to complete the Multi Fibre Agreement gradually between 1995 and 2005.

For all these reasons, a process of "hard" decoupling from China seems inviable in the short term, especially in the technology field. Chinese technology is a very important part of many of the products we consume in both the EU and United States, and a very rapid departure from current production processes would entail high costs, especially in terms of prices – which are already highly stressed.

In the medium term, however, the pandemic and, more recently, the war in Ukraine, have shown us that a clear will – and, perhaps better said, need – exists to redesign some of the highly global and disintegrated value chains (including technology ones). Although it is too early to know what changes will occur, chains are likely to include more redundancy of key components (i.e., with higher numbers of suppliers of those components), to be equipped with digital technology that allows them to detect failures in the chain more quickly, and to be shorter and therefore less global, and in many cases less dependent on China (Canals, 2022). All of these changes will lead us towards the greater technological "autonomy" both the EU and the United States advocate.

4. Conclusions

There has been an indisputable link between technological revolutions and the prosperity and transformation of societies. Currently, immersed in the fourth industrial revolution – brought by AI, advanced robotics and Big Data – and in the midst of a rebalancing of global geopolitical powers, the transatlantic allies do not want China to define the rules of the game of tomorrow. The Asian giant is a country with a markedly different political, economic and social system from the United States and EU.

This is the context framing the TTC dialogue forum, whose objectives, among others, are to consolidate common transatlantic strategies in the technological field, to establish standards and rules for global adoption, and to restrain China in this field.

The new approach will have to withstand winds blowing in different directions. In its favour is the perception that, having arrived in a world that differs from what we knew until a few years ago (shaped by events like Brexit, the growing internal and external threats to liberal values, the pandemic and the Russian invasion of Ukraine), new economic diplomacy tools are needed that have clear geopolitical consequences. On the other hand, this forum could act as a preferential mechanism for establishing the "rules of the game" in new markets, where the regulatory framework has yet to be defined. Thus, working to avoid regulatory disputes in more mature markets may improve the chances of success in new markets (with great development potential).

However, significant headwinds can also be expected along the way. The history of transatlantic disagreements over international trade is long, in part as a result of antagonistic regulatory traditions. This divergence in approaches to how regulatory frameworks are determined is another possible headwind: in the United States, the regulation of new markets is usually carried out ex post, through the establishment of "standards"; in the EU, such an exercise is usually done ex ante, prescribing rules that can ensure a level playing field.

Thus far, the experience of the first months of the TTC means we can already identify several nuances in various areas of collaboration. On the one hand, progress has been made in terms of cutting-edge technologies, as evidenced by the advances in digital regulation and information exchange, as well as sharing objectives with respect to artificial intelligence. On the other hand, cooperation on the climate is proving more challenging than expected. In this area, both discourse and regulation are much more advanced in the EU and, as a field that affects multiple markets, the reservations on the US side may become even more acute.

Finally, the apparent transatlantic consensus reached on economic sanctions against Russia, a technical task facilitated by various working groups within the TTC, is unlikely to be replicated in the case of China. Thus, the greatest challenge to transatlantic relations and the TTC's most significant task remains unresolved: China, strategic competitor or geopolitical rival?

In this sense, it is worth reflecting briefly on the alternative paths that could be taken regarding the relationship with China. Recently, the United States has chosen the path of confrontation for China–United States relations, but in truth, cooperation with China and other great powers in specific fields, like green technologies, could be particularly fruitful in the context of the TTC. After all, China is not only the largest greenhouse gas emitter, it is also a leader in renewable energy technologies, as well as in investment in and development of these technologies both within its borders and beyond (Chiu, 2017). So, while strategic competition between geopolitical blocs seems inevitable in some key areas of the fourth industrial revolution, identifying specific areas where strategic cooperation with other trading partners is desirable or even essential will also be important for the EU and for the success of a forum like the TTC.

Having arrived in a world that differs from what we knew until a few years ago (shaped by events like Brexit, the growing threats to liberal values, the pandemic and the Russian invasion of Ukraine), new economic diplomacy tools are needed that have clear geopolitical consequences.

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The greatest challenge to transatlantic relations and the TTC's most significant task remains unresolved: China, strategic competitor or geopolitical rival?

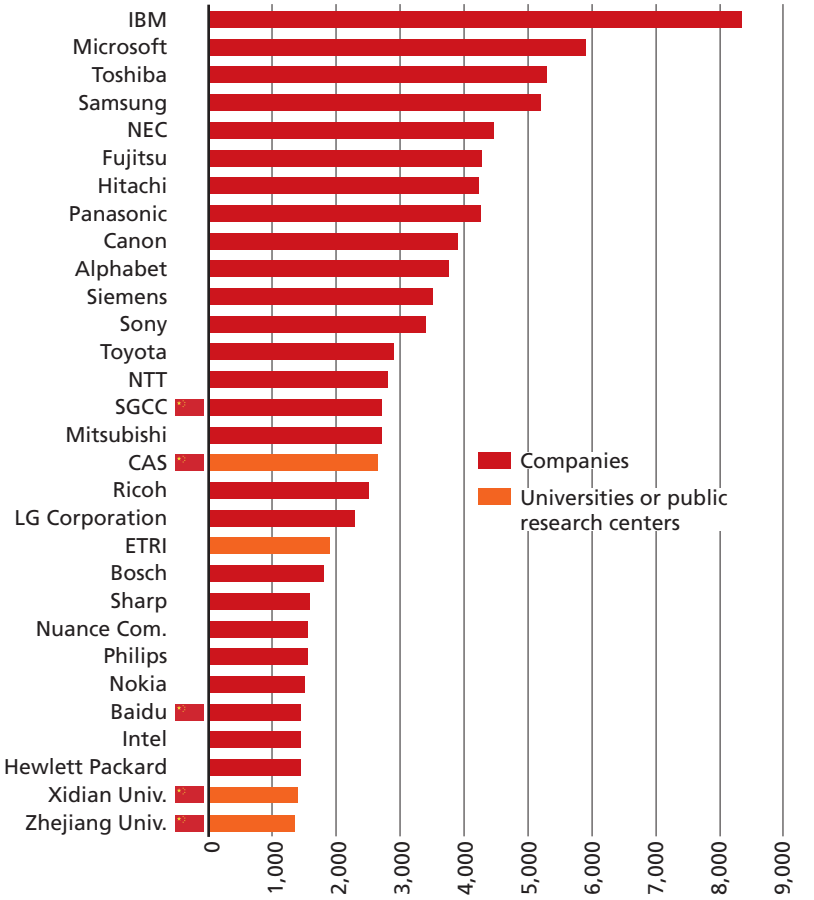
Figures and Tables

Figure 1. TTC: 10 Working Groups

1. Technology Standards Cooperation	**6.** Misuse Of Technology Threatening Security & Human Rights
2. Climate And Clean Tech	**7.** Export Controls Cooperation
3. Secure Supply Chains	**8.** Investment Screening Cooperation
4. ICTS Security and Competitiveness	**9.** Promoting Sme Access To And Use Of Digital Technologies
5. Data Governance and Technology Platform	**10.** Global Trade Challenges

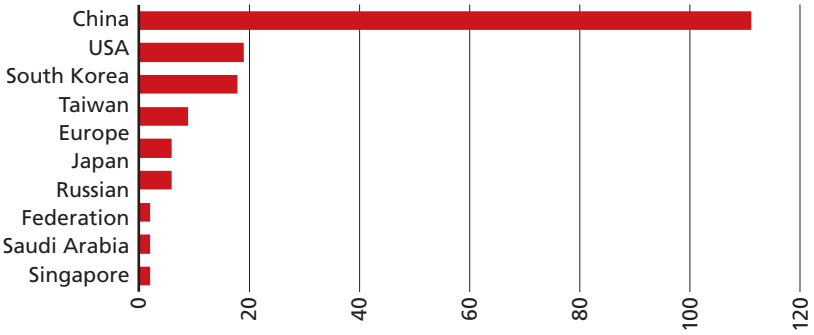
Source: European Commission (Factsheet: EU-US Trade and Technology Council. EU–US Relations).

Figure 2. Top 30 Global AI Patent Applicants; Total number of patents in AI technology



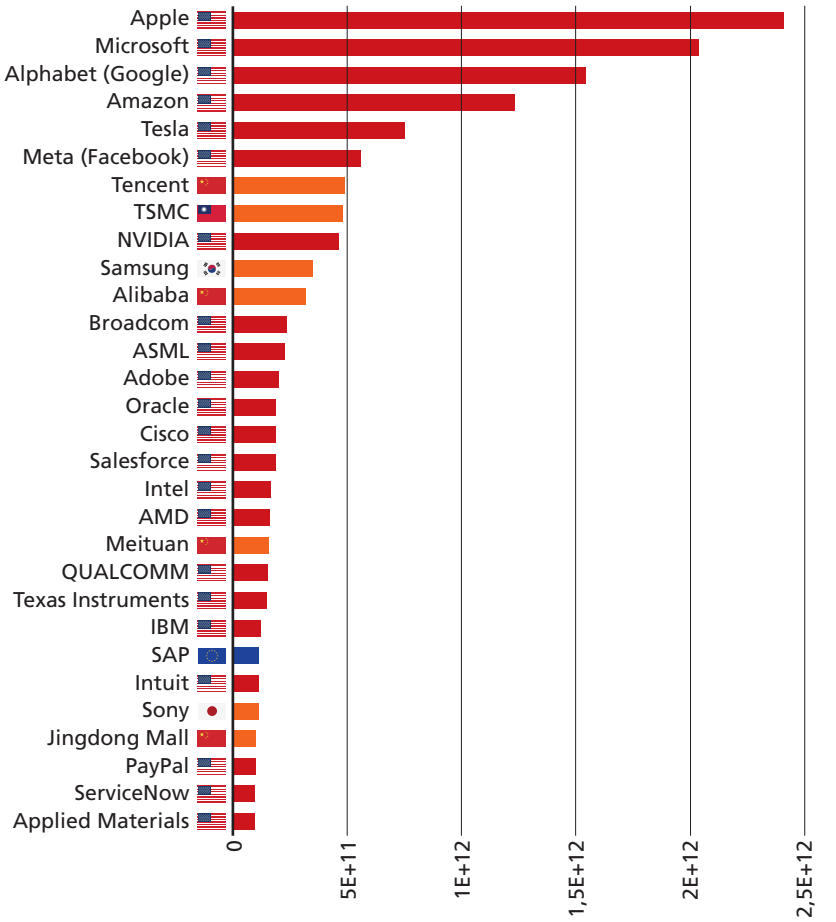
Note: Initials stand for Nippon Telegraph and Telephone Corporation (NTT), State Grid Corporation of China (SGCC), Chinese Academy of Sciences (CAS), and the Electronics and the Electronics and Telecommunications Research Institute (ETRI).
Source: Canals and Pinheiro de Matos, based on WIPO data (2019).]

Figure 3. Geographical origin of universities and public research centres in the top 500 AI patent applicants; Number of organisations



Source: Canals and Pinheiro de Matos, based on WIPO data (2019)].

Figure 4. Top technology companies; Billion dollars



Note: (*) Size by market capitalisation.
Source: Canals and Pinheiro de Matos, prepared using data from https://companiesmarketcap.com/.

Table 1. Composition of EU27 final demand by origin of value added; (% of final demand)

	UE27			USA			China			United Kingdom			Russia			Japan			India	Turkey	S. Korea	Brazil	Canada
	2015-18	1995-2000	2002-2007	2015-18	1995-2000	2002-2007	2015-18	1995-2000	2002-2007	2015-18	1995-2000	2002-2007	2015-18	1995-2000	2002-2007	2015-18	1995-2000	2002-2007	2015-18	2015-18	2015-18	2015-18	2015-18
TOTAL	**85.4**	**89.4**	**87.7**	**2.6**	**2.3**	**2.1**	**1.9**	**0.3**	**0.8**	**1.6**	**1.8**	**1.8**	**0.9**	**0.5**	**0.8**	**0.6**	**0.9**	**0.8**	**0.4**	**0.4**	**0.3**	**0.2**	**0.2**
Agriculture	81.9	87.5	85.1	2.2	1.8	1.8	1.2	0.2	0.5	1.1	1.3	1.2	1.1	0.5	1.1	0.3	0.4	0.3	0.4	0.6	0.2	1.0	0.3
Mining	23.7	42.3	32.5	3.4	2.6	2.1	1.7	0.4	0.4	4.5	4.5	5.9	16.0	4.6	9.8	0.3	0.5	0.3	0.3	0.3	0.1	0.5	0.9
Manufacturing	69.4	79.0	75.1	4.3	4.1	3.7	5.7	0.8	2.2	2.4	3.3	3.0	2.0	0.9	1.7	1.5	2.4	2.0	0.9	1.0	1.0	0.5	0.4
Food	80.5	86.9	84.6	2.2	2.0	1.7	1.7	0.3	0.7	1.9	2.0	2.0	1.0	0.4	0.8	0.4	0.4	0.4	0.6	0.6	0.2	0.9	0.3
Textiles and clothing	51.2	77.4	70.0	1.8	2.2	1.8	19.1	2.6	7.4	1.6	2.4	2.1	0.7	0.4	0.7	0.7	1.0	0.9	3.3	4.0	0.7	0.4	0.2
Wood and paper	83.4	85.5	84.3	2.5	3.0	2.4	1.7	0.4	0.7	1.7	2.2	2.2	1.4	1.1	1.5	0.5	0.7	0.6	0.5	0.4	0.2	0.7	0.3
Coke and refined petroleum products	36.9	53.2	42.8	3.5	2.1	1.9	1.2	0.3	0.5	2.9	4.0	4.1	16.6	9.3	13.3	0.3	0.5	0.4	0.7	0.4	0.2	0.5	0.5
Chemicals and pharmaceuticals	67.3	80.0	73.5	9.4	5.4	7.3	2.9	0.5	1.0	3.3	3.9	4.2	1.5	0.8	1.4	1.2	1.3	1.1	0.8	0.3	0.6	0.3	0.4
Rubber and plastics	77.0	84.0	81.5	3.1	2.7	2.5	3.8	0.7	1.3	2.9	3.6	3.4	1.4	0.6	1.2	1.0	1.4	1.3	0.8	0.9	0.7	0.3	0.2
Other non-metallic mineral products	80.8	88.6	84.4	2.3	1.8	1.6	3.4	0.4	1.6	1.6	2.1	2.0	2.1	0.8	1.5	0.7	0.8	0.7	0.5	0.6	0.3	0.4	0.3
Metals	79.7	85.8	82.8	2.4	2.1	1.8	3.6	0.5	1.4	1.6	2.7	2.3	2.0	1.0	1.8	0.7	1.0	0.8	0.8	0.9	0.5	0.4	0.3
Computers and electronics	45.9	56.3	53.8	8.8	12.1	9.5	17.8	2.0	7.5	1.8	5.5	3.6	0.7	0.4	0.7	4.3	9.1	7.1	0.6	0.4	3.8	0.3	0.4
Electrical equipment	67.5	82.4	78.2	3.3	2.8	2.6	11.1	0.7	2.7	1.4	2.9	2.7	1.3	0.7	1.2	1.9	3.1	2.5	0.8	1.3	1.3	0.3	0.3
Machinery	74.4	79.4	77.8	3.9	4.7	3.8	5.5	0.6	2.0	2.2	3.6	3.1	1.0	0.7	1.1	2.5	3.4	2.8	0.7	0.7	1.0	0.3	0.3
Motor vehicles and trailers	76.7	81.2	78.9	3.0	3.1	2.9	2.9	0.3	1.0	3.3	4.6	3.8	0.9	0.5	0.9	2.7	4.1	3.8	0.6	2.0	1.4	0.3	0.3
Other transportation equipment	53.5	56.1	54.7	15.1	17.0	14.0	5.7	0.7	2.6	4.5	5.6	5.2	1.4	0.7	1.1	2.9	6.6	5.2	0.7	0.6	4.7	0.7	1.4
Other manufactures	73.1	85.2	82.5	4.5	3.0	3.3	7.8	0.9	1.9	1.8	2.6	2.4	0.9	0.6	1.0	1.1	1.0	0.8	0.8	0.7	0.5	0.3	0.3
Services	87.0	90.8	89.6	3.0	2.3	2.2	1.1	0.2	0.5	1.9	1.9	2.0	0.7	0.4	0.6	0.5	0.6	0.5	0.4	0.3	0.2	0.2	0.2
Commercial services	86.0	90.2	88.8	2.9	2.2	2.2	1.6	0.2	0.5	1.9	2.2	2.2	0.8	0.4	0.7	0.6	0.9	0.8	0.4	0.5	0.2	0.2	0.2
Logistics	75.5	82.0	79.2	3.9	3.6	3.2	2.5	0.5	1.2	2.2	2.7	2.7	2.2	1.1	1.7	0.8	1.1	1.1	0.5	0.9	0.3	0.4	0.5
Hospitality	87.7	88.5	88.5	2.2	3.1	2.0	0.8	0.2	0.5	1.3	1.7	1.5	0.6	0.4	0.5	0.3	0.3	0.2	0.3	0.6	0.1	0.3	0.2
Information and communication	78.1	86.6	85.1	6.4	4.0	3.9	1.8	0.3	0.6	3.8	2.8	3.2	0.5	0.3	0.5	0.7	0.9	0.7	1.5	0.1	0.3	0.2	0.4
Financial	84.5	89.6	88.3	4.6	2.8	2.8	0.6	0.1	0.2	3.6	2.9	3.9	0.3	0.1	0.2	0.4	0.4	0.4	0.3	0.2	0.1	0.1	0.2
Real estate	96.6	97.5	97.2	0.7	0.6	0.5	0.3	0.1	0.1	0.5	0.5	0.6	0.2	0.1	0.2	0.1	0.1	0.1	0.1	0.1	0.0	0.0	0.1
Other services	86.4	91.2	89.2	3.9	2.7	3.0	1.0	0.2	0.4	2.5	2.0	2.5	0.5	0.3	0.5	0.6	0.5	0.5	0.4	0.2	0.2	0.3	0.2

Note: Data refer to the average for the years 1995–2000 (before China joined the WTO in 2001), 2002–2007 (after China's joined the WTO, pre-financial crisis) and 2015–2018 (most recent years). The data from the most recent OECD TiVA update in November 2021 are used. The colour of the table reflects the degree of integration between the regions. Blue and green indicate less integration, while orange and red indicate more integration. The first columns show the value added from the region itself. Source: Canals and Pinheiro de Matos, using OECD TiVA data (November 2021).]

Tabla 2. Composition of US final demand by origin of value added; (% of final demand)

	USA			EU27			China			Canada			Mexico			Japan			United Kingdom	India	S. Korea	Brazil	Russia
	2015-18	1995-2000	2002-2007	2015-18	1995-2000	2002-2007	2015-18	1995-2000	2002-2007	2015-18	1995-2000	2002-2007	2015-18	1995-2000	2002-2007	2015-18	1995-2000	2002-2007	2015-18	2015-18	2015-18	2015-18	2015-18
TOTAL	**87.9**	**89.5**	**87.7**	**2.4**	**2.3**	**2.6**	**2.2**	**0.5**	**1.2**	**1.1**	**1.4**	**1.6**	**0.9**	**0.7**	**0.8**	**0.7**	**1.5**	**1.1**	**0.5**	**0.5**	**0.4**	**0.2**	**0.2**
Agriculture	80.8	84.5	83.2	2.6	2.8	2.6	1.4	0.4	0.7	2.3	2.0	2.3	2.3	1.3	1.8	0.4	0.9	0.6	0.5	0.5	0.2	0.5	0.3
Mining	90.7	88.7	88.1	1.7	3.2	2.4	1.0	0.2	0.5	1.4	1.8	2.1	0.6	0.4	0.6	0.5	1.0	0.7	0.4	0.2	0.2	0.2	0.4
Manufacturing	61.9	72.0	65.1	7.4	5.8	7.0	8.4	1.5	4.2	3.0	3.7	4.1	3.3	2.0	2.5	2.8	4.8	4.0	1.0	1.1	1.6	0.5	0.4
Food	81.1	85.9	83.5	3.4	3.0	3.3	1.9	0.4	0.9	2.4	2.2	2.6	1.8	0.9	1.3	0.5	0.9	0.7	0.6	0.7	0.3	0.4	0.2
Textiles and clothing	22.3	60.5	40.9	5.7	6.7	8.1	37.1	6.8	18.9	1.0	1.6	1.8	2.3	2.6	3.0	1.2	1.8	1.8	0.5	4.4	1.4	0.6	0.4
Wood and paper	77.7	80.1	75.9	4.3	3.4	4.4	3.2	0.8	1.4	4.9	7.7	8.1	1.1	0.6	0.9	0.8	1.3	1.1	0.5	1.6	0.5	0.8	0.3
Coke and refined petroleum products	63.8	58.8	53.2	2.2	2.9	2.7	0.8	0.3	0.4	9.3	6.6	8.7	2.3	3.5	3.9	0.4	0.7	0.4	0.7	0.6	0.3	0.8	1.9
Chemicals and pharmaceuticals	66.5	78.8	72.0	14.8	8.3	11.7	2.7	0.6	1.1	1.7	1.9	2.4	0.5	0.7	0.8	1.3	2.2	1.6	1.8	1.6	0.5	0.2	0.3
Rubber and plastics	72.4	80.6	74.1	5.2	3.7	4.8	6.2	0.9	2.3	3.1	5.1	6.6	2.0	1.1	1.5	1.5	2.2	2.0	0.8	0.8	1.1	0.4	0.4
Other non-metallic mineral products	78.5	83.1	79.0	4.4	5.2	5.2	5.8	1.0	3.4	2.1	2.3	2.5	1.4	1.0	1.3	0.9	1.9	1.1	0.5	0.8	0.4	0.6	0.3
Metals	73.0	78.7	73.6	5.0	4.6	5.1	4.8	0.7	2.4	3.0	3.8	4.7	2.6	1.0	1.7	1.2	2.5	1.7	0.7	1.8	0.8	0.7	0.8
Computers and electronics	50.6	65.8	56.3	5.1	4.0	5.7	19.8	2.0	9.2	0.9	1.9	1.4	3.4	2.5	3.2	3.6	9.8	7.5	0.5	0.4	4.3	0.2	0.3
Electrical equipment	49.4	71.2	60.2	7.8	5.9	7.8	18.8	1.9	6.4	2.0	2.8	3.2	5.4	3.4	4.9	3.8	6.2	5.3	0.6	0.8	2.2	0.5	0.5
Machinery	59.5	69.4	63.2	11.0	9.8	11.5	8.1	1.0	3.5	2.8	2.9	3.5	3.2	1.1	1.9	5.1	7.5	6.3	1.1	0.8	1.7	0.6	0.4
Motor vehicles and trailers	53.2	64.6	57.1	9.8	7.1	8.9	5.5	0.6	2.0	4.7	8.0	7.7	8.8	3.7	4.5	7.1	9.6	10.2	1.4	0.6	3.2	0.5	0.4
Other transportation equipment	71.3	70.9	69.3	8.0	9.1	9.1	3.6	0.6	1.7	2.9	3.9	4.3	1.9	1.0	1.2	2.8	4.3	3.5	1.7	0.4	0.9	1.2	0.4
Other manufactures	55.2	74.1	65.5	7.8	6.4	7.0	16.0	3.5	7.8	2.0	2.9	3.1	2.0	1.4	1.4	1.2	1.5	1.3	0.8	3.1	0.7	0.4	0.5
Services	91.8	93.3	92.1	1.8	1.7	2.0	1.0	0.2	0.5	0.7	0.9	1.0	0.5	0.5	0.5	0.4	0.7	0.6	0.6	0.5	0.2	0.1	0.1
Commercial services	89.0	90.0	88.7	2.4	2.2	2.6	1.8	0.4	0.9	1.2	1.5	1.7	1.1	0.8	1.0	0.7	1.5	1.2	0.6	0.3	0.3	0.2	0.1
Logistics	77.3	80.2	75.8	5.3	5.6	6.2	2.7	0.6	1.5	2.1	2.1	2.6	1.4	1.4	1.6	1.1	1.7	1.5	1.0	0.6	0.4	0.3	0.5
Hospitality	88.2	87.9	88.0	2.8	3.6	3.1	0.8	0.3	0.5	1.0	1.4	1.5	1.1	1.1	1.1	0.5	0.5	0.4	0.6	0.5	0.2	0.2	0.1
Information and communication	91.4	94.2	93.1	1.7	1.4	1.6	1.1	0.2	0.5	0.7	0.8	0.9	0.3	0.3	0.3	0.4	0.8	0.6	0.5	1.6	0.2	0.1	0.1
Financial	93.3	95.9	93.4	1.5	1.1	1.8	0.4	0.1	0.1	0.4	0.4	0.5	0.1	0.1	0.1	0.3	0.3	0.4	1.5	0.2	0.1	0.1	0.1
Real estate	97.5	98.1	97.5	0.5	0.5	0.5	0.3	0.1	0.1	0.3	0.2	0.3	0.1	0.1	0.1	0.1	0.2	0.1	0.2	0.1	0.1	0.1	0.0
Other services	92.2	95.1	93.4	2.1	1.5	2.0	0.8	0.2	0.3	0.5	0.6	0.7	0.3	0.2	0.2	0.5	0.6	0.5	0.7	0.4	0.4	0.2	0.1

Note: Data refer to the average for the years 1995–2000 (before China joined the WTO in 2001), 2002–2007 (after China's joined the WTO, pre-financial crisis) and 2015–2018 (most recent years). The data from the most recent OECD TiVA update in November 2021 are used. The colour of the table reflects the degree of integration between the regions. Blue and green indicate less integration, while orange and red indicate more integration. The first columns show the value added from the region itself. Source: Canals and Pinheiro de Matos, using OECD TiVA data (November 2021).]

THE EUROPEAN COMMISSION'S PROPOSED ANTI-COERCION INSTRUMENT FROM AN INTERNATIONAL LAW PERSPECTIVE

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In a global context characterised by rising geopolitical and economic tensions, the European Union (EU) is equipping itself with new tools to ensure its open strategic autonomy and promote fairer and more sustainable international trade. In principle, it wants the rules of the World Trade Organization (WTO) to be reformed and updated. But repeated failures to reach significant global consensus, particularly with China and other emerging economies, is leading the EU to opt to negotiate regional trade agreements and to endow itself with new autonomous legal instruments. Examples include a general sanctions regime for human rights violations, a corporate sustainability due diligence directive, a regulation on foreign subsidies that distort the internal market, a regulation on international public procurement, a carbon border adjustment mechanism, and a new initiative to combat deforestation (Erixon et al., 2022). Far from pursuing discriminatory, protectionist unilateralism, these instruments seek to project essential values and contribute to designing a new regulatory framework for international trade.

Of these instruments, this paper will focus on the Proposal for a Regulation of the European Parliament and of the Council on the protection of the Union and its Member States from economic coercion by third countries (COM(2021) 775 final), which was presented on December 8th 2021. For brevity's sake it will be referred to as the "anti-coercion instrument".

In essence, the instrument aims to establish rules and procedures for the EU to defend itself from economic coercion by third states and includes commercial countermeasures based on international law. At the time of writing, the proposal remains under review by the European Parliament and Council, with the final text expected to be approved by the end of 2022. Several specialists have already commented on the proposal (Baetens and Bronckers, 2022; Hackenbroich, 2022; Szczepanski, 2022), and this paper will contribute a brief analysis from an international law perspective.

First, the paper will focus on what economic coercion means in international relations. Second, the various options states have to defend themselves against economic coercion will be set out, including the

possible use of countermeasures. Third, the question of why the EU needs to adopt an anti-coercion instrument will be examined. Finally, potential incompatibilities between the instrument and WTO rules will be addressed, along with how these issues may be handled.

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1. What is economic coercion in international relations?

Article 2.1 of the European Commission's proposal states that a third country engages in economic coercion when it "interferes in the legitimate sovereign choices of the Union or a Member State by seeking to prevent or obtain the cessation, modification or adoption of a particular act by the Union or a Member State … by applying or threatening to apply measures affecting trade or investment".

In serious cases, at least, economic coercion may involve the violation of one of the basic principles of international law: the "duty not to intervene in matters within the domestic jurisdiction of any State[1]",wherein "No State may use or encourage the use of economic … measures to coerce another State in order to obtain from it the subordination of the exercise of its sovereign rights and to secure from it advantages of any kind".

The impact assessment report annexed to the European Commission proposal (SWD(2021) 371 final) gives numerous examples of economic coercion in international practice committed by countries including China, the United States, Indonesia, Russia and Turkey. Various cases involve China, whose rise as a great global power has significantly increased its ability to exert pressure. China's economic coercion activities have affected a range of countries and have on many occasions been conducted silently, informally or covertly (Harrell et al., 2018).

In 2020, for example, Australia proposed an international investigation be conducted into the origins of the COVID-19 pandemic. Since then, China has applied a host of trade restrictions against Australia, in some cases under the guise of standard trade defence measures like anti-dumping and countervailing duties on barley and wine, creating a formal separation from any political motivation (Ferguson and Lim, 2021).

Lithuania is another example. In July 2021, the Baltic state announced that a Taiwanese representative office would be opening in Vilnius. Since then, China has applied multiple trade restrictions against Lithuania, both formally and informally (Szczepanski, 2022: 3).

2. How can economic coercion be defended against?

States subjected to economic coercion may respond in various ways. Often, they end up bowing to the pressure or bearing it stoically. But, if a coercive measure is considered incompatible with the rules of the WTO or any other trade or investment agreement in force between the parties involved, the affected state may file a claim via the relevant dispute settlement system.

1. As stated, among other international instruments, in the Declaration on Principles of International Law approved by Resolution 2625 (XXV) of the General Assembly of the United Nations (UN), of the 24th of October 1970.

Australia, for example, has complained to the WTO about China's anti-dumping and countervailing duties on barley (WT/DS598/1) and wine (WT/DS602/1). The EU has also launched a case against China at the WTO over the trade restrictions imposed on Lithuania, submitting a request for consultations on January 27th 2022 (WT/DS610/1), initiating the dispute settlement procedure.

The WTO's dispute settlement mechanism has yet to resolve these recent allegations of Chinese coercion. And it is also worth noting that while that this defensive route can contribute to combatting economic coercion, it is not enough. In particular, the WTO's adjudicating bodies have limited jurisdiction and are restricted to determining whether or not the trade measures implemented are compatible with the specific rules of the WTO. They do not examine economic coercion in the light of international law, as this lies beyond their competence.

The WTO's adjudicating bodies (like those of other trade or investment agreements) thus limit themselves to their own sphere of competence (examining the issue from their particular perspective). They cannot determine that a state has violated a basic principle of international law like non-interference, nor can they draw out all the legal implications (such as the obligation of reparation) provided for in the general rules on the responsibility of states for internationally wrongful acts[2].

In theory, other means of peaceful dispute settlement may be used to respond to an internationally wrongful act under the general rules of international law, including negotiation, conciliation, arbitration, among others. Ideally, states affected by economic coercion could appeal to a competent international court to rule on whether a basic principle of international law has been violated. But this is not easy, because there is no generalised mandatory interstate jurisdiction in the international legal system, and the UN's International Court of Justice (ICJ) can only prosecute if a state has in some way consented to it.

The ICJ's weakness, and that of the international legal system in general, mean that so-called unilateral self-help measures remain protected by international law, and usually take the form of retaliation or countermeasures. Retaliation sees the injured state take unfriendly measures against the responsible state, such as freezing negotiations over a treaty or ruling out future uncommitted investments. Countermeasures, meanwhile, may mean the injured state fails to comply with one or more international obligations it has towards the responsible state in order to force a halt to the illegal act and seek redress for the damages caused. Thus, states subject to economic coercion may seek to defend themselves by applying countermeasures.

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3. Should the EU approve an anti-coercion instrument?

Approving an anti-coercion instrument is a legal necessity for the EU for several reasons. In principle, by virtue of its sovereignty, any state in the world is competent to resort to countermeasures based on the general rules of international law. As an international organisation, however, the EU's powers are conferred via a legal instrument that the EU itself

2. Rules codified in the Draft Articles adopted by the International Law Commission (CDI) in 2001 and annexed to Resolution 56/83 of the UN General Assembly, of December 12th 2001.

promulgates, and which defines its action. The EU is already endowed with provisions that allow it to impose international sanctions within the framework of its Common Foreign and Security Policy (CFSP), like those the Council approved on Russia following the armed aggression against Ukraine, as well as in the final stage of the WTO's dispute settlement process. However, in cases of economic coercion by third countries, the EU lacks a specific instrument that enables the European Commission (without the need for Council intervention) to deploy countermeasures in the areas covered by the common commercial policy (e.g., imposing import restrictions on goods, services, foreign investment, etc.).

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It should also be recalled that in cases like Lithuania's economic coercion by China, EU member states cannot unilaterally raise customs tariffs or apply other trade restrictions on third countries, as these fall within the EU's exclusive competence for the common commercial policy. The proposed anti-coercion instrument will allow the European Commission to defend EU interests and those of each member state, acting, in this case, like a federal state that considers itself injured as a whole by coercion against any of its members.

The proposed anti-coercion instrument grants broad powers to the European Commission to classify specific actions by third states as economic coercion and to respond via negotiation or other international dispute settlement mechanisms and, as a last resort, to apply trade countermeasures.

4. What incompatibilities may arise with WTO rules?

The annexes to the proposal for an anti-coercion instrument set out the measures the European Commission can take in response to a third state engaging in economic coercion. They include, for example: "the imposition of customs duties beyond the most-favoured-nation level, or the introduction of any additional charge on the importation … of goods".

From the outset, these and other planned measures clearly conflict with the basic principles of the WTO (and of other trade and investment agreements concluded by the EU) and are difficult to justify given the exceptions already provided for in these regimes. However, the exceptions to the current General Agreement on Tariffs and Trade (GATT) from 1994, including those related to public morals or security, are not easily applicable in many cases of economic coercion. The security exception relating to restrictions imposed in the event of "serious international tension" is undoubtedly open to multiple interpretations. For example, when tensions escalated between Russia and Ukraine after Euromaidan in 2013 and Russia's illegal annexation of Crimea in 2014, Russia imposed trade restrictions on the transit of goods with Ukraine. In 2016 Ukraine filed a complaint against Russia at the WTO. In the report issued in 2019 the adjudicating body handling the case specified that a member invoking this type of exception must be able to demonstrate the "veracity" of the relationship between the measures imposed and "security interests" (WT/DS512/R, paragraph 7.134). The conclusion in this case was that Russia was entitled to an exception on security grounds, due to the confrontation between the

two countries – a clear sign of the ample discretion the WTO grants states in this area. However, in many cases of economic coercion there is no active or potential armed conflict between the countries involved, and they can hardly be considered security-related.

It should be underlined that the European Commission's proposed anti-coercion instrument does aim to not justify restrictions imposed in response to economic coercion in the light of specific exceptions provided for in WTO rules or other trade and investment regimes. Rather, its justifications are drawn from the general rules on countermeasures in international law, addressing the subject less in terms of violations of a particular rule, than of counteracting economic coercion that amounts to a violation of a basic principle of the international legal order.

The WTO does not explicitly prevent the use of countermeasures amounting to non-compliance with its rules in response to breaches of international obligations.

The question of whether particular WTO rules can be breached by countermeasures based on international law has long been contentious among scholars. Some authors (Bartels, 2002: 396) argue that they cannot, because, when it comes to countermeasures, WTO law is a discrete system that is disconnected from the rest of the international legal system.

Other authors (Fernández Pons, 1999: 99; Kuijper, 2008: 706) note that the WTO does not explicitly prevent the use of countermeasures amounting to non-compliance with its rules in response to breaches of international obligations outside its regime. In practice, certain cases appear to demonstrate this. Thus, when Argentina refused to comply with certain rulings by the International Centre for Settlement of Investment Disputes (ICSID) and the United States excluded it from its generalized system of preferences for developing countries, to which it was entitled by virtue of the Enabling Clause in force at the WTO, Argentina made no complaint at the WTO against this US "countermeasure" (Fernández Pons and Lavopa, 2013: 249–250).

The European Commission's proposed anti-coercion instrument fits with the latter approach (Baetens and Bronckers, 2022: 5). In the case of economic coercion that violates, among other things, general rules of international law, it includes the possibility of the EU adopting certain trade restrictions that are clearly incompatible with the most basic substantive WTO rules. Disregarding the specific WTO exceptions, it provides such actions with direct protection as countermeasures in international law.

From a procedural point of view, a further question may be raised. What would happen if the state engaging in economic coercion (for example, China) filed a complaint at the WTO against the trade restrictions adopted by the European Commission under the anti-coercion instrument?

The EU could attempt to defend itself by invoking one of the exceptions provided for in WTO law – claiming, for example, that "serious international tension" affects its security. Certain authors (Azaria, 2022) have argued that the WTO's adjudication bodies should, as an incidental question, find in favour of an EU defence based on the general rules on countermeasures in international law. However, given their circumscribed jurisdiction, the WTO's adjudication bodies seem highly unlikely to accept such a defence.

The European Commission is aware of this. However, the impact assessment points out that, on the one hand, the state engaging in economic coercion will not always react by filing complaints against the anti-coercion measures the institution employs (so as to avoid, for example, airing their original misconduct). On the other hand, without prejudice to what the WTO's adjudicating bodies may decide in reference to its particular regime, the EU will continue to feel entitled to impose anti-coercion measures under the general rules of international law (SWD(2021) 371 final, pp. 16, 22, 23, 41–43).

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5. Final considerations

Economic coercion at an international level is nothing new. But in an increasingly Hobbesian or anarchic international landscape it is a growing issue. Economic coercion involves not only the violation of particular commercial or investment obligations, but also of general norms of international law. Neither the WTO nor other international institutions currently offer specific or fully adequate means of defence against economic coercion. Hence, states often try to defend themselves using self-help measures typical of international law, such as so-called countermeasures.

In a context like the current one, the European Commission needs an anti-coercion instrument in order to defend the EU and its member states from economic coercion by applying trade countermeasures in accordance with the general rules of international law. In some cases, the states that initiate the economic coercion are likely to react with more means of exerting pressure and/or challenge specific anti-coercion measures adopted by the European Commission at the WTO (or other fora), which are unlikely to accept the EU's defence based on the general rules of international law, given the limited nature of their specialised jurisdictions. Nevertheless, the legal basis for European Commission's proposed anti-coercion instrument are basic norms of the international legal order, and the instrument must be conceived, essentially, as a deterrent mechanism that is gradual in nature, and which should be administered with caution.

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China has become a key player on the global economic stage, including for local European economies like Barcelona's. But its role in international trade causes tensions. The development model entailed by Chinese "state capitalism", with its state-owned companies, subsidies and forced transfers of intellectual property, distorts the world economy. Meanwhile, the fall-outs between China and the United States only seem to increase, in what is already seen as a new episode of great power competition. The European Union, for its part, is busy redefining its strategy with China, following the failure of the investment agreement signed in 2020.

In this context, the chapters in this volume seek to grasp the central axes of Chinese economic policy, and its main effects on the rest of the world, focusing on the reaction of the European Union. The content is structured into two parts: the key elements of Chinese economic policy are examined first, and then potential European responses are presented.