EU Trade and Investment with China: Changes, Challenges and Choices

Speech by Peter Mandelson at the EU-China Conference

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Summary

EU Trade Commissioner Peter Mandelson asks how Europe and China can ensure that Europe faces up to the Chinese challenge, and that European businesses do not "meet a Chinese wall rather than an open door". He asks: "How do we build bridges with China rather than throwing up protectionist barriers?"

Mandelson argues that "Europe is looking for a broad-based twenty-first century partnership based on converging values and economic interests". He argues that Europe needs to adapt to China's dramatic rise, and China needs to meet its WTO obligations and recognise its massive new weight in the global economy. He says: "China sometimes still talks as if it is at the edge of the WTO system looking in. But China now is the system".

Mandelson argues that China is turning "our whole approach to the European supply chain… on its head". With European companies investing heavily in China and producing manufactures there, Mandelson asks "what do we mean when we say 'cheap Chinese exports' are threatening European livelihoods?"

Mandelson echoes the call from European business for fair treatment in China, arguing that China needs to better enforce intellectual property rules and improve access for European investment and European imports. He says: "Too often Europe's businesses meet a Chinese wall rather than an open door". Ultimately, he argues, this will make it hard to silence calls for greater protection from China in Europe.

Mandelson says China faces huge social, economic and environmental challenges including completing the transition to a market economy, addressing the environmental costs of rapid development and meeting the expectations of its growing middle class of access to education and health care.

Mandelson concludes: "Is there the material for a grand bargain here? I believe there is. China has everything to gain from successful integration into the global economy… It has benefited hugely from global trade liberalisation and with that comes new responsibilities. In return, Europe must accept the Chinese challenge to adapt and compete".

Towards the strategic review

In a few months from now, I intend to publish a strategic review that aims to bring a new sense of direction and coherence to Europe's trade and economic policy towards China.

In its political relationship with China, Europe has always been constructive and frank. Our expectations on political pluralism, human rights, and democratic reform in China are clear. It is important to bring the same clarity to our economic relationship, because in the global economy there is no Chinese wall between trade and politics. Europe is looking for a broad-based twenty-first century partnership based on converging values and economic interests. The question is: is China looking for the same?

In a year and a half as Europe's Trade Commissioner I have visited China five times. This reflects a simple reality. China is the single greatest challenge to European trade policy: diplomatically, politically, and commercially. It is the fastest changing part of a fast changing world. It is a source of anxiety, but it has also set alight Europe's commercial imagination, and re-energised its spirit of enterprise. This is welcome.

I have always been an Asia-minded person - I came to the work of EU Trade Commissioner with a sense that we have allowed Europe's trade policy to be overtaken by the pace of change in Asia, and nowhere more than in China. China is reshaping the global economy. We simply have to get our relationship right.

The EU-China relationship: A thousand relationships

Europe's commercial relationship with China is built on thousands of contractual relationships, literally tens of millions of transactions. At the end of the 1970s China accounted for less than 1% of global exports. By the turn of the century it counted for 5%. Now, China's exports are rising by 15% or more a year. 20 years ago Europe's trade relations with China were, literally, negligible. Today we are China's largest trading partner and our bilateral trade is worth about 200 billion euros a year. Europe invests hugely in China. It buys in China. It sells to China. Increasingly, it produces in China.

But our economic relationship is, of course, also made up of the hundreds of European businesses who have found themselves at the sharp end of competition with China over the last decade. Who find themselves competing with China in labour-intensive low-cost production. And beyond those on the commercial frontline, there are the trades unions, civil society groups and private citizens for whom the EU-China relationship matters for any one of a hundred reasons.

Our strategic review must take all these diverse experiences into account. In our initial consultations we have already approached more than 200 European companies. We have received more than a thousand pages of submissions from businesses and citizens through our on-line consultation.

Today's conference is a part of that process. Today, more than anything, I am here to listen.

How do we integrate China into the global economy?

For that reason, let me frame my remarks today as a series of questions.

China has achieved its 5% of global trade and global GDP in a staggeringly short time. If the current rates of growth in China and the world economy continue, it seems likely that by 2030 China's share will rise to around 15%. China will overtake the US to become the world's second largest exporter after Europe. China will - by some estimates - produce half the world's textiles. It is already the world's biggest user of steel, copper, coal and cement.

There is a view that says that, because of the phenomenal rise of China and the other Asian economies, the 21st century will somehow "belong" to them. But of course these growing economies are part of a global economy - they sell into our markets and will increasingly invest here, but we sell and invest there too. That's why China's energy policy, its currency policies, its relationship between the market and the state - will impact as much on those who trade with China as on the Chinese themselves.

So my first question is this: is China's growth sustainable? Are we right to plan on this basis? Politically, socially and environmentally, will it last?

Second, if our answer is yes, then how do we integrate an economy on this scale, changing this fast, into the global trading system? Can it absorb continued rapid growth of this kind? China has now been in the WTO for five years, and we can legitimately ask how far it has come in meeting the expectations placed on a WTO member. China sometimes still talks as if it is at the edge of the WTO system looking in. But China now is the system.

How can Europe adapt?

My next set of questions relate to Europe's own reaction to China. What will be China's impact on traditional sectors of the European economy? Which of our Member States will be most affected? What does it mean for jobs? What does it mean for interest rates, for energy and commodity prices and for the euro? What does it mean for our exports, our technology, our brands - our whole approach to the European supply chain?

I have not seen similar figures for Europe, but in the US, cheap imports from China are estimated to have saved US consumers half a trillion dollars in the last decade, and saved manufacturers probably about the same in cheaper inputs for domestic production. Those savings are invested or spent elsewhere in the economy.

China is turning our picture of what constitutes European production, or even the European economic interest, on its head. France and Italy are Europe's two biggest textile and clothing producers. They are also among Europe's biggest importers of clothing and textiles from China precisely because they are Europe's biggest textile and clothing producers. So we can and should ask: what do we mean when we say "cheap Chinese exports" are threatening European livelihoods?

China's initial challenge for Europe has been to low-cost labour-intensive manufacturing, particularly clothes and textiles and shoes. But increasingly, as China deepens its investment in research and development and moves into higher-cost production it will be cars and precision manufacturing. And after that aircraft and marine engineering.

It is hard to overstate the challenge that this will pose for Europe. Our response will be decisive for our own competitiveness. How do we maintain a comparative advantage in the high-tech, high-value, design-driven production in which we are the global leader? How do we help workers adjust to economic change in Europe? How do we prevent fear of heightened competition being channelled into political pressure for economic protection? How do we build bridges with China rather than throwing up protectionist barriers, whilst retaining our right to use legitimate trade defence measures?

What do we need from China…?

These questions are related to a third set of questions. Because Europe's reaction to China will of course be conditioned by China's own conduct, and by the extent to which Europeans feel that the Chinese market is open to our goods and our investment, on fair terms of competition. Does China offer a level playing field? How really open is the Chinese market?

China is a growing market for the things the EU produces best. 50 million Chinese already have a standard of living equivalent to that of the European middle class. Yet, for every four containers loaded at Shenzen for Europe, three still come back empty. This has nothing to do with a lack of European entrepreneurialism. But if those containers stay empty because the rights of European businesses are not being properly protected in China, or because they do not have proper access to the Chinese market, then we will have a big problem. An economic problem, but then also a major political problem.

Even from the early results of our public consultation it is clear that many European businesses feel that they are not getting a fair deal in China. Barriers to EU investment range from the inadequate protection of Intellectual Property to regulatory restrictions on investment and services trade. Safety standards, and market access regulation are applied disproportionately, or inconsistently, or in the case of IPR protection - not really at all.

Too often Europe's businesses meet a Chinese wall rather than an open door. Just last week there were fresh complaints from European construction companies that capital requirements and rules limiting them to joint ventures are barring them from effective competition in China - at the same time as Chinese construction companies are expanding rapidly overseas. China is now the sixth largest engineering contractor in the world. Economic nationalism is wrong for Europe and it is wrong for China.

So any strategy that the EU and China develop must offer concrete commitments to resolving such problems. We cannot simply be offering jam tomorrow for EU business in China, while the bread and butter of our own markets is on the table for Chinese exporters today.

We can, and must, live with some asymmetry for now, but not forever. Particularly in the manufacturing sector, the global playing field is levelling fast and Europe will not be the only one making concessions. As China's exports keep increasing, so will the pressure for China to deliver real opportunities to its trading partners.

…and what does China need to do for itself?

Of course, there is a further set of questions - China also faces its own internal political challenges. A country of China's scale, whatever its political system, has to manage economic growth in a way which narrows the widening social gaps between rich and poor, or in China's case between the developed coastal regions and the rural West. Will China be able to reform its banking sector to cope with rapid expansion? How will China clean up the environmental scars left by rapid growth? How will it continue to navigate the difficult political transition to a market economy?

It is impossible to imagine effective answers to these questions that do not require China's openness to the world. China's energy consumption and the environmental costs of its rapid industrialisation affect us all. Chinese stability will be built on a strong Chinese economy with strong domestic industries; decent jobs, effective financial and physical infrastructures, and a modern Chinese welfare and health system. How will China meet the expectations of its rapidly growing and ageing population - particularly its growing, entrepreneurial middle class?

China will need to unlock some of its high levels of personal savings - among the highest in the world, about half of Chinese GDP in 2005. High savings are depressing domestic consumption, pushing Chinese producers to produce for export, and funnelling savings into fixed state investment that runs the risk of creating excess capacity. This is a recipe for trade friction.

How do we handle the frictions?

Which leads to a fifth set of questions: how shall we handle the frictions that are inevitable in a fast expanding economic relationship? If Europe and China are like two huge weather fronts meeting, then some turbulence is inevitable. On textiles, and shoes, on car parts and intellectual property rights protection we have already had a sense of what we need to handle.

How do we ensure that these tensions do not spill over into the wider relationship? How do we ensure that they do not undermine confidence in globalisation and confidence in China? Can we maintain what I believe is a strong mutual commitment to a collaborative, non-confrontational trade relationship?

Not just a 21st century silk road: the broader relationship

Part of the answer lies in greater mutual understanding and constant dialogue. I have already suggested that trade is only one part of the wider EU-China relationship. Trade will not be partitioned off from our wider dialogue on the environment, energy politics and social and political rights. Nor should it be.

We need to ask: how can we strengthen co-operation in areas like education? Young European business leaders need more hands on experience in China, and I would like to see Europe welcome more Chinese graduates and trainees.

How can we build on research or technology-projects like Europe's Galileo satellite navigation system which will start operating within three years with Chinese participation? Or the ITER nuclear fusion research programme which also brings together European and Chinese expertise?

Is there a grand bargain?

And so to my final question: is there the material for a grand bargain here? I believe there is.

China has everything to gain from successful integration into the global economy. While its focus in the years to come will be on managing the process of domestic adjustment, by looking outwards, by engaging with the international economy, it can ease this process of change. China's journey from the periphery to the centre of the global economy is all but complete. It has benefited hugely from global trade liberalisation and with that comes new responsibilities.

We in Europe cannot afford to be naïve. China's growth will accelerate a painful process of adjustment here in Europe. Protectionist voices will be raised and if - if! - the public perception is that China is closed to our trade while benefiting from our openness then they will be impossible to silence.

China must continue to work to meet its WTO obligations and it must commit to playing by the rules. In return Europe most accept the Chinese challenge to adapt and compete. That is the grand bargain.

I've left you with two dozen questions. Now I look forward to hearing your answers.