

**Summary:** The Europe-China economic relationship is too big, and too well developed, to fail, but the protection of past achievements is currently the only factor keeping EU-China policy relations in balance. Cooperation on trade and investment is fraught with misunderstanding, offended egos, discontent, and anger. Beijing and Brussels seem content to wait for China's new leadership to take office before they attempt to deepen economic and commercial policy cooperation, but there is little reason to believe that the bilateral relationship will radically improve under changes in the Chinese capital. The EU has tried time and time again to pressure China into opening more of its market to European exports by threatening to cut access to its own markets if Beijing does not comply. And China has repeatedly tried to bypass Brussels in its negotiations with Europe, preferring instead to work through member states. But a fractured EU will have negative long-term consequences for China and its economic interests.

## When Sisyphus met Icarus: EU-China Economic Relations during the Eurozone Crisis

By *Fredrik Erixon*

### Introduction

The Europe-China economic relationship is too big, and too well developed, to fail. Bilateral exchange recovered quickly from the sharp drop in 2008-09, and bilateral trade, despite the overall contraction in the eurozone, increased considerably in 2011. Even if growth in trade and investment were to slow in 2012, the European Union and China will, under current forecasts, post a record high with two-way trade exceeding €500 billion. The EU is China's biggest trading partner, and China is the EU's second biggest. Neither party will allow the relationship to be fractured by economic and commercial policy conflicts. It is a sign of maturity that current volumes of trade and investment glue the relationship together. That's the good news. The bad news is that the protection of past achievements is currently the only factor keeping EU-China policy relations in balance.

### The EU-China Trust Deficit

The climate of EU-China policy cooperation has soured considerably in the past two years. Cooperation on trade and investment is fraught with misunderstanding, offended egos, discon-

tent, and anger. In some quarters, frustration is reaching a boiling point. The EU-China High Level Economic and Trade Dialogue, which followed hard on the heels of the U.S.-China Strategic and Economic Dialogue, has become largely dysfunctional, both as a forum for efficient, business-style negotiations on selective market-access issues and as a venue for forming joint strategic visions for future bilateral economic relations. In some policy areas, e.g. the growing dispute over the EU's carbon fees for aviation, relations are not far from complete breakdown. Key officials do not speak to each other. E-mails and phone calls go unanswered.

There is generally little energy in EU-China talks, and few expect much from them. While U.S. newspapers ran series of articles about the Valentine's Day visit of Xi Jinping, China's President-in-waiting, to the United States, the European media barely bothered to pass comment on the fact that, at the same time, the EU's top leadership – including the President of the European Commission, José Manuel Barroso, and the President of the European Council, Herman Van Rompuy – were in Beijing for the EU-China

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summit. Obviously, there is an air of excitement when European leaders such as Chancellor Merkel meet with the Beijing leadership, but national European leaders do not speak for the EU and cannot engage in most economic matters of importance.

Moreover, despite Premier Wen Jiabao's recent defense of a Chinese role in the European Financial Stability Facility (EFSF) and the smaller sums that Beijing has contributed quietly, there is little hope that China will play a greater paymaster role to eurozone countries with wrecked public finances. This is partially due to the failure of Europe's leaders to build China's and others confidence as they pleaded for contributions to the EFSF, more popularly known as the "eurozone's bailout fund." The morning after the eurozone leaders had agreed to court investors to leverage the paltry financial guarantees they had given to the EFSF, French President Nicolas Sarkozy called Chinese President Hu Jintao. Sarkozy was preparing the ground for the message that the EFSF's chief executive officer, Klaus Regling, who boarded a flight to Beijing before the ink had dried on the agreement, would deliver in person the next day: Europe is finally getting its act together; what had been agreed at the crisis summit in October was what was needed to avoid the euro cooperation slipping into chaos; and China now had a unique investment opportunity that would earn them a good return while at the same time helping its key trading partner. And yet, six weeks later, eurozone leaders were in Brussels once again for another crisis meeting to address the profound threats to financial stability in Europe.

That China rejected these requests, disavowed past promises of considerable bilateral loans to individual crisis countries in Europe, and instead aired positive (but guarded) views on increasing its financial support to the International Monetary Fund is a sign of China's frustration with matters related to Europe. Beijing's core strategy had been to deal directly with Europe, preferably through national capitals, allowing it to engage in opaque structures of cooperation and sweeten policy agreements with financial assistance or trade-promotion deals. That China prefers to route money to the eurozone through a multilateral organization, and one it is suspicious about, shows how its confidence in the EU has declined and that it is reluctantly being forced into unknown territory for Chinese international economic policy.

### **Individual Limitations: Like Sisyphus and Icarus**

Beijing and Brussels seem content to wait for China's new leadership to take office before they attempt to deepen economic and commercial policy cooperation, but there is little reason to believe that the bilateral relationship will radically improve under changes in the Chinese capital. Individuals matter, but the problems in EU-China relations are rooted in divergent views on state, government, and international economic policy that are unlikely to diminish anytime soon. The economic crises are not the source of the differences, but they have accentuated the differences and tensions that were on display before Europe slipped into its age of crises.

The EU increasingly embodies Sisyphian traits in its economic and commercial policy posture towards China. Like Sisyphus, the mythological Greek king condemned to repeatedly roll a huge boulder to the top of a steep hill without success, the EU has tried time and time again to pressure China into opening more of its market to European exports by threatening to cut access to its own markets if Beijing does not comply. The rhetoric on climate change has been equally confrontational. But the EU is unconvincing when it is tasked to drum up protectionist threats: it has neither the treaty support nor the necessary policy tools to carry them through. The European Commission's attempt to introduce a European version of the U.S. Committee on Foreign Investment in the United States, which screens all incoming investments for national security threats, was outside of its mandate.

Likewise, the Commission's new initiative to close its procurement market for China and other countries outside the Government Procurement Agreement will hardly cajole them into opening up their procurement. Import penetration in Europe's public-sector demand is 7.5 percent, and China is estimated to represent as little as 1 percent of that amount. No doubt it would be beneficial for China to

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liberalize its public procurement, but Beijing is unlikely to acquiesce to Brussels' heavy-handed move for such small sales.

The broader effort of the Commission to act as arch-mercantilist in Europe goes against the essence of its role, which has always been to find a compromise between opposing camps in the EU membership. China, aware of these limitations, remains deaf to the EU's empty threats and the demands that accompany them.

The EU, for its part, is also aware of its limitations, but persists anyway. Sisyphus' perpetual struggle, said Albert Camus in the *Myth of Sisyphus*, has no chance of success but gives meaning to his life. It is an absurd meaning, but as long as he accepts the repetitious struggle, it gives happiness "enough to fill a man's heart." Many EU politicians and officials are satisfied with the current approach to China, despite the lack of progress. As Camus ended his essay: "One must imagine Sisyphus happy."

China, on the other hand, is more like Icarus, the Greek mythological figure who failed in his ambition to fly with his wax-and-feather wings because he got too close to the sun. Having acquired serious market power in the past ten years, China flaunts its fortunes in its relations with the EU (and others) without using it to accomplish anything concrete. Beijing's ambivalence to Europe is the result of what has been a more general strategy of keeping a low international profile, biding its time and avoiding relationships with other big economies that could force it into a position of using its economic power when it is profoundly uncertain about what it should be using that power for.

But inaction is not a policy that befits an economy of China's size. As with the United States in the 19<sup>th</sup> century,

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China has grown to become one of the giants of the world economy, but has not yet accepted that its newly acquired systemic importance requires a corresponding and attendant responsibility to the international system of exchange. China's foreign economic aspirations still remain an enigma. Does Beijing support the underlying principle of the post-war international economic policy, a gradual but constant move towards globalization based on a market economy and shared responsibility for a multilateral system of rules? Or does it want to rewrite this principle?

## Diverging Views on Global Political Economy

For many in Europe, the crisis has been a litmus test of China's loyalty to the existing international economic system. The EU was created by the same post-war trends of economic cooperation that midwived multilateral economic institutions, and it has benefited tremendously from their existence. It has been neither capable nor willing to economically underwrite those institutions, leaving that task to the United States. Europe has not been guided by the spirit of "visionary generosity" that once informed United States' policy towards global economic policy. European countries were often unwilling to accept new trade or monetary deals that would have an unequal distribution of gains, even if the net outcome was of benefit to Europe. There has been partial change in Europe in its outlook. Yet there is a vexing belief in Europe that China has made gains from the global economic system disproportionate to its contributions. For many officials in Europe, the EU-China High Level Trade and Economic Dialogue was established on the premise that China would start returning on some of those gains. When Beijing has made clear that it is not prepared to dance to that tune, it has only served to irritate Europe further.

China is not innocent in all of this. Its stalled economic reform agenda and unwillingness to accept a leadership role corresponding to its economic size are now major sources of friction in the global economy. Beijing's ham-fisted diplomacy towards Brussels has not made them many friends. It has repeatedly tried to bypass Brussels in its negotiations with Europe, preferring instead to work through member states more susceptible to Beijing's *faiblesse* for trade-promotion deals and avoidance of hard policy negotiation. It has been far more serious in the Strategic and Economic Dialogue with the United States, repeatedly agreeing to

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improved market access, than in its equivalent dialogue with the EU.

Beijing's officials often excuse themselves by claiming that they do not understand how the EU works. It is an excuse that could be believed. Confusion about how the EU works has also increased as a consequence of Europe's response to the sovereign debt crises, and the further entrenchment of the EU's post-modern political personality. While other regions operate on the basis of the classic, Westphalian, modernist view of nation, state, and government power, the EU has been in the rival business of substituting modernist government with post-modern governance. Governments in Europe have deliberately and willingly weakened their own autonomous authority and power even when new pan-European structures of power have proven inadequate. National economic interests are now channeled through Brussels and arduous negotiations between EU member states. Chinese politicians, who are used to hard-power realities and schooled in a one-nation mentality, find working with a centralized Europe both difficult and threatening. In Beijing's view, the EU is unpredictable.

While the EU's complicated structures might be confusing, Beijing's bypassing of Brussels is at least partly deliberate. Beijing prefers to deal directly with big European capitals, even on those issues where policy has been clearly centralized in Brussels, because it has more leverage over individual governments than over the Union as a whole. There are short-term gains for China from a divisional approach to Europe. A divided Europe will put less pressure on political change and economic reform in China. But a fractured EU will have negative long-term consequences for China and its economic interests. Beijing has taken its big-power strategy too far for EU-China policy relations not to be weakened.

Icarus has a lesson for China. Daedaleus, according to the Roman poet Ovid, tells Icarus to keep to the middle range and don't fly too high. But Icarus, increasingly hubristic, wonders "what limits there are to his father's invention. He flaps his wings and rises higher – but nothing bad happens." Those watching Icarus from earth assume the winged creature is a god. What Icarus cannot see is that the wax melts. Soon he plunges into the sea.

China has made a bad bet in assuming that its interests are better served by weak rather than effective centralized

policies and institutions in Europe. The divisional strategy may work for yet another few years. But before long China will learn the same lesson as others in the past 60 years of global economic policy: a fractured Europe will be less reliable and predictable, and occupied by intra-continental squabbles rather than designing rules and policies for global commerce.

## About the Author

Fredrik Erixon is the director and co-founder of the European Centre for International Political Economy (ECIPE), a world economy think tank based in Brussels.

## About the Stockholm China Forum

This is part of a series of papers informing and informed by discussions at the Stockholm China Forum. The Stockholm China Forum is an initiative of the German Marshall Fund, the Swedish Ministry for Foreign Affairs and the Riksbankens Jubileumsfond. It brings together policymakers, intellectuals, journalists, and businesspeople from Europe, the United States, and Asia on a biannual basis for an ongoing and systematic dialogue to assess the impact of China's rise and its implications for European and U.S. foreign, economic, and security policy.

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