Li Keqiang and Angela Merkel.
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Bracing for China's Systemic Competition

A View from Germany

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The attitude of the German business community vis-à-vis China is increasingly torn between short-term profits and long-term strategic interests. While China has been Germany's largest trading partner since 2016, with commercial ties registering a total of 186.6 billion euros in 2017 (Nienaber 2018), a forthcoming strategy paper of the Federation of German Industries (BDI)—Germany's most influential industry association—is urging German companies to reduce their dependence on the Chinese market (Barkin 2018a).

The Paper highlights the long-term challenge posed by China's state-driven economic model, as part of which state-subsidised companies take advantage of the openness of Germany's economy, easily outcompeting German businesses playing by market rules. 'We are facing a systemic competition between our open markets approach and China's state-driven economic model,' a draft of the upcoming Report reads, calling for a discussion across politics, society, and industry.

BDI's newfound position comes closer to that of some German political elites, who have been warning against the systemic challenge that China's authoritarian system poses to liberal democracy, not only in economic, but also in political terms. It also goes hand in hand with the EU's and other larger member states' increasingly assertive tone in their requests for access to the Chinese market, in line with the Chinese leadership's promises for greater openness.

One day after the BDI Report—which has been in the pipeline since spring 2018—was publicised by Reuters, the EU listed rather specific expectations for China's future opening up (EEAS 2018). These came ahead of the China International Import Exhibition, an event that supposedly showcases China's commitment to market opening. The EU's requests addressed various examples of China's discriminatory behaviour against foreign companies and unfair practices, from market access barriers created by intrusive cyber-security regulations, to subsidies under the industrial policy Made in China 2025. These requests were also echoed by the French and German ambassadors to Beijing in a joint op-ed for *Caixin* (Ripert, von Goetze 2018).

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Overall, this concerted effort and toughening up of European political and business elites signals an intention to move away from the quiet approach taken thus far, which has not produced the results that were hoped for. In fact, the idea that an accommodating attitude would have gently pushed China to follow through on its free trade rhetoric and eventually transform itself into a market economy has turned out to be mere wishful thinking.

The wait and see approach of German economic and political actors, just like that of those in most Western advanced economies, started with the beginning of China's reform and opening-up four decades ago, in 1978. Since then, various moments in history have nurtured the hope that, eventually, China would turn into a fully-fledged market economy.

China's accession to the World Trade Organization (WTO) in 2001 was interpreted as a first step in the direction of economic liberalisation. Western countries also hoped that economic reforms would be followed by political opening. Notably, the 2002 East Asia Concept of the German Federal Foreign Office, drafted only one year after China's entry into the WTO, stated Germany's support for 'China's transition to an open society based upon the rule of law and human rights' (Auswärtiges Amt 2002).

Promises to loosen control measures made by Chinese officials in Beijing's bid to host the 2008 Olympics, along with the 2013 Third Plenum of the Chinese Communist Party (CCP), pledging a stronger role for market forces into China's economy, further raised expectations. More recently, Xi's Davos speech in January 2017, which promoted China as a champion of free trade and globalisation amidst US protectionism under Trump, was also welcomed with hope by western political and economic elites.

The Nineteenth Party Congress of October 2017, and then the National People's Congress in March 2018, can be considered watershed moments in prompting German business lobbyists to devise alternative strategies to limit dependency on the Chinese market.

Up until October 2017, many thought that reforms might materialise. By contrast, the Nineteenth Party Congress showed the CCP's confidence in its state-driven political and economic system, and even its exportability to other countries. This set out more clearly the Chinese central leadership's intention to strengthen its grip on power, including through further control over the economy. With the abolition of the presidential term limits in March 2018, the consolidation of authoritarian rule in China has become even more evident.

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Former German Foreign Minister Sigmar Gabriel.
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As Xi Jinping committed to put China back at the 'centre of the world stage', Beijing's increased assertiveness and control started to show. This also hit German businesses directly. In November 2017, the CCP's announcement that it would start installing Party cells into foreign firms operating in China led German industry representatives to warn that German firms might reduce their activities in the Chinese market (He 2017). To make things worse, in February 2018 the CCP asked for an apology from Daimler, leveraging the feelings of 'the Chinese people': the multinational had quoted the Dalai Lama in a Mercedes-Benz ad on Instagram, a social media platform that is censored in China and thus cannot be accessed by users in the Mainland (Wee 2018).

These cases added up to already-existing issues in commercial ties, such as China's intrusive cybersecurity legislation, which puts foreign enterprises operating in China at a disadvantage.

In the meantime, China's rare openings have remained selective, meant to appease European criticism about China's reluctance to follow through on its promises to open up. Especially amid the ongoing US-China trade spat, China has been trying show goodwill as it looks for European partners to counter the US. Deals signed with German chemical giant BASF and carmaker BMW in July 2018 can be seen in this light (Croft 2018). Rather than an indication of China's opening, they are the result of bespoke backroom deals.

With its updated strategy on China, BDI is now adjusting to a reality in which it has become evident that China has no serious intention to open up. While the draft Report clarifies that German businesses have no interest to fence China in, its words echo the rhetoric of some German political leaders who have been warning against the challenge that China's state-driven political and economic system poses to liberal democracy.

For example, speaking at the Munich Security Conference (MSC) in February 2018, former German Foreign Minister Sigmar Gabriel stated that: 'China is developing a comprehensive systemic alternative to the Western model that, in contrast to our own, is not founded on freedom, democracy and individual human rights' (Auswärtiges Amt 2018). The same view has been bolstered by the President of the Bundestag, Wolfgang Schäuble, and by senior Members of Parliament (Braun 2018).

And while the Federal Foreign Office still aims to strengthen the rule of law and improve the human rights situation in China, now it has also started to brainstorm ways of dealing with an increasingly authoritarian partner. This will mean adjusting strategies for China's domestic situation, but also for third countries, where Beijing is a competitor that can export its repressive approaches.

On China's Belt and Road Initiative (BRI), too, the rhetoric of German business and political elites seems to be increasingly converging. Still, BDI has to balance the different interests of its members. While a general interest of larger German companies to seek selective, profitable opportunities under the BRI label persists, German SMEs, the backbone of the country's economy, have so far been excluded from BRI. Others openly endorse the initiative, like business conglomerate Siemens, which dedicates a whole Beijing office to BRI.

In its Report, BDI describes BRI as an attempt by Beijing to establish geopolitical influence and shape third markets according to its own interests. In response, it suggests carrying out a 'diplomatic offensive' from Berlin and Brussels, to reach countries in Eastern Europe, Central Asia, Southeast Asia, and Africa.

This description of BRI resonates with what Gabriel said at the MSC, when he argued that 'the initiative for a new Silk Road ... stands for an attempt to establish a comprehensive system to shape the world according to China's interests.'

The EU itself has come up with its own Euro-Asian connectivity strategy, announced in September 2018 (EU 2018). While it is open to cooperation with China, it also represents a challenge to the Chinese government's approach to pursue infrastructure diplomacy, with Europe's own commitment to standards and sustainability.

However, if Europe wants to show that it is serious about promoting a type of connectivity that is sustainable, comprehensive, and rules-based, projecting confidence and unity of purpose will be key. Ideally, European member states would follow suit. For example, when they are pressured by China to sign a BRI MoU, they should respond by setting their own terms for any form of cooperation on BRI. If anything, they should use China's appetite for high-level endorsement of the initiative ahead of the second Belt and Road Summit, planned for April 2019, as leverage to advance their own interests.

Continuing to push China more assertively to seek common ground with European interests will also help to avoid the escalation of tensions into a trade dispute, like the one currently ongoing between China and the US. To be sure, this is currently unlikely, in Germany and Europe. BDI itself only recommends limiting dependence on the Chinese market, being fully aware that China remains an important trade partner. Nevertheless, problems should be tackled before tensions arise.

In the United States, too, contentious issues in trade relations remained long unaddressed in the hopes that a quiet approach would be rewarded by China with market access. Ultimately, continuous disappointment led to the current escalation of a

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trade war, in which hawks like Robert Lighthizer and Peter Navarro, previously silenced by a more China-friendly business community, seized the opportunity to take over.

Moreover, European business and political leaders should also keep using strategic momentum created by the US-China trade dispute, and China's need to 'make concessions' in a sign of goodwill, to woo European partners. They should also take the level of coordination reached through negotiations for an EU investment screening mechanism as the starting point for a healthy practice of intra-European exchanges on other topical issues in relations with Beijing.

Jointly debating risks and opportunities associated with China's involvement in Europe's 5G infrastructure could be one. Indeed, a new concern currently being debated in Germany is China's National Intelligence Law, which forces all Chinese organisations and citizens to cooperate in the country's intelligence work. Chinese telecoms giant Huawei, which is bidding to build 5G infrastructure in Germany and Europe, would operate under this law (Barkin 2018b).

Looking ahead, a stronger posture in the promotion of European values and interests vis-à-vis China should be upheld beyond economic issues and expanded to other problematic aspects of Europe's relationship with China, such as extensive human rights violations and concerning developments in Xinjiang. So far, the desire for cosy business ties with China has largely muted strong, public rhetoric on 'uncomfortable' topics that Beijing is unwilling to discuss. Now, a more assertive stance on economic issues could lay the groundwork for a more confident position on other values-related issues in the relations between Europe and China. ■